BANKING ACT OF 1935

HEARINGS

BEFORE THE

COMMITTEE ON BANKING AND CURRENCY
HOUSE OF REPRESENTATIVES

SEVENTY-FOURTH CONGRESS

FIRST SESSION

ON

H. R. 5357

A BILL TO PROVIDE FOR THE SOUND, EFFECTIVE, AND UNINTERRUPTED OPERATION OF THE BANKING SYSTEM, AND FOR OTHER PURPOSES

FEBRUARY 21, 22, 26, 27, 28, MARCH 1, 4, 5, 6, 11, 12, 13, 14, 15, 18, 19, 20, 21, 22, 25, 26, 27, 28, APRIL 2, 8, 1935

CORRECTED PRINT

UNITED STATES
GOVERNMENT PRINTING OFFICE
127297 WASHINGTON : 1935

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BANKING ACT OF 1935

THURSDAY, FEBRUARY 21, 1935

HOUSE OF REPRESENTATIVES,
COMMITTEE ON BANKING AND CURRENCY,
Washington, D. C.

The committee met at 10:30 a. m., Hon. Henry B. Steagall (chairman) presiding.

The CHAIRMAN. Gentlemen, the committee will come to order, please.

I have asked Mr. Crowley, of the Federal Deposit Insurance Corporation, to come before us this morning and discuss H. R. 5357. I assume that he desires to address his remarks mainly to the provisions of title I of the bill, which relates to the Federal Deposit Insurance Corporation.

I am going to desist from making any preliminary statement myself at this time, but if I have the opportunity, I should like to incorporate in the hearings a short preliminary statement of my own.

In deference to a suggestion which Mr. Crowley has made to me, and what I think might be in the interest of time and orderly procedure, I am going to suggest to the committee that they permit Mr. Crowley to make his statement and complete his discussion in a general way before committeemen interrogate him.

You may proceed, Mr. Crowley, if you will.

STATEMENT OF LEO T. CROWLEY, CHAIRMAN OF THE BOARD, FEDERAL DEPOSIT INSURANCE CORPORATION

Mr. CROWLEY. Gentlemen, we have prepared a digest of this bill, together with our recommendations. If it is agreeable to the committee we will pass to each one of you a copy of our report, in order that you may follow the report with me. If you will be kind enough to let us follow through with it and answer your qestions afterward, we would like to do that. We have a number of charts that we would like to present to you. Is that agreeable to you, Mr. Steagall?

The CHAIRMAN. Yes; that will be perfectly all right.

Mr. CROWLEY. Gentlemen, last year I appeared before you and recommended that the provisions of the so-called "permanent insurance plan" be suspended for another year, and that the temporary insurance fund be continued to July 1, 1935. At that time it was stated that we need additional experience before the permanent plan went into effect. We also suggested that, through the administration of the temporary fund, we might gain some knowledge which would indicate desirable changes in the permanent plan. You have asked me to appear before you today to discuss with you the results of our 13 months' experience and study and to explain the reasons behind the proposals which you have before you, and which comprise title I of the Banking Act of 1935.

With your permission, I would like to outline to you in detail the reasons which have motivated our suggestions for changes in the permanent insurance plan. The charts and tables give a vivid picture of the commercial banking structure of the United States. These data cover all insured and noninsured banks, arranged according to total deposit liability size groupings.

They do not include mutual savings banks or private banks.

Ninety percent by number of all of the licensed commercial banks in the United States have been admitted to the insurance fund. Over 98 percent of the total deposits in commercial banks and trust companies in the United States are in banks, the deposits of which are insured. On October 1, 1934, there were only about 1,100 licensed commercial banks, with deposits of slightly more than $500,000,000, which were not insured, while insured commercial banks numbered more than 14,000 on that date, and their deposits amounted to some $36,000,000,000. Mutual savings banks have been excluded from these figures. There are 68 of the 576 mutual savings banks in the fund for mutuals.

We have in our fund 1,928 banks with deposits of $100,000 and under; of banks with deposits of $100,000 to $250,000 we have 3,929; with deposits of $250,000 to $500,000 we have 3,278; with deposits of $500,000 to $750,000, we have 1,531; with deposits of $750,000 to $1,000,000 we have 970; with deposits of $1,000,000 to $2,000,000 we have 1,664; with deposits of $2,000,000 to $5,000,000 we have 1,076; with deposits of $5,000,000 to $50,000,000 we have 647; with deposits of $50,000,000 and over we have 96 banks in our fund.

The banks are broken down in our chart into national banks, State banks, and State member banks, and the insured and uninsured nonmember banks.

For instance, out of 1,091 banks that are outside of the fund, 426 of those have deposits of $100,000 and under, 349 have deposits of $100,000 to $250,000, 169 have deposits of $250,000 to $500,000, 54 have deposits of $500,000 to $750,000, 27 have deposits of $750,000 to $1,000,000, 34 have deposits of $2,000,000 to $5,000,000, 16 have deposits of $5,000,000 to $50,000,000, and 16 banks have deposits of $50,000,000 and over, which make a total of 1,091 banks.

The CHAIRMAN. Does your statement disclose the total of the deposits in each of these groups?

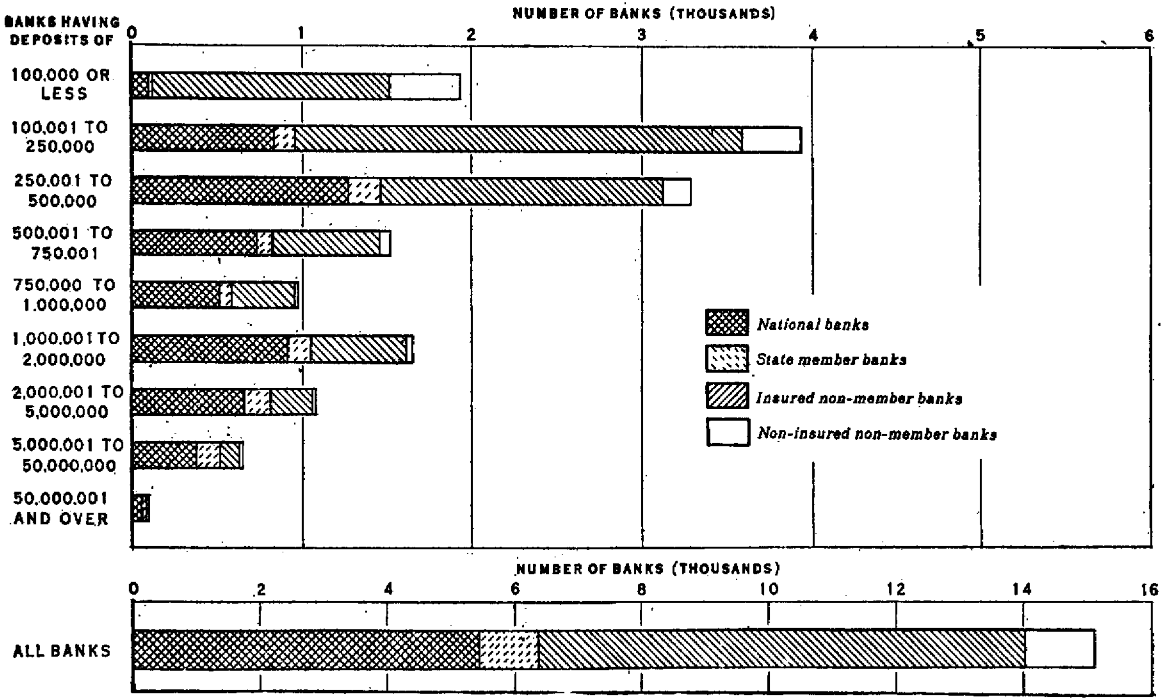
Mr. CROWLEY. Yes, sir.

The next chart that you have there shows that the banks with deposits of $100,000 and under have a total deposit liability of $123,-831,000. In other words, 1,900 banks have deposits of $123,831,000.

The banks with deposits of $100,000 to $250,000 have total deposits of $664,493,000, and so on down. The $50,000,000 banks, and over, have deposits of $18,942,000,000.

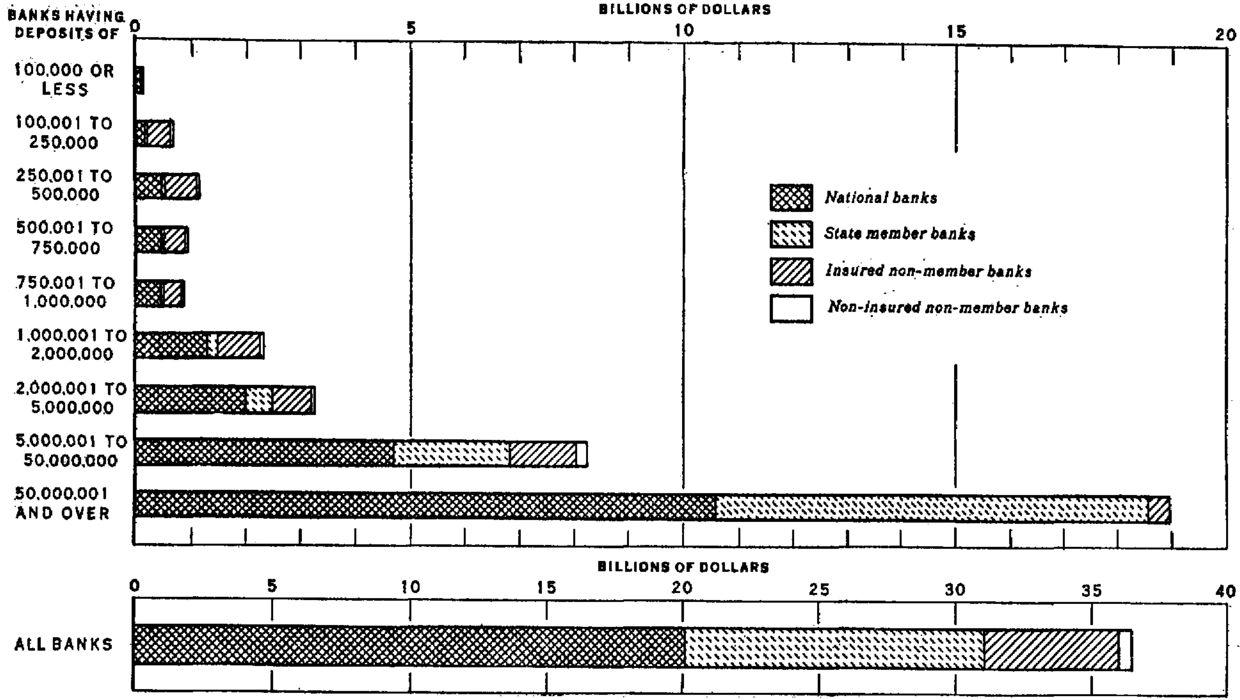
(The charts and tables referred to are as follows:)

NUMBER OF INSURED AND UNINSURED COMMERCIAL BANKS, OCT. 1, 1934 CLASSIFIED BY SIZE OF BANKS



FEDERAL DEPOSIT INSURANCE CORPORATION — DIVISION OF RESEARCH AND STATISTICS

DEPOSITS IN INSURED AND UNINSURED COMMERCIAL BANKS, OCT. 1, 1934, CLASSIFIED BY SIZE OF BANKS



FEDERAL DEPOSIT INSURANCE CORPORATION

DIVISION OF RESEARCH AND STATISTICS

Insured and uninsured commercial banks classified by size of bank, Oct. 1, 1934

	All banks	National banks	State member banks	Insured nonmember banks	Uninsured nonmember banks
Banks having deposits of—					
$100,000 and under	1,928	94	22	1,386	426
$100,001 to $250,000	3,929	834	119	2,627	349
$250,001 to $500,000	3,278	1,261	186	1,662	169
$500,001 to $750,000	1,531	741	97	639	54
$750,001 to $1,000,000	970	506	67	370	27
$1,000,001 to $2,000,000	1,664	923	142	565	34
$2,000,001 to $5,000,000	1,076	659	153	248	16
$5,000,001 to $50,000,000	647	380	141	110	16
$50,000,001 and over	96	52	39	5	----------
Total, all groups	[1] 15,119	5,450	966	7,612	1,091

[1] Exclusive of 71 insured banks not reporting statistics and 31 uninsured banks for which no deposit figures were available.

Deposits in insured and uninsured commercial banks classified by size of bank, Oct. 1, 1934

[000's omitted]

	All banks	National banks [1]	State member banks [1]	Insured nonmember banks [1]	Uninsured nonmember banks [2]
Banks having deposits of:					
$100,000 and under	$123,831	$7,265	$1,700	$90,750	$24,116
$100,000 to $250,000	664,493	152,705	21,304	435,381	55,103
$250,001 to $300,000	1,167,228	460,706	68,180	579,700	58,642
$500,001 to $750,000	936,016	455,702	58,545	388,983	32,786
$750,001 to $1,000,000	836,608	437,095	57,331	318,940	23,242
$1,000,001 to $2,000,000	2,324,922	1,300,832	199,540	778,427	46,123
$2,000,001 to $5,000,000	3,242,721	1,982,864	487,542	723,051	49,264
$5,000,001 to $50,000,000	8,250,016	4,691,139	2,118,575	1,216,797	223,505
$50,000,001 and over	18,942,184	10,582,628	7,951,575	407,981	----------
Total, all groups	[3] 36,488,019	20,070,936	10,964,292	4,940,010	512,781

[1] Total deposits reported to the corporation on Oct. 1, 1934 differ in some respects from those shown on published statements.
[2] As reported in Rand-McNally Bankers' Directory for July 1934.
[3] Exclusive of deposits of 71 insured banks not reporting statistics and 31 uninsured banks for which no deposit figures were available.

Mr. CROWLEY. To arrive at a practical basis for estimating the amount of funds necessary to cover the insurance liability of the Corporation, our first consideration has been the volume of losses which depositors have borne during the past.

From July 1, 1864, the beginning of the national banking system, to June 30, 1934, about 16 thousand commercial banks, which include national banks, State banks, loan and trust companies, stock savings banks, and private banks for which there are data in the reports of the Comptroller of the Currency, with deposits of nearly 9 billion dollars, are known to have suspended operations. Losses to depositors in these banks are estimated at 3 billion dollars over and above all recoveries.

The estimates of losses to depositors in suspended commercial banks are based upon available data which clearly minimize the facts. The figures for national banks are fairly complete and reliable, and are taken from reports of the Comptroller of the Currency. The figures for other commercial banks, however, are incomplete, particularly for the period prior to 1920. Since all failures have not been recorded, bank depositors have suffered losses which have not been recorded. For example, many records of voluntary liquidation by banks ignore the fact that depositors were not paid in full. Then, again, bank reorganizations, in late years, have been based upon the waiving of depositors' claims, while in other cases depositors have voluntarily reduced their claims or made contributions to capital as a means of absorbing losses.

Mr. KOPPLEMANN. Mr. Crowley, do you mean to say that even today there are banks that fail without being reported, private banks or any kind of a bank?

Mr. CROWLEY. What we are talking about is during the last few years.

Mr. KOPPLEMANN. I know, but I wondered whether that situation still exists.

Mr. CROWLEY. I think there are some States in which banks might fail, and we cannot get the information from them.

Mr. KOPPLEMANN. There are still?

Mr. CROWLEY. Yes.

The CHAIRMAN. Inasmuch as that question has been asked, what information have you to support the statement that there have been voluntary liquidations of State institutions, in which the depositors are not paid in full? How do you get information like that?

Mr. FOX. Mr. Chairman, the source of the information is the Federal Reserve Board. They make contacts with the State authorities through their agents in the 12 Federal Reserve districts. If the State authorities inform the agents, we get the information. However, if the State authorities have no control over the banks, as is the case with some private banks, we would not get the information.

The CHAIRMAN. Would it not follow as a matter of course that when a bank became insolvent, to the extent of wiping out its capital structure, and leaving it with its depositors unprotected, there would be a liquidation in the regular way of such an institution?

Mr. CROWLEY. What we are trying to bring out, Mr. Chairman, is that there have been a lot of insolvent banks that have gone to their depositors and made private deals with them, whereby they wrote down their deposits liability in some instances as high as 40, 50, or 60 percent, and when they waived a portion of those deposits, the portion that they waived was used for capital purposes.

Mr. CROSS. Did you get that through the Internal Revenue Department?

Mr. CROWLEY. No; there would be no reason for their reporting to the Internal Revenue Department.

The CHAIRMAN. I was of the opinion that there would be no report of that kind to the Commissioner.

Mr. CROWLEY. There would be no way to have it recorded. The only place you could get it would be through the local bank commissioner, and a lot of them do not keep complete records.

Mr. HANCOCK. What is your best estimate of the losses which have occurred that are not accounted for?

Mr. CROWLEY. Have you any idea what that might amount to, Mr. Fox?

Mr. FOX. No, sir.

Mr. CROWLEY. What we have been trying to do is to find out from the various State departments how much their depositors have lost through waivers, and it has been an almost impossible thing to determine, because they have kept no records of it, but we do know it has been a very substantial sum.

Mr. Reilly. In the case of Wisconsin have you a record?

Mr. Crowley. We have not been able to get that as yet.

Mr. Fox. We are getting a record for the past 4 years. We already have records from 18 States.

Mr. Goldsborough. Have you a record from Maryland?

Mr. Fox. Yes, sir.

The Chairman. Before you leave that, do you attempt to include these estimated and unrecorded losses as a part of the total embraced in your figures?

Mr. Crowley. No. As I understand it, Mr. Chairman, the $3,000,000,000 of loss has been determined from the actual liquidations; is that correct, Mr. Fox?

Mr. Fox. Yes; from the actual figures.

The Chairman. Then there are no figures based on that, so it is not so material.

Mr. Crowley. The charts which I will later file show, by years from 1864 to 1934, the percentage of national and other commercial banks suspending and the ratio of deposits in suspended banks to deposits in active banks. The ratio of deposits in suspended banks to total deposits in all active banks is smaller for national than for other commercial institutions.

In other words, the loss from 1864 to 1934 was considerably less in the national system than it was in the State system.

Our estimates indicate that about 1 billion dollars of the 9 billion dollars which was on deposit in commercial banks that failed during the 70-year period were secured by pledge of collateral or otherwise. Of the remainder, some 6 billion dollars were in accounts of less than $5,000 or constituted the first $5,000 of large accounts. In other words, 6 billion dollars were within the $5,000 limit. Two billion dollars represents the volume of these deposits which were in accounts with balances above $5,000. The estimates of the amount of funds representing balances in excess of $5,000 were made on the basis of figures showing deposits classified by size of accounts in national banks in 1918, in member banks of the Federal Reserve System as of May 13, 1933, and in all insured commercial banks as of October 1, 1934.

For every $100 of deposits in the entire commercial banking system, about 32 cents a year was lost. Of this figure, it is estimated that 24 cents represents losses to depositors with balances not in excess of $5,000, while the remaining 8 cents represents losses to depositors having balances in excess of $5,000. For every $100 of deposits in the national banking system, 21 cents per year was lost as against 42 cents per $100 per year in the State system. The following table summarizes the estimates of losses to depositors in suspended national and other commercial banks during the 70 years ending June 30, 1934.

(The table referred to is as follows:)

Losses to depositors in suspended commercial banks July 1, 1864–June 30, 1934

	All commercial banks	National banks	Other commercial banks
Deposits in suspended banks (millions of dollars)	$8,778.00	$2,715.00	$6,063.00
Secured	1,033.00	184.00	849.00
Unsecured under $5,000	5,762.00	1,675.00	4,087.00
Unsecured over $5,000	1,983.00	856.00	1,127.00
Estimated losses (millions of dollars)	3,113.00	1,015.00	2,098.00
Secured deposits	(1)	(1)	(1)
Unsecured deposits under $5,000	2,301.00	667.00	1,634.00
Unsecured deposits over $5,000	812.00	348.00	464.00
Average loss per year for each $100 of deposits in active banks	.32	.21	.42
Unsecured deposits under $5,000	.24	.14	.33
Unsecured deposits over $5,000	.08	.07	.09

[1] Negligible.

Mr. CROWLEY. Losses to depositors have been most severe during the periods of business depression. Two-thirds of the losses during this entire 70-year period resulted from bank suspensions occurring during the 4 years ending June 30, 1934. In other words, two-thirds of the losses in the banking system in this country took place from 1929 to June 30, 1934. For these 4 years losses to depositors are estimated at $1.32 per year for each $100 of deposits in the commercial banking system. Comparable losses during the depression of the 1870's amounted to 35 cents, and during the depression of the 1890's amounted to 23 cents. The figures for the early periods understate the losses, but it is apparent that the losses in these earlier periods were not as great in proportion to total deposits as during the past 4 years. The data are summarized on the following tables. The first shows the losses in commercial banks which suspended and did not reopen during the three depression periods; the second compares losses during the 14 years included by the three critical periods, with the other 56 years since 1864.

(The tables referred to are as follows:)

Losses to depositors in commercial banks suspending during periods of crisis, banks which did not reopen

[Federal Deposit Insurance Corporation, Division of Research and Statistics]

	All commercial banks [1]		
	1873–78	1892–97	1931–34
Deposits in suspended banks (millions of dollars)	$85.00	$134.00	$5,356.00
Secured	10.00	13.00	637.00
Unsecured under $5,000	66.00	103.00	3,256.00
Unsecured over $5,000	9.00	18.00	1,473.00
Estimated losses in deposits (millions of dollars)	26.00	43.00	2,142.00
Secured deposits	(2)	(2)	(2)
Unsecured deposits under $5,000	23.00	36.00	1,478.00
Unsecured deposits over $5,000	3.00	7.00	664.00
Average loss per year for each $100 of deposits in active banks	.35	.23	[3] 1.28
Unsecured deposits under $5,000	.31	.19	.89
Unsecured deposits over $5,000	.04	.04	.40

[1] Periods beginning on July 1 and ending on June 30 of the years specified.
[2] Negligible.
[3] If losses of banks which subsequently reopened are included, the average loss per year for each $100 of deposits in active banks is raised to $1.32.

Losses to depositors in suspended banks, July 1, 1864–June 30, 1934, 3 crisis periods contrasted with the remaining years, all commercial banks

[Federal Deposit Insurance Corporation, Division of Research and Statistics]

	70 years, 1864–1934	14 years during 3 crisis periods [1]	Remaining 56 years
Deposits in suspended banks (millions of dollars)	$8,778	$6,084	$2,694
Secured	1,033	716	317
Unsecured under $5,000	5,762	3,738	2,024
Unsecured over $5,000	1,983	1,630	353
Estimated losses (millions of dollars)	3,113	2,269	844
Unsecured deposits under $5,000	2,301	1,578	723
Unsecured deposits over $5,000	812	691	121
Average loss per year for each $100 of deposits in active banks	.32	1.17	.11
Unsecured deposits under $5,000	.24	.82	.09
Unsecured deposits over $5,000	.08	.36	.02

[1] Includes figures for banks suspending during period July 1, 1930, to Mar. 15, 1933, which subsequently reopened.

Mr. CROWLEY. The experience of the past 70 years indicates that to repay losses suffered by all depositors in our suspended commercial banks, an assessment of 33 cents per $100 of total deposits, or one-third of 1 percent of total deposits in all open commercial banks, would have been necessary. Excluding the losses incurred during the three depression periods—1873–78, 1892–97, and 1931–34—and confining ourselves to losses occurring during the balance of the 70 years, an assessment of one-eighth of 1 percent would have been necessary.

In the past, the number, timing, and geographic concentrations of bank suspensions have been chiefly due to fundamental weaknesses in banking structure and the course of economic events. Suspension of individual banks within the areas affected has reflected, in the main, the quality of bank management. In the future, the magnitude of losses which will result from bank failures will also depend upon the trend of economic events, the changes which may occur in the structure and functions of the commercial banking system, the caliber of the individual bank management, the extent to which the system is reinsured against defalcations, and the quality of the supervision exercised over these banking institutions.

Of course, the future trend of economic events cannot be forecast.

Changing tendencies are now apparent in the structure and functions of commercial banking. On the one hand, the drastic reduction in the number of banks during the past 14 years has greatly relieved the overbanked condition in many communities. On the other hand, new financial agencies, serving specialized needs, have been created, and will compete, to some extent, with commercial banks. The types of credit which may be extended by commercial banks may be subject to varying degrees of risk.

The extent to which the caliber of bank management will improve in the future, over what it has been in the past, cannot be estimated. While it is hoped that a better quality of personnel will develop, it must be recognized that there will continue to be poorly managed banks and that such institutions will eventually succumb. We cannot foretell the extent to which the existence of deposit insurance will influence bank management.

To establish a fair rate of assessment which the banks shall pay for Federal deposit insurance, the hopeful expectations of the future must be tempered by a consideration of the realities of the past. Let me repeat that a premium at the rate of one-third of 1 percent of total deposits would have been necessary to cover all losses to depositors during the past 70 years. A premium at the rate of one-eighth of 1 percent would have covered depositors' losses in all years except those of severe depression.

We are concerned next with the basis of assessment and with the ability of the banks to pay the required amount.

The existing permanent insurance law provides that all insured banks may become liable for an uncertain number of successive assessments. It is not sound deliberately to subject an operating business to an unpredictable liability. The maximum rate and number of assessments should be fixed so that an insured bank may know in advance its potential liability to the Corporation. An annual premium of a known maximum amount constitutes a sound basis for insurance revenue, as it provides a specific payment to cover a clearly defined risk for a definite period of time.

We also believe that payments made by insured banks should be in the form of premiums, rather than through the purchase of stock. As in the case of other insurance companies, receipts from premiums should be added to the reserve funds of the Corporation. Such reserve founds should not be considered an earning asset of the insured banks. The interest received by the Corporation from the investment of reserve funds should not be made on the basis of dividend payments.

It is recommended that assessments be based upon total deposits in insured banks, regardless of whether or not the insurance is limited to $5,000 per depositor. To base assessments solely on the first $5,000 of each depositor's account places an undue burden upon the small banks, since most of the accounts of these institutions are less than that amount. It does not necessarily follow, however, that the greatest risk to the Corporation lies in these institutions. On the contrary, it has been demonstrated frequently in recent years that the consequences of the failure of a large bank may be more disastrous than the failure of a number of small institutions. The closing of a large bank often brings in its wake the failure of correspondent institutions.

The benefits of deposit insurance are not limited solely to the protection of the individual depositor. The entire banking structure of the country is so intimately interwoven that a disturbance in any part of the system may cause repercussions of far-reaching proportions. The benefits which will accrue to the large city banks because of great stability in the country banks are real and tangible.

All banks, large and small, should be required to support the insurance system. Banking is no longer merely a private business proposition. It involves great social consequences. The stability of the banking system affects the economic prosperity of the country. The raising of a sufficient revenue, solely through the levying of premiums against the deposits of those receiving direct insurance benefits will not be a fair distribution of the burden.

Our analysis of the ability of the banks to pay assessments is confined solely to the national banks since adequate data for other institutions are not available. The figures for earnings, profits, and dividends of national banks since 1870, as published by the Comptroller of the Currency, have been used. If the operating result of national banks can be taken as criteria, the banking system as a whole could have paid its losses during the past 70 years without impairing its stability or the payment of reasonable dividends to stockholders.

Operating profits of the banks have been below normal during recent years. The condition is reflected not only in reductions in gross earnings but also in unusually heavy write-offs made necessary by shrinkage in values. As we come out of the depression, losses on existing credits will appear. Banks should charge off these losses currently as they develop. They should not allow them to accumulate as was frequently the case prior to the banking holiday of 1933. These losses may absorb a considerable part of the banks' earnings over the next few years. To ask the banks to bear the entire cost of insurance at a rate comparable to the experience of losses over the past 70 years would subject them to a heavy burden at the present time.

It is probably true that after the period of adjustment has been completed, the banks' earnings will enable them to pay an assessment adequate to cover losses at the rate shown for the past 70 years. To ask them to do so, however, without making some effort to reduce the burden of losses seems to me to be unfair to the banks and to the public, which must ultimately bear the cost. This factor prompts us to ask for specific powers which will reduce these losses so that the insurance plan can be operated upon a reasonable assessment basis.

The following table compares annual averages of earnings, expenses, losses, and profits of the national banks for the years 1918 to 1930 with similar figures for the 6 months' period ending December 31, 1933. If charge-offs during the last half of 1933 had been no heavier than the average for the years 1918 to 1930, the national banks would have shown net profits of more than $1 for each $100 of total deposits, or more than $7 for each $100 of invested capital.

(The table referred to is as follows:)

Earnings, expenses, losses, and profits of national banks averages for 1918–30, compared with 6 months ending Dec. 31, 1933

Items	Amounts per year per $100 of total deposits		
	Average 1918 to 1930	6 months ending Dec. 31, 1933 [1]	Change
Gross earnings plus recoveries	$6.46	$5.18	−$1.28
Interest paid	1.92	1.05	−.87
Other expenses	2.44	2.18	−.26
Net earnings plus recoveries	2.10	1.95	−.15
Losses on loans and investments	.81	3.76	−2.95
Net additions to profits	1.29	[2]1.81	−3.10

[1] The figures for the 6 months have been adjusted to show a rate per year, rather than for 6 months only.
[2] Deficit.

Mr. CROWLEY. It will be noted that the expenses of operating national banks were considerably lower in 1933 than during the period 1918 to 1930. Most of this reduction was due to a decline in the average rate of interest paid on deposits. About two-thirds of this reduction in interest occurred before the Banking Act of 1933 became effective and reflected the general decline in money rates. One-third of the reduction took place after the passage of the act, reflecting almost entirely the prohibition against the payment of interest on demand deposits. The savings in interest on account of this change in the law amounted to 26 cents for each $100 of total deposits, or more than the premium necessary to cover losses on deposits insured up to $5,000, as indicated by the experience of the past 70 years.

The cost of insurance will not be disproportionately heavy in relation to earning power if paid by banks in proportion to their total deposits. If insurance be limited to $5,000 for each depositor and the cost is distributed among the banks in proportion to their insured deposits, the payments by smaller banks would be nearly double the assessments distributed on the basis of total deposits. In other words, we have over 13,000 banks that are insured 70 percent or greater; and if you place your premium on the insured portion only, it is going to very materially raise the assessment on those 13,000 smaller banks.

We have recommended not only that subscriptions by insured banks to capital stocks of the Corporation be eliminated but also that the Corporation be given the right to allocate to surplus any portion of the some $300,000,000 paid to it by the Treasury and the Federal Reserve banks. If the amounts paid in subscriptions to stock were to be carried in full on the books of the Corporation as capital stock, the Corporation would be unable to pay any losses except out of income, over and above operating expenses, without impairment of its capital. The Corporation would have no surplus; and while it might legally be permitted to spend its capital in meeting its obligations, a substantial capital impairment shown in its published reports would have a most adverse effect upon public confidence. We are therefore recommending that the stock issued by the Corporation to the Federal Reserve banks and the Treasury be without par value, and that the balance be placed in a surplus or reserve account.

Until such time as the resources of the Corporation may be adequate to handle the volume of anticipated losses it would be very unwise for the Corporation to pay dividends. We therefore recommend that the payment of dividends be eliminated.

It is important that the Corporation be given adequate means for increasing the funds at its disposal during critical periods. It is doubtful, however, if at such times the Corporation could borrow from private sources. The United States Treasury is the logical purchaser of these obligations. The Government is vitally interested in the maintenance of the country's banking system. We recommend that the obligations of the Corporation be issued only with the approval of the Secretary of the Treasury, so that any credit which the Corporation may require shall not conflict with the financial policies of the Government.

The success of deposit insurance depends upon the soundness of the insured banks. In my opinion the two major objectives of those administering the affairs of the Federal Deposit Insurance Corporation should be, first, to assist in making the insured banks sound financially and, second, to keep them in sound shape.

During the past year the activities of the Corporation have been chiefly concerned with the first of these problems, that is, the rebuilding of the capital structures of insured banks. In the future, the Corporation should devote a large part of its efforts to the maintenance of sound conditions among the insured institutions.

To maintain sound conditions among all insured banks it is essential that the Corporation have the power to control the admission of banks to the insurance fund. We cannot return to the overbanked condition of 1920 if we wish to have a sound banking structure. The growth of excessive banking facilities was one of the most destructive influences which existed prior to the banking holiday of 1933.

Since the banking holiday much effort has been expended in reorganizing and relicensing banks in order that the frozen funds of the depositors might be released. The accompanying table indicates that more than 2,000 banks have been added to those which withstood the shock of the banking crisis.

(The table referred to is as follows:)

Newly licensed banks grouped according to volume of total deposits by class of bank, July 1, 1933 to Dec. 31, 1934 [1]

[Deposit figures in thousands]

	July 1, 1933 to Dec. 31, 1934					
	Number of banks			Aggregate deposits [2]		
	National	State	Total	National	State	Total
Banks with deposits of—						
$100,000 or under	25	379	404	$2,070	$22,905	$24,975
$100,001 to $150,000	29	222	251	3,624	27,528	31,152
$150,001 to $250,000	131	268	399	25,862	50,956	76,818
$250,001 to $500,000	219	248	467	78,988	87,635	166,623
Subtotal	404	1,117	1,521	110,544	189,024	299,568
$500,001 to $750,000	110	90	200	67,346	55,735	123,081
$750,001 to $1,000,000	58	42	100	50,765	36,665	87,430
$1,000,001 to $2,000,000	76	65	141	104,282	88,732	193,014
$2,000,001 to $5,000,000	44	35	79	131,970	102,133	234,103
$5,000,001 to $10,000,000	16	6	22	113,573	35,067	148,640
$10,000,001 to $50,000,000	5	3	8	91,414	51,860	143,274
Not available	6	88	94			
Total	719	1,446	2,165	669,894	559,216	91,229,110

[1] By "newly licensed" is meant existing banks reopened, banks reorganized, and primary organizations.
[2] Deposit figures for the most part as reported in Rand-McNally Bankers' Directory for July 1934.

Source: Card records of newly licensed banks maintained by the Division.

Mr. CROWLEY. Under present conditions, the Corporation insures all newly licensed banks which apply for insurance, if they are found to be solvent. Approximately 90 percent of the newly licensed institutions have become insured. The Corporation should be granted the specific power to refuse the admission of new banks into the insurance fund where such admission would weaken the banking system. The Corporation should also be given the specific right to require a higher standard than mere solvency for admission to the insurance fund.

It is my firm belief that every community which can produce a sufficient volume of deposits to support a bank should receive the advantages of such facilities. There are many localities throughout the United States, however, which can support only one or two banks. To establish a second or third bank in such communities leads to speculative and destructive practices in an effort to earn sufficient income to pay expenses. For the protection of the insured institutions, the Corporation and the public welfare, the admission of banks to the insurance fund should be carefully supervised.

You understand that under our bill all of the banks that are now members, State banks and member banks, automatically come into the permanent fund, without being certified over again. The fact that they are now members automatically washes them into the fund, so that the only thing you are dealing with is the banks that are outside of the fund, or banks that may be chartered in the future.

The CHAIRMAN. It might be well to state in that connection that under the act for the insurance of bank deposits all national banks and State banks of the Federal Reserve system were automatically admitted into membership or participation in the benefits of the Deposit Insurance; were they not?

Mr. CROWLEY. That is correct.

It is for these reasons that we have recommended that the legislation incorporate specific standards to be met by future applicants before admission to the benefits of deposit insurance. These standards have already been recognized by Congress in other legislation.

In the latter part of 1933, banks were admitted to membership in the insurance fund under exceptional conditions. The situation existing at the close of 1933 was critical. The lack of real public confidence in banks was unsettling. Congress, therefore, provided that all solvent banks should be admitted to the insurance fund even though their capital was impaired in a number of instances. However, the Corporation immediately undertook to assist all banks which needed it in rebuilding their capital structures and correcting capital impairments which our examinations had disclosed.

The capital rehabilitation of banks was to be effected either through local contributions or through the facilities of the Reconstruction Finance Corporation. The Insurance Corporation assisted State nonmember banks to rebuild their capital structure. The responsibility for the condition of national and State member banks rests with the Comptroller of the Currency and the Federal Reserve Board, respectively. The Comptroller of the Currency and the Federal Reserve Board had the right to insist that banks under their jurisdiction accept necessary aid. The Corporation, however, had no such power. To accomplish the task of rebuilding the capital of a nonmember State bank which had been admitted to the benefits of insurance, the Corporation could only use the power of rational appeal to the board of directors or to the State banking authorities. Without the cooperation of the State banking authorities the capital structure of nonmember banks would not have been rebuilt.

State nonmember banks which could not obtain local capital contributions were assisted in securing aid from the Reconstruction Finance Corporation. Banks which had already made applications were assisted in complying with the conditions laid down by the

Reconstruction Finance Corporation. The accompanying table reveals the extent of the aid extended by the Reconstruction Finance Corporation to the various classes of banks in this country. While it is true that by the close of 1934 Federal Reserve member banks—State and national—had received almost three times as much Reconstruction Finance Corporation aid as had nonmember banks, in proportion to total deposit liability the aid given nonmember banks was twice as great as the assistance extended member banks.

(The table referred to is as follows:)

Reconstruction Finance Corporation purchases of capital obligations of insured banks

[In millions of dollars]

	National banks	State member banks	Insured nonmember banks (excluding mutuals)	Total insured banks (excluding mutuals)
Total deposits, June 30, 1934 [1]	$19,896	$11,116	$4,746	$35,814
Capital surplus and undivided profits, June 30, 1934 [1]	2,843	1,886	1,005	5,752
Net R. F. C. contribution to capital to June 30, 1934 [1]	384	202	184	773
Ratio R. F. C. to total deposits (percent)	1.9	1.8	3.9	2.2
Ratio R. F. C. to total capital (percent)	13.5	10.7	18.3	13.4
R. F. C. cumulated disbursement to all banks, Feb. 1, 1935 [2]	465	238	256	959
Ratio of item 6 to item 1 (percent)	2.3	2.1	5.4	2.7
Ratio of item 6 to item 2 (percent)	16.4	12.6	25.5	16.7

[1] Call Report of Insured Banks No. 1.
[2] As reported by the R. F. C.

Mr. Crowley. In some instances the necessary capital reconstruction had hardly been accomplished when applications were made by the banks to retire the preferred stock or debentures purchased from the Reconstruction Finance Corporation. As has been indicated, the capital reconstruction program was carried out for the purpose of protecting not only the banks but the Insurance Corporation. The capital and surplus of banks constitute a guaranty fund to depositors. They represent a cushion for the liability of the Corporation. When this capital and surplus are exhausted through losses, the depositor must turn to the Insurance Corporation for the payment of his deposits. The Corporation is vitally concerned, therefore, with the amount and condition of the capital and surplus of insured institutions. The reduction of this cushion of safety should be permitted only after obtaining the approval of the Corporation. If banks are allowed to retire this new capital, the rehabilitation, which has been so tediously accomplished, would be of no avail. The Corporation should have the right to control any future reductions in capital by insured banks.

The Corporation should have the right to review all mergers and consolidations affecting insured banks. It is possible that banks which have been refused admission to the insurance fund may be absorbed by insured institutions, thus extending the liability of the Corporation to depositors of the absorbed bank. Under the existing conditions there is no way in which such a subterfuge could be prevented.

In the interests of the depositor the Corporation should have the right to refuse to give its stamp of approval to inequitable or unsound reorganizations. Last year the Corporation was called upon to review more than 700 such plans. Many of those which we have seen are inequitable. The Corporation should have the right to pass upon the justice and soundness of reorganization plans. Depositors have often made tremendous sacrifices without the comparable sacrifice by stockholders and other special groups.

The Corporation now has the right to buy assets of closed Federal Reserve member banks. We have recommended that this right to purchase be extended to operating insured banks until July 1, 1936, whenever such action will avert an impending loss and facilitate a merger or consolidation. It will be to the best interests of both depositors and the Corporation if, through the absorption by the Corporation of a comparatively small loss, a more serious loss will be averted. Furthermore, such a procedure will offer both an incentive and a method for completing the rehabilitation of all insured banks prior to July 1, 1936. The right to purchase assets from operating banks should not be exercised unless in conjunction with a merger or consolidation and only for the purpose of averting loss.

Bank failures are frequently precipitated by defalcations. We, therefore, recommend that the Corporation be given the right to require adequate fidelity and other insurance. Such insurance provides protection to depositors, to bank executives, and to the Corporation. Where a given institution does not carry sufficient insurance, the Corporation should be given the right to contract for such insurance and charge the bank therefor.

A method whereby nonmember banks may withdraw from the insurance fund should be included in the legislation. Banks leaving the insurance fund should give adequate notice to the Corporation and to their depositors. However, such withdrawals should not expose the depositors to a sudden cancelation of the protection afforded them, and the insurance benefits should be extended to the depositors for 2 years after the withdrawal of any bank.

We also believe that the Insurance Corporation should have the right to terminate the insurance of any bank if, after a hearing and after notice to depositors, such action is in the best interests of both depositors and the Corporation. In establishing deposit insurance, Congress has assumed not only a definite responsibility to bank depositors but also a moral obligation for the sound management of banks. If the Corporation finds that an insured bank is engaged in repeated practices detrimental to the depositors, the Corporation should not be placed in the position of sanctioning such practices but should be given the right to terminate the insurance of the bank's deposits without jeopardizing the depositors. For the protection of depositors, we have recommended that in such cases insurance be extended for 2 years from the time that membership in the fund is terminated.

The right of dismissal may seem to be somewhat drastic, but it is hoped that the use of this power may seldom be necessary. As an intermediate step and as a means of notifying the public, it is suggested that the Corporation be authorized to publish either all or such portions of examination reports as it deems necessary. The State supervisory authorities will be advised of the intention to publish all or part of the examination report and only after adequate notice has been served on the executives of the bank concerned will such action take place. This procedure is designed to allow sufficient time for the executives of the bank concerned to correct the practices which jeopardize the safety of the depositors' funds. The Comptroller of the Currency has this right in the case of national banks.

Reports of condition now being issued to the public are confusing because of their inadequacy and lack of uniformity. Considerable efforts have been made to study this question. Conferences have been held with the State and Federal supervisory agencies in an effort to develop standard and uniform reports of condition. In order that the public may be informed as to the status of the institutions with which they do business, periodical statements of condition should be required of all banks.

Revision of the provisions of the law reciting the obligation of the Corporation to pay the insured deposits of a closed insured bank is necessary. As it now stands, the law requires the Corporation to organize a new national bank to act as its instrumentality in paying the insured deposits of every closed insured bank. This procedure must be followed, even though there is not the slightest possibility of the community being able to capitalize the new national bank. Eleven insured banks have thus far closed, but in only one instance were the local people in a position to capitalize the new bank.

This procedure for paying insured deposits has proved unsatisfactory, since it involves needless expense and many unnecessary accounting problems which could be eliminated if the Corporation were permitted to pay its obligations in the same manner as other insurance companies engaged in the commercial field. Accordingly, it is proposed that the organization of a new bank be at the discretion of the Corporation.

Under the present law, where it pays the insured portion of a deposit claim which is larger than $5,000, the Corporation becomes subrogated to the entire amount of the depositors' claim until it is reimbursed for the amount paid out to the depositor. This is manifestly inequitable to the larger depositors. We believe that the Corporation should be subrogated only to that portion of the claim which it pays, the depositor retaining his claim for any insured portion and receiving all dividends payable thereon directly from the liquidating officer. In the case of every closed bank there are some depositors who can never be located by reason of death, disappearance, or change of residence. We believe claims which are not filed within 1 year after an insured bank is closed should not be paid by the Corporation. This suggestion finds ample precedent and will enable the Corporation to close its books on each pay-off within a reasonable period.

The bill before you includes suggestions for clarification of provisions of the existing law about which some doubt has arisen. The adoption of these provisions will facilitate administration.

We recommend that the maximum limit of insurance to any one depositor be retained at the present figure of $5,000. Congress, in establishing deposit insurance, was presumably most concerned with the mass of depositors with small accounts. Our reports cover 51,000,000 accounts, of which over 98 percent are fully insured with the $5,000 limitation. Many of the accounts not fully covered are interbank accounts, public funds, deposits of corporations, institutions, and trust estates. The actual number of individuals with deposits in excess of $5,000 is probably less than 1 percent of the total number of depositors. Out of the 14,000 insured banks, over 9,600 have more than 80 percent of their deposits insured under the $5,000 limitation. To raise the limit of insurance above $5,000 would materially increase the maximum possible liability of the Corporation. If all the deposits were insured, this would be more than doubled. It would be increased from the present 16½ to nearly 30 billion dollars by the permanent plan which now exists in the statute. This tremendous increase in the maximum possible liability of the Corporation would benefit only one out of each hundred bank depositors.

The Insurance Corporation's interest in the sound operation of banks is more tangible and more vital than that of any supervisory authority. Deposits in practically all commercial banks and trust companies of the United States are insured by the Corporation. Bank supervisory agencies have a responsibility to the depositing public, and it is their duty to see to it that the bank laws are properly enforced. The Corporation, however, has a financial liability to these depositors. Its interest in the sound operation of these institutions is one of dollars and cents.

There are two courses open to the Insurance Corporation. It may be a charitable institution which will pay for the mistakes, bad banking, and dishonesty of bankers, in which case the cost of the insurance must be set so high that it will be an injustice to every sound bank. Or, by being placed on a sound basis, the Corporation may be used as an instrument to improve the standards of bank management and reduce the losses to depositors through bank failures. The latter course, which I prefer, requires that the standard of bank supervision throughout the country be improved, that the Corporation be given the right to protect itself against excessive risks, and, finally, that the Corporation be not handicapped by taking into the fund banks which are unsound or by continuing in the fund banks which are mismanaged.

We have a number of charts, Mr. Chairman, and we would be glad to answer any questions.

The CHAIRMAN. I would suggest, Mr. Crowley, that the charts that are pertinent and connected with your statement might well be appended as a part of your statement and published in the hearings at the proper place. Without objection, that will be done.

Mr. FORD. If a bank is put out of the fund, does the bank continue to pay the assessment?

Mr. CROWLEY. Yes, sir. We collect the assessment for this reason: The deposits of that bank remain insured for 2 years. If we put a bank out of the fund we have naturally got to go in there from time to time to look after our interests, and they must pay the premium.

Mr. HOLLISTER. Even if the bank withdraws voluntarily?

Mr. CROWLEY. Even if the bank withdraws voluntarily, they must pay for 2 years. The reason for that is this: That you may put some money in a bank, believing it to be insured, and if it withdraws from the fund tomorrow you may be the victim of a misunderstanding. So we believe the depositors should be given a reasonable protection before our liability ceases.

Mr. HOLLISTER. Isn't it also a protection of the fund? Isn't it true that some banks would like to withdraw from the fund in order to escape responsibility for assessments? That would be a great weakening of the fund, would it not?

Mr. CROWLEY. Correct.

Here is another thing. Banks may come into the fund in order to obtain the psychological effect of having insured deposits. As they go along and find that it is going to cost them a little something they would like to get out. They might believe that they can live outside of the fund. They would like to come in in bad times and get out in good times and have the door swinging both ways for them. That is very unsound. I think, for the sake of the whole banking system, every bank in the United States should be forced to be a member of the Federal Deposit Insurance Corporation. Then you would have uniformity all the way through.

Mr. REILLY. Don't you think there is going to be little opposition amongst the banks, except the large banks?

Mr. CROWLEY. The cost of the insurance that we have recommended to the small banks is very nominal. To 13,000 banks it is a very nominal sum. There will be no excuse, in my opinion, for the smaller banks getting out of the fund on account of the cost of this insurance, because it is not excessive.

Mr. CROSS. It is the big banks, you think, that are asking to get out?

Mr. CROWLEY. I do not believe it is. If this corporation were properly set up and properly sold to the depositors, I do not think many banks could live outside of this fund, and I think that is the way it should be.

Mr. KOPPLEMANN. I am very much interested in what you said a moment ago, that every bank ought to be compelled to belong to the Insurance Corporation. You know, of course, the difficulty we have had in my State, Connecticut. Is there anything in this law which would either compel the banks to come in, or make it so attractive that they would come in?

Mr. CROWLEY. There are only 1,100 banks outside of this fund now.

Mr. KOPPLEMANN. I am specifically interested in Connecticut, and in the Nation as a whole, because of the difficulty we have had.

Mr. CROWLEY. I think that whole question is going to be answered when we get our permanent law. If it is a law that we can all get behind and support and sell to the depositors, and if the cost is not excessive, I do not believe the banks of very many States can afford to stay out of the system.

Mr. KOPPLEMANN. Is not the real reason they did not want to come in, this feature of examination, which they look upon as an interference?

Mr. CROWLEY. You do not get so much objection to the examination from a good bank. Our experience indicates this, that the objection to examination comes from the fellow who should be examined often. Your better institutions do not object to regulation.

Mr. KOPPLEMANN. What I am trying to get at is how we are going to get these 1,100 banks in. Have you got anything in the law on that?

Mr. Crowley. No; but I think we have quite a few applications before us now, have we not, Mr. Fox?

Mr. Fox. Yes; we have.

Mr. Crowley. We have been in operation 15 months, and we have some 8,760 State banks which are insured. There are only 1,100 licensed banks outside of the entire system.

Mr. Kopplemann. I believe the depositors throughout the Nation are 100 percent for this thing, except those who have been told, as they were in my State, that it is a terrible thing, and because they do not have the facts, they believe that statement.

Mr. Crowley. We have had some opposition from the bankers, because there were doubts in their minds. For instance, they had an unlimited liability hanging over them. I think if that and some other features were straightened out you would get the cooperation of a great many of your financial institutions—especially if you give to this Corporation some regulatory powers, so that it might have a part in holding up your banking system.

Mr. Goldsborough. I have noticed in several banks a sign reading, "The deposits in this bank insured by the Federal Deposit Insurance Corporation." That creates the impression that all the deposits are insured. Is there anything in this bill which would require those signs, when they are put up, to show what the limitation is?

Mr. Birdzell. Yes. I think you may have an erroneous impression of the effect of the present sign. The present sign that we have adopted shows the amount right on the sign.

Mr. Goldsborough. I did not mean that the sign of the Federal Deposit Insurance Corporation was misleading, because I was talking to a Congressman the other night, and he said that in his territory the signs all disclose the amount of the insurance, but I want to say that I have seen this misleading sign and it does not seem to me that it ought to be allowed.

Mr. Birdzell. From the very beginning we have used the utmost care to prevent advertising being put out that would be misleading to the public in that respect.

Mr. Hancock. Mr. Crowley, what would be the annual return to your insurance fund, based upon one-twelfth of 1 percent of the total?

Mr. Crowley. About $30,000,000, Congressman Hancock, per year.

Mr. Hancock. What would the assessment amount to?

Mr. Crowley. About $30,000,000, and income from the investment would amount to about $9,000,000.

Mr. Hancock. Under the proposed new bill, is the levying of that assessment mandatory or discretionary?

Mr. Crowley. We have the right to reduce it, but not below 50 percent. In other words, we have a refunding provision in there, after we get our reserves built to a certain point.

Mr. Hancock. Is it your purpose and intention to levy an annual assessment every year?

Mr. Crowley. Yes; and that would have to be, because you will have to build your reserves for the future, in order to take care of some unforseen obstacle. If you do not do that, but only try to assess in times of difficulty, you are going to create additional hardships when banks are already subjected to as great a load as they can carry.

Mr. HANCOCK. I know that you have been making an exploratory inquiry into this subject, and I am interested to know, as a result of the figures and reports you have got, whether it is true that 1 percent of the people in this country own and control 60 percent of the deposits in the banks?

Mr. CROWLEY. I think that 800,000 individuals and corporations control about 65 percent of the deposits.

Mr. REILLY. Corporations too?

Mr. CROWLEY. They are included in depositors.

Mr. GIFFORD. You said a good deal about the impairment of the capital. When the R. F. C. provides a new capital structure, is it easy for the banks to withdraw and repay the R. F. C.? Can you explain to the committee what the conditions are they have to meet before they are allowed to repay? Do you want to have something to say about it?

Mr. CROWLEY. Yes. Let me say this: We have gone out in the last year and have aided, with the help of the Reconstruction Finance Corporation, in strengthening very nearly 3,500 out of some 7,800 State banks in this country not members of the Federal Reserve System. The difficulty is this, that we go out and we work with the stockholders and directors and everyone, getting that money in the bank. A lot of these banks seem to confuse liquidity with capital position. In other words, because their deposits are increasing, although they may not have any capital to speak of, they feel that they should be able to pay back the Reconstruction Finance Corporation. What we want is this, that after doing this great job that has been done, these banks should not be permitted to again weaken their capital structures by repaying the R. F. C. unless some local contribution is made, or unless earnings place the banks in such a position that they will have sufficient capital to form an adequate cushion for the protection of the depositors and this Corporation. These banks should not be allowed to undo the constructive work of the past 15 months.

Mr. GIFFORD. As I understand it, many banks have come and applied to the R. F. C., in order to get this capital structure, because they were forced to mark off and mark down a considerable fund, and to meet that contingency they felt it necessary to add to their capital structure, but when that contingency seemed to have passed, and the bank was in perhaps better shape, they desired to get rid of the R. F. C., because the public at large felt that if they had to apply to the R. F. C. they necessarily must be involved. When they have gotten out of the condition that the examiner has forced them to remedy, are you going to resist their dismissal of the R. F. C.?

Mr. CROWLEY. I do not think we would object, provided they really have corrected that condition.

Mr. GIFFORD. Isn't it a case of resisting sometimes, because there is another second examination, one by you and one by the national bank examiner? Doesn't that defeat them?

Mr. CROWLEY. No. There is no duplication in Federal examinations. We do not examine a national bank, nor do we examine a State member bank. We take the examination report of the Comptroller and the Federal Reserve.

Mr. GIFFORD. I had assumed that you did, and by this talk this morning had suggested that you wanted the power to refuse. Are you going to take another examiner's word for the condition?

Mr. CROWLEY. Are you talking about banks coming into the fund?

Mr. GIFFORD. Yes.

Mr. CROWLEY. With regard to the requirement for banks coming into the fund, the Comptroller and the Federal Reserve may use the same yardstick as we are expecting the State banks to use, for admission to this fund.

In putting the banks out of the fund, we notify the Comptroller or the Federal Reserve or State supervisor of the condition that exists, and we give him 90 days time in which to make the correction. If it is not made we serve notice on the bank and give the bank the right of hearing.

As far as the capital-rebuilding program of the national banks is concerned, that has been done exclusively by the Comptroller. We have done it with the State nonmember banks only.

Mr. GIFFORD. Don't you realize that the public at large have the feeling that when the R. F. C. comes to the rescue of a bank it assumes more than 51 percent of the control? You realize that?

Mr. CROWLEY. That is not true. If you mean control of the individual bank.

Mr. GIFFORD. Yes.

Mr. CROSS. On the question of examinations you said you always accept the Comptroller's examination of a national bank and the Federal Reserve's examination of a member bank.

Mr. CROWLEY. That is right.

Mr. CROSS. But in this bill you ask for authority to make an examination, with the consent of the Comptroller and the consent of the Federal Reserve.

Mr. CROWLEY. That is done for this reason, that we are asking for the right to purchase assets in the case of consolidations and mergers. Suppose you had a national bank that was in some difficulty. We want the right to go in with the Comptroller and see if there is anything we might be able to do.

Mr. CROSS. You do not contemplate a general request to the Comptroller and to the Federal Reserve for examination of the institutions?

Mr. CROWLEY. No, sir.

Mr. FORD. Where the R. F. C. has purchased $100,000 of capital stock of a bank, in order to strengthen its structure, and in the course of 6 months they feel that they want to repay that, wouldn't it be a good idea to permit them to repay it, when capital is secured in the district to replace that sum?

Mr. CROWLEY. Let me say this to you gentlemen, that banks do not improve their position materially in 6 months' time.

Mr. FORD. Whatever the period would be.

Mr. CROWLEY. Oh, I agree with you—either through earnings or an improvement in conditions, or local contributions. Does that answer your question?

Mr. GIFFORD. Don't you understand that when there are three or four banks in one community, and all receive assistance from the R. F. C., but one is allowed to divest itself from the capital structure of the R. F. C., the public then begins to think that that bank may be a little bit stronger than the other two? Do you think that the public is very tender in its viewpoint of the strength of the local banks these days?

Mr. CROWLEY. That may be true, but, as a matter of fact, what are you going to do if you have three banks and the impairment of one of them was less, and through its own local contributions or its own earning capacity it put itself in shape so that it could go on by itself? The Government can only stay in these banks until the banks are able to carry on themselves.

Mr. GIFFORD. That is what I asked you in the first place, if you were going to attempt to resist their repayment of the R. F. C.?

Mr. CROWLEY. No; I think Mr. Jones and everyone would be glad if the banks could pay back a billion dollars tomorrow, without weakening the banking structure, but we do not want them to pay it back if it is going to mean a weakened situation.

Mr. HANCOCK. The chairman of the Federal Deposit Insurance Corporation has made a very able, interesting, and comprehensive statement here, and one that deserves the best thought and study of our committee. I am wondering if he will be available to come back to us from time to time.

The CHAIRMAN. Oh, yes.

Mr. CROWLEY. Surely.

Mr. HANCOCK. To discuss this report and statement after we have had a chance to absorb it?

The CHAIRMAN. Surely.

Mr. DIRKSEN. The question is perhaps speculative, but here is a thought that was suggested to me last summer, when we were liquidating one of our banks in East Peoria, that probably one of the best insurances of good banking comes from the fact that the bankers look after each other somewhat. In other words, they are just as much interested to see that their neighbor indulges in good banking practice, because if the losses entailed should appreciate year after year it would mean that sometime or other your insurance premium would have to go up.

Mr. CROWLEY. That is right.

Mr. DIRKSEN. However, the banks in Wisconsin in the aggregate would have no way of looking after or having contact with the banks in Illinois.

Mr. CROWLEY. That is right.

Mr. DIRKSEN. Suppose, as time goes on, you find that a geographical classification of these losses discloses that they are infinitely higher in one State than in another. I have heard bankers raise the point that they are heartily in favor of this insurance, but if it should be developed that there were losses in other areas over which they have no control or with which they had no contact, it would constitute an unjust penalty upon them in that particular area. Has it ever occurred to you that at some time or other it may be necessary to think of classifying these insurance rates on the basis of the geographical areas? It would involve a lot of work, I know, but the equity involved must be considered.

Mr. CROWLEY. I do not think that would be a practical thing for the corporation, at least until the whole banking system is almost foolproof, for this reason, that the thing that is the best security for the corporation now is the diversification of risk which is spread over the entire country.

For instance, if you put the Middle West in a class by itself, and they have a drought like this last year, and they must stay on their own, you are going to make insurance for those banks so expensive that it is going to be almost prohibitory for them to belong to the fund.

As I see this thing, the bankers have got to take this viewpoint, that we had an almost complete collapse of the banking system in March 1933. You can hear people say, " We were still able to stay open " but the fact remains that the banking system, including the New York banks and other Federal Reserve member banks, had, for all practical purposes, broken down. The interest which the banks should have in the Federal Deposit Insurance is to help it build a banking system that will remain independent and sound. None of us can justify a continuance of our kind of banking system, (and I am an advocate of our present banking system) if we are to have a reoccurrence in 10, 15, or 20 years of the situation which existed in 1933.

Mr. GOLDSBOROUGH. Why does it require a recurrence? Why should you have to do it twice to prove it?

Mr. CROWLEY. I believe that the Federal Deposit Insurance does offer the vehicle for the correction of the banking system of this country. I am not talking about monetary control; I am talking purely of supervision.

Mr. GOLDSBOROUGH. In the last analysis, the Federal Deposit Insurance Corporation has access to no more money than the banking system itself has access to, and the banking system itself only has access to about $7,000,000,000, which is the entire capital, surplus, and undivided profits of all the banks, so that in the last analysis the Federal Deposit Insurance Corporation can do absolutely nothing except act as one means of maintaining the confidence of the people in the integrity of the banks, and thus avoid runs on the banks.

Mr. CROWLEY. Yes.

Mr. GOLDSBOROUGH. That is the truth of the situation.

Mr. DIRKSEN. At the present time one who goes to a bank and makes a time deposit can under no circumstances withdraw that money, even though he may waive all interest thereon. I understand that is embodied in regulation Q.

A man went into a small bank in my district, and he wanted to place $1,200 on time deposit, for 90 days. He said, "A contingency may arise whereby I might need the money. Can I get it out before that time in such a case?" They said, " No." He said, " Suppose I waive the interest? " They said, " You cannot get your money anyway." He went across the street and put his money in Postal Savings. He can put his money in the Postal Savings and if any portion of the money is there up to the interest pay day, he can even get interest, and get new certificates for the balance of his money. It occurs to me that there is a disparity between the obligation imposed by regulation Q and the practice of the Postal Savings System.

Mr. BIRDZELL. That is correct.

Mr. DIRKSEN. They ought to be brought into uniformity, because it is affecting these small banks. And it is not necessarily the fact that the bank loses income from the small deposit, but it is a fact that a man goes out of that bank and he says, " There is something wrong with this bank ", and he does not realize the implications of regulation Q, and once he gets to talking to his neighbors, he impairs some of the local confidence in the bank, because of that lack of consistency in these systems at the present time.

Mr. CROWLEY. I do not think ours in inconsistent. I think ours is consistent, and theirs is inconsistent.

Mr. DIRKSEN. You mean the Postal Savings?

Mr. CROWLEY. Yes.

Mr. DIRKSEN. I agree with you, but I agree with you also that the practice ought to be uniform, and the Postal Savings should be compelled to do precisely as you do.

Mr. BIRDZELL. There is a feature of the law that you may be familiar with, which provides that where Postal Savings are permitted to be withdrawn without the service of the notice required by the Banking Act of 1933, no interest shall be paid except interest accruing prior to the effective date of the banking act. But notwithstanding that, apparently they are paying interest up to the date of withdrawal.

Mr. DIRKSEN. Precisely, and even if they did not pay interest it would only remedy one-half the problem, because a man could still go and deposit and withdraw the deposit, which he cannot do now under regulation Q.

Mr. BIRDZELL. Your statement is correct, I believe. Attention should be given to that matter, because there is some unfair competition between the Postal Savings and the banks. That is particularly true now, when the banks are paying low rates of interest.

The CHAIRMAN. Of course, many people hold the view that if you insure all deposits in private banks the Government should not set up and maintain a deposit institution in competition with them. It is contrary to sound public policy, and the necessity for it has been removed, and there is no excuse for it. That is what we attempted in the Banking Act of 1933, which has not been followed as was contemplated by the framers of the act, to at least require that the Government, insofar as it competed with the banks in the matter of deposits, should maintain a purely savings system and not regular checking accounts.

It might be well to state in that connection, I think, that we have quite a number of communities, and you might say sections of the country, where the banking facilities have been, for the time being at least, swept away, so that the only depository left for the citizen was the Postal Savings System. So that difficulty confronts us in undertaking to deal with that problem, but for my part I think we should in some way legislate on that subject.

Mr. CROWLEY. It will help eventually to correct a part of your banking trouble when the Postal Savings deposits are permitted to go into your small banks. They would get that volume of business that may be helpful to them, so that they may be able to make some money.

Mr. DIRKSEN. May I make one observation on the table on page 16 of Mr. Crowley's report? I see that in the first column, from 1873 to 1878, the deposits were $85,000,000 and the losses $26,000,000, so the loss was approximately 30 percent. From 1892 to 1897 the deposits were $134,000,000 and the losses $43,000,000, which was 32 percent. Then the deposits from 1931 to 1934 were $5,356,000,000 and the losses $2,142,000,000, which was a loss of about 40 percent.

I am merely remarking the facts, because at the bottom the average loss per year for each $100 of deposits of $1.28 seems disproportionately so much lighter than 30 percent and 40 percent.

Mr. CAVICCHIA. That is because it takes in a greater part of this.

Mr. DIRKSEN. That is probably true.

Mr. WOLCOTT. I am given to understand that a man may have a deposit guaranteed up to $5,000, and his wife may have a deposit guaranteed up to $5,000, and there is no question about those. Is the joint account, in addition to those guaranteed up to another $5,000?

Mr. BIRDZELL. Yes.

Mr. WOLCOTT. Is a bona fide trust account, as a part of that savings division, subject to this insurance?

Mr. BIRDZELL. That is an account held in another capacity.

Mr. WOLCOTT. I say "bona fide" to distinguish it from a mere creation of a trust fund to avoid the purposes of the act.

Mr. BIRDZELL. Under the terms of the law, in paying off a bank we have to combine all of the deposits of the particular claimant which he holds in the same capacity and the same right. If he holds them in different capacities—for instance, you may maintain a bank account in your bank in your private capacity, and you may be a member of a partnership that also has a bank account in that same bank.

Mr. WOLCOTT. I know, those are separate.

Mr. BIRDZELL. They are separate. If you and your wife have a joint account, that is an account held in a different right. It may be all collected by your wife, or may be all collected by you while the bank is operating, and we have the problem of offsets, and the same law that applies in solving the problem of offsets in the closing of a bank must apply and work harmoniously with regard to the insurance. We must treat each one separately.

Mr. WOLCOTT. Let us work that out in a practical way. Assume that a man and his wife have $20,000 between them, and the man has $20,000 in bank, in a joint account between himself and his wife, with the feeling that upon his death his wife will not have to administer his estate, or probate his estate, but she can go down and avoid any such probation by merely drawing that money out as a joint depositor. Then comes along the F. D. I. C., and my understanding is that they can take that account and divide it up, so that the deposit will be divided $5,000 to the husband, $5,000 to the wife, and $5,000 in a joint account, with the possibility of another $5,000 in a trust account.

Mr. BIRDZELL. No; as long as the account is in the name of the husband and wife, no matter what the amount is, it is treated as one deposit, but it will be treated separately from any other account of the husband.

Mr. WOLCOTT. My point is this: John Jones has $5,000 in the bank, and John Jones and Mary Jones, his wife, have another $5,000 in a joint account. Are both of those accounts insured up to $5,000?

Mr. BIRDZELL. The first being an individual account, and the other being a joint account; yes.

Mr. WOLCOTT. The same thing follows if Mary Jones has another $5,000 in her name?

Mr. BIRDZELL. Exactly.

Mr. WOLCOTT. So he can take this $20,000 that they had in the original account, and split it up, $5,000 in his own name, $5,000 in her name, $5,000 in their joint names, and then $5,000 in the bona fide trust account?

The CHAIRMAN. They could not do that after the bank had failed.

Mr. WOLCOTT. I am saying that in that manner it would be possible for him to insure the total of his $20,000.

Mr. BIRDZELL. If it is done merely as a cover, so as to enable a man to get more insurance on his own money, we would pay him $5,000.

Mr. GOLDSBOROUGH. In that case the burden of proof would be on the Deposit Insurance Corporation.

Mr. BIRDZELL. Yes.

Mr. WOLCOTT. I know all the intricacies of the chancery practice, and I know you could split it up in different banks, but my point is on the face of it are those accounts insured, or upon the failure of that bank or the closing of that bank must the individual go into chancery and by suit against the Insurance Corporation, or something of that nature, prove that they were bona fide separate accounts?

Mr. BIRDZELL. If the information we get, upon going in to pay off the bank, indicates that there has been an attempt to increase our insurance liability to one owner of a deposit, using simply a joint account, or some other device to cover up his ownership, we would investigate that before we would pay the claim, and if we found enough evidence to satisfy us that there was a subterfuge for the purpose of increasing the insurance of one depositor, we would decline to pay it.

The CHAIRMAN. The law specifically makes the test the individual ownership.

Mr. BIRDZELL. Individual ownership.

The CHAIRMAN. Without objection, we will take a recess until 10:30 o'clock tomorrow morning, and Mr. Crowley, we would like to have you and Judge Birdzell back tomorrow morning at 10:30 o'clock.

(Whereupon, at 12:30 p. m., the committee adjourned until Friday, Feb. 22, 1935, at 10:30 a. m.)

BANKING ACT OF 1935

FRIDAY, FEBRUARY 22, 1935

House of Representatives,
Committee on Banking and Currency,
Washington, D. C.

The committee met at 10:30 a. m., Hon. Henry B. Steagall (chairman) presiding.

STATEMENTS OF LEO T. CROWLEY, CHAIRMAN FEDERAL DEPOSIT INSURANCE CORPORATION; AND L. E. BIRDZELL, GENERAL COUNSEL FEDERAL DEPOSIT INSURANCE CORPORATION—Continued

The Chairman. The committee will come to order. We will continue the hearing on H. R. 5357.

Mr. Crowley, I would like to ask you two or three questions.

Did you give the figures showing the amount of insurance in banks that have failed since the passage of the Deposit Insurance Act?

Mr. Crowley. We have that here, Mr. Chairman. Do you wish the figures for each bank, or the total?

The Chairman. I do not care about having it broken down.

Mr. Crowley. The deposits in 11 banks that have failed amounted to $2,890,000, and of that amount the estimated net amount for which depositors were insured was $1,765,000; the secured deposits, and those subject to offset, amounted to $935,000. The uninsured balance amounted to $190,000. In other words, of total deposits amounting to $2,890,000 in failed insured banks, all but $190,000 were fully protected.

The Chairman. The amount of deposits insured for which your corporation was responsible amounted to $1,765,000?

Mr. Crowley. Yes, sir.

The Chairman. How much would you say, of that amount, will represent losses, if you can estimate it, by the Deposit Insurance Corporation?

Mr. Markham. We only have estimates of anticipated recoveries on the nine insured banks which failed during 1934. These banks had total deposit liabilities of $1,938,000. The estimated net loss to the F. D. I. C. amounts to about $356,000.

The Chairman. Do you mean to say that you will disburse to depositors to make good their losses, above what you will receive, the sum of $356,000?

Mr. Markham. Yes, sir.

Mr. MARKHAM. Of the $2,890,000, the offsets and the amount of the security that the depositor has pays everything but $190,000.

The CHAIRMAN. What will you pay to depositors? Your net disbursements, or what we might term your "final losses" in the Corporation down to date, amount to how much?

Mr. CROWLEY. It is impossible for us to tell you that because all we can do is to estimate.

The CHAIRMAN. That is what I am asking for, an estimate.

Mr. CROWLEY. We have estimated, I think, that in the case of the nine banks that suspended during 1934 the net losses to the Federal Deposit Insurance Corporation will be something like 40 percent.

The CHAIRMAN. I can understand you can only give us an estimate, but that is what I want to get.

Mr. CROWLEY. I think that is about correct, that it is about 40-percent loss that we anticipate.

Mr. CROWLEY. All of the claims of depositors in the 11 banks that were closed, with the exception of about $460,000, have already been paid. All but about $50,000 or $60,000 will eventually be paid, according to our estimates.

The CHAIRMAN. They have been paid up to now?

Mr. CROWLEY. $2,430,000, including offsets settled and secured claims paid.

The CHAIRMAN. All I want to ascertain is, first, the total amount of deposits in banks insured that have closed down to date.

Mr. CROWLEY. That is $2,890,000.

The CHAIRMAN. What portion of that amount of deposits was insured?

Mr. CROWLEY. All except $190,000, when you add to our insurance offsets and secured deposits. The net insured deposits amounted to $1,765,000.

The CHAIRMAN. That is the amount of deposits to be covered by insurance?

Mr. CROWLEY. That is correct.

The CHAIRMAN. For which you were responsible. That is the total of your actual liabilities?

Mr. CROWLEY. That is right.

The CHAIRMAN. And of that your estimate is that you will actually lose 40 percent?

Mr. CROWLEY. We will recover 60 percent.

The CHAIRMAN. That is the same thing, is it not?

Mr. CROWLEY. Yes.

The CHAIRMAN. The losses will be 40 percent?

Mr. CROWLEY. Yes.

The CHAIRMAN. That will be about what amount?

Mr. MARKHAM. $356,000 in nine of the banks.

The CHAIRMAN. There were 11 of them that failed?

Mr. CROWLEY. That is right.

The CHAIRMAN. How many of those failures were normal or legitimate failures, and how many of those failures were due to defaults?

Mr. CROWLEY. I think six of them were due to defalcations.

The CHAIRMAN. Those figures are correct?

Mr. CROWLEY. That is right.

The CHAIRMAN. So we have had five bank failures other than those due to defalcations since the effective date of the Deposit Insurance Corporation Act?

Mr. CROWLEY. Let me say this: There are three banks that I think will pay 100 cents on the dollar.

The CHAIRMAN. How many failed insured banks will not pay 100 cents on the dollar and were not closed on account of defalcations?

Mr. CROWLEY. There are four. For example, we have a little bank with $40,000 deposits, which is so small that they put it in liquidation because they could not make any money.

The CHAIRMAN. Did you have any actual loss in that?

Mr. CROWLEY. Yes; I think we may have a small loss.

The CHAIRMAN. You have already accounted for three banks in which you have no substantial loss.

Mr. CROWLEY. Take the bank in Pittsburgh that closed. They had some $700,000 in Postal Savings accounts. They took collateral that might be helpful to us, which was necessary to use for Postal Savings. Those depositors were protected by collateral that was taken from the assets of the bank. It weakened us to that degree.

Every time they post collateral for public funds, or what not, they only weaken our position that much more.

The CHAIRMAN. I believe you said yesterday that your earnings had amounted to about $9,000,000 down to this time; is that correct?

Mr. CROWLEY. They are running about 9 million, between 22 and 23 thousand dollars a day.

The CHAIRMAN. Taking your losses down to date, your net balance will show a profit of something approaching 8½ million dollars?

Mr. CROWLEY. No. They will before the overhead is deducted; after the overhead is deducted, they will still show a substantial profit. This corporation could be wound up today and pay its losses and return to the Federal Reserve bank and to the Government their money plus a return on their investment.

The CHAIRMAN. And a substantial return?

Mr. CROWLEY. That is correct, sir. You understand, there were some suspensions outside of our fund; there were 47 banks that failed outside of the fund.

The CHAIRMAN. You had made that statement yesterday, as I recall, that there were 47 failures outside of the Insurance Corporation.

Mr. CROWLEY. Yes.

The CHAIRMAN. In that connection, to make those figures clear, you might state how many banks are uninsured.

Mr. CROWLEY. We have 1,100 banks that are operating in this country today that are uninsured.

The CHAIRMAN. And out of the 1,100 banks you had 47 failures outside of the Corporation, and of the total number inside the Corporation you had the number to which you had already testified?

Mr. CROWLEY. That is correct.

The CHAIRMAN. Mr. Crowley, I want to ask you what your present resources are for the protection of depositors?

Mr. CROWLEY. We have $140,000,000 from the Federal Reserve banks and $150,000,000 from the Treasury, which has been subscribed in the form of stock. We also have $41,000,000 from the banks themselves. So we have approximately $330,000,000, and we have that invested in Government securities, with the exception of about $15,000,000 that we carry on hand for any normal expenses that we might have.

The CHAIRMAN. You have the right and the privilege and the authority under the law to expand your capital three times?

Mr. CROWLEY. By borrowing.

The CHAIRMAN. By issuing obligations?

Mr. CROWLEY. That is correct, Mr. Chairman.

The CHAIRMAN. So you have potential resources of about $900,000,000, which would give you four times the amount of your capital?

Mr. CROWLEY. That is correct.

The CHAIRMAN. Which would be 1,200 million dollars?

Mr. CROWLEY. Yes.

The CHAIRMAN. In addition to that, under the act passed in 1934, the amendatory act of last year, you have also the right to borrow $250,000,000 from the Reconstruction Finance Corporation.

Mr. CROWLEY. That is correct, sir.

The CHAIRMAN. Summed up, it means that your Corporation is equipped practically to the amount of a billion and a quarter dollars at this time?

Mr. CROWLEY. There is a question, Mr. Chairman, whether the $250,000,000 that we have the right to borrow from the Reconstruction Finance Corporation should not be included in our borrowings of three times the amount of our capital.

The CHAIRMAN. How do you get that? The original act gave you the right to expand your capital three times.

Mr. CROWLEY. That is right.

The CHAIRMAN. We attempted and I thought we had supplemented that last year in the bill passed at that time giving you entirely separate authority to borrow a quarter of a million dollars from the Reconstruction Finance Corporation.

Mr. BIRDZELL. This is the situation, Mr. Chairman. The law under which we are operating does not provide for a Government guarantee of either the principal or the interest of our debentures which we may issue to the extent of three times our capital.

The CHAIRMAN. I know that.

Mr. BIRDZELL. Because of that fact we suggested that that guaranty be given. It was in the bill that was under consideration last year and was stricken out in the Senate. When the bill was ultimately passed, however, it was not passed quite in the form that you now have in mind, Mr. Chairman.

It was passed in this form, that as to the debentures that might be issued by our Corporation, our Corporation could call upon the Reconstruction Finance Corporation to purchase at par to the extent of $250,000,000. That is a sort of substitute for Government guarantee, to provide us with a par market for our debentures up to that amount.

I think if you will turn to the provision of the act where that is found you will be impressed with the fact that the $250,000,000 is part of the debenture authority of the board of directors, and not in addition to that.

The CHAIRMAN. In any event, you have about twelve hundred million dollars?

Mr. BIRDZELL. That is right.

Mr. CROWLEY. In our proposal we are asking for the right of issuing three times the amount, which will give us $1,200,000,000. We say nothing about the 250 million, but it is still available from the Reconstruction Finance Corporation.

Mr. FORD. I wanted to make one observation. The banks pay this premium.

Mr. CROWLEY. That is right.

Mr. FORD. As a matter of fact, the depositors pay it.

Mr. CROWLEY. Of course, the depositors, like the consumers of anything, ultimately pay the expense.

Mr. FORD. They have cut out the interest on the unused dollars, and since they have quit paying interest that really make the depositor pay for his own protection.

Mr. CROWLEY. That does not affect the rank and file of the depositors. The average depositor never got anything on his demand deposits.

Mr. KOPPLEMANN. Further on the banks that the chairman was talking about, what, under the present law, or under the bill proposed that is before us, are you empowered to do about rehabilitating many of these closed banks.

Mr. CROWLEY. There is the possibility that in the 1,100 licensed uninsured banks a very substantial number of those may be brought into our fund. There are some that are staying out because they do not wish to join.

Mr. KOPPLEMANN. But what I specifically would like to know is whether or not under the old law, or under the new bill as proposed, you have the power to help these banks get back on to their feet.

Mr. CROWLEY. No; we have no legal power to force them to do anything. With the help of the Reconstruction Finance Corporation we have been able to aid them.

Mr. KOPPLEMANN. Have you done so?

Mr. CROWLEY. We have already rebuilt the capital structure, with the help of the Reconstruction Finance Corporation, of about 3,500 insured State banks in this country.

Mr. KOPPLEMANN. I mean after they are in trouble.

Mr. CROWLEY. They were in trouble when we got them.

Mr. KOPPLEMANN. I am talking about 11 closed banks that were insured.

Mr. CROWLEY. We have not any authority.

Mr. KOPPLEMANN. No authority to keep them going. You see what I am trying to bring out, whether or not this act even goes further than merely guaranteeing deposits, whether it does not also save the banks.

Mr. BIRDZELL. Under the existing law we could not, if we would, purchase any assets or loan any money to a nonmember bank, and of the 11 banks that have closed there were only 2 member banks. So we could not, if we would, go into those banks and rehabilitate them ourselves, except as to member banks. In this bill provision is made for something like that to be done.

Mr. DIRKSEN. Does the $41,000,000 that has been referred to represent the income from the deposit fund?

Mr. CROWLEY. No; it represents the assessment of one-fourth of 1 percent on insured deposits against the banks. The members of our fund pay an assessment. They have paid us $41,000,000.

Mr. DIRKSEN. Under the original law, could you still issue stock to the Federal Reserve bank?

Mr. CROWLEY. Yes; you could offer stock to the Treasury, or, under the set-up that now exists, you could authorize——

Mr. DIRKSEN (interposing). The original law provided that the Federal Reserve banks could subscribe to the extent of one-half of their surplus, on the first of January 1933.

Mr. CROWLEY. They have done that.

Mr. DIRKSEN. Then you have discretionary power to require only the payment of one-half of the subscription?

Mr. CROWLEY. We have required the payment of the entire subscription.

Mr. DIRKSEN. It has been paid entirely?

Mr. CROWLEY. It has been paid entirely; yes, sir.

Mr. GIFFORD. You have used the expression recover immediately.

Mr. CROWLEY. We have started to pay off to depositors in closed insured banks, Congressman, within 10 days from the time the bank closed.

Mr. GIFFORD. You have made no new suggestions?

Mr. CROWLEY. We have made some suggestions that are purely administrative.

Let me explain that to you. There is a little bank in Montana that closed. They are way off in the country. We had to go way up in the hills and bring the people down to get their money. Under the present law we must carry on the expenses of continuing that bank, and it may be that all the depositors except three or four were paid. We are asking for the right to bring the balance of the affairs of the bank into Washington so that we might complete the tag-end of those payments from our office here.

Mr. GIFFORD. Then I notice that you want some proof from depositors that a deposit in a bank that you may find is really one deposit, is held for the benefit of one person.

In the future you may want written proof that a certain number of deposits may be held for the benefit of one person, under different names, unless it were proven to be a trust deposit.

Questions asked you yesterday related to deposits carried as trustee, or in a joint account.

I thought I noticed a recommendation in reference to the matter of determining whether there were not various deposits in a bank of only one individual.

Mr. BIRDZELL. There is nothing specific on that further than this. It provides for the claim agents of the Corporation being able to take proof to determine the ownership of the different amounts of money.

Mr. GIFFORD. My question was leading up to that.

Mr. BIRDZELL. We will not find occasion to use that provision of law in any great number of cases, because we get practically all our information from the books in the banks. These proofs of claims are made up and then the depositors are asked to come in and get their money. All that remains to do is to reconcile with the depositor's passbook.

Mr. GIFFORD. I am certain that there is a recommendation there that seemed to be an attempt to prove that certain people might divide their accounts in the same bank for the sake of being insured under the $5,000 limit.

Mr. BIRDZELL. Would that be under the definition of insured deposits?

Mr. GIFFORD. I cannot recall.

Mr. GOLDSBOROUGH. How much in the way of income is derived from one-twelfth of 1 percent?

Mr. CROWLEY. About $30,000,000.

Mr. GOLDSBOROUGH. As I understand it the law provides that the assessment may be lowered, but there is no provision in the proposed act under which the assessment can be raised.

Mr. CROWLEY. That is correct.

Mr. GOLDSBOROUGH. On what theory do you feel that it would not be wise to place in the proposed act some provision permitting the Insurance Corporation to raise that contribution from one-twelfth of 1 percent to such amount as might be necessary?

Mr. CROWLEY. This is my own personal viewpoint about that. I think that in building a fund the insurance of deposits, the first responsibility is to correct some of the mistakes or weaknesses in our banking system. In other words, I do not believe we are justified in charging to the bank system of this country the mistakes of the past. This Corporation should be given sufficient authority to eliminate a great many of the past mistakes.

There is a question in my mind as to whether we are justified in taking from a bank a large percentage of its income, or leaving it liable to an assessment which might jeopardize the soundness of that particular institution. To subject a bank to an additional assessment at a time when they are having about all the difficulties that they can encounter themselves may not be a wise policy.

Mr. GOLDSBOROUGH. That is the time when the Insurance Corporation can be of service to the depositors in banks.

Mr. CROWLEY. I think that the Government now has a direct responsibility in connection with our banking system. I think it has a responsibility to the Federal Deposit Insurance Corporation, and to the depositors. I believe that if we are going to build this fund over a period of years, that in addition to the income you get from the banks, you must have a way to build up a sufficiently large reserve. If we have a recurrence of the conditions that existed in 1907 or 1893, we will then have a cushion that we may fall back on out of which to pay losses.

I am not disturbed particularly at the losses of this Corporation in the next, 3, 4, or 5 years. Because of the rebuilding program and a recovery of business which will restore values, losses will not be great in the next 3 or 4 years.

I think over a period of 10 years this fund should build a substantial reserve.

Mr. GOLDSBOROUGH. You mean the act should be amended to provide for a Government contribution?

Mr. CROWLEY. I do not care whether it is a Government contribution or income from some other source.

Mr. GOLDSBOROUGH. I have no objection to it; I am just asking the question.

Mr. CROWLEY. I think where we go into the field of insuring deposits our first responsibility is to keep this Corporation solvent so that it can at all times meet its demands. Otherwise, I think confidence in banking would be broken down entirely.

Mr. GOLDSBOROUGH. Personally, I have no fear about that for the next 20 years.

But there is another consideration, and a very serious one, in my mind. This Corporation, in the minds of the public, is a Federal organization, a Federal deposit-insurance corporation; and unless it has a dual responsibility, the title is just as misleading as the title of the Bank of the United States in New York. It simply deceives the public.

I personally see no objection whatever to amending this proposed act so as to give the Corporation the right to raise this contribution from the banks from one-twelfth of 1 percent to one-fourth of 1 percent.

For a long while the banks will be afraid to make loans; the examinations are going to be rather strict; but we have given the banks in the last few years $13,000,000,000, and we are continuing to issue bonds and give them more billions of dollars.

As they wax strong and arrogant, and as business is resumed, and as they begin to brush the examinations aside, as they will in time, it will become necessary to fortify this Corporation and serve notice on the banks that they have the bag to hold if they go too far, as I see it.

I believe if the public knew that this is a one-twelfth of 1 percent limitation, and that the limitation was absolute and the Corporation could go no further, I think it would interfere very seriously with the morale of the public. That is my opinion—that they are bound to give way in a short time.

Mr. CROWLEY. Congressman Goldsborough, I think that for the psychological effect on the depositors they must have confidence in this Corporation. Depositors must have confidence that the fund is sufficiently large and that the Corporation is well managed. If they lose that confidence, that is where the difficulty will be. The great contribution which we have made is the establishment of confidence in the minds of the depositors.

Mr. GOLDSBOROUGH. One other thing: When the time comes to sell the debentures, aside from whatever the Reconstruction Finance Corporation may think, what would be the justification in the market for those debentures?

Mr. CROWLEY. I would say that if it got to the point where we had to issue debentures up to three times the amount of our capital there would be no open market for them at all. By the very nature of things, if we had such a situation that we would have to issue our debentures up to the limit, there is only one place where we could go to get that aid, and that is from the Treasury.

Mr. GOLDSBOROUGH. That is my opinion, and that is the reason I asked you the question.

Mr. CLARK. I want to say one thing in regard to the first point that Mr. Goldsborough made. I think it is a point well taken, that the Corporation should have the administrative power to raise the rate.

I want to state right here that I think of all the "new deal" agencies that have been set up this Corporation is the finest and has been handled in the finest manner, administratively. In the 15 months you have been in existence you have done pretty nearly a superhard job; and I for one would be willing to trust the administration of this Corporation to them, and give them administrative latitude, so that they could, if necessary, raise these premiums or assessments, and I think the public has more confidence in the work you have done than in the work that has been done by practically any other agency that has been set up in the last 2 years.

I am thoroughly convinced of that, both so far as the administration is concerned and in the way you have done it.

I think, personally, I would like to have you consider whether you think such an amendment as Mr. Goldsborough proposes would have a bad effect, because it seems to me it would have a good effect in giving you the administrative authority to raise the assessment, if the times and conditions demanded it.

Mr. FORD. The reason I asked the question as to whether or not the depositors were actually paying the insurance was with the idea of making a suggestion along the lines that Mr. Clark has made. But it seems that the banks, of course, will tell you, "Of course, it is all right to insure the deposits, but we pay the bill."

As a matter of fact, the bill is paid by the people whose money is in the bank. Quite a number of those deposits did not draw interest at any time. But there are also quite a number of them that did heretofore draw interest, and they have cut down on their normal interest. Where they used to pay 4 percent, they have cut as low as 2½ percent; so that in the long run, if the banks are paying the bill, I think the Deposit Insurance Corporation should have a broader latitude in reference to that assessment, so that they can raise it, instead of one-twelfth of 1 percent to one-sixth of 1 percent.

Mr. CROWLEY. You appreciate, of course, Mr. Congressman, that we have changed the way of determining our assessments.

Mr. FORD. Yes.

Mr. CROWLEY. We propose to assess on total deposits. A number of your larger banks are only insured up to 26 percent, while a vast majority are insured 70 percent or more.

I think that if the Deposit Insurance Corporation is going to bring about good banking, it is not going to do that through paying out losses. I think that the protection that it is going to afford will be brought about through studying and correcting a great many of our ills. I can foresee that, over a number of years, with this Corporation properly conducted you would have a minimum number of bank closings.

In other words, if we have the power to protect ourselves, there are going to be very few forced liquidations in this country; and if we are careful in the way we recharter banks—if we are careful in the way we conduct ourselves—the Federal Deposit Insurance Corporation might become the greatest vehicle in the Government for the rehabilitation of our whole banking system.

The CHAIRMAN. Mr. Crowley, under the act now proposed, the large banks will have, of course, to pay a premium of one-twelfth of 1 percent, based on all their deposits now?

Mr. CROWLEY. That is correct.

The CHAIRMAN. So that, whether the general banking structure is sound or not, these individual banks will realize that their liability is limited; and they will have no incentive to try to keep the banking structure on a legitimate basis.

On the other hand, if they realize that when they encourage speculative activities, which are always unloaded on those who know least about business, that their assessments are going to be increased, it seems to me that it would be a great restraining influence on those institutions.

Mr. CROWLEY. Well, I do not think——

The CHAIRMAN. It would influence them to conduct themselves in a very different way than they did in the period of 1925 to 1929.

Mr. CROWLEY. I do not think, Mr. Chairman, that the assessment is going to be the thing that might prevent the recurrence of that sort of thing, for this reason: Suppose that you double the assessment in some institutions, I do not believe that that would be a sufficient disciplinary measure to prevent speculation.

The CHAIRMAN. Those institutions are the ones that have prevented a provision like that going into the law. There could not have been any other reason why it has not become law. Is not that correct?

Mr. CROWLEY. I think that is——

The CHAIRMAN. They are the ones who do not want that provision in the law.

Mr. CROWLEY. Well, I think this, Mr. Chairman, that your fund must be kept sound. I think that the Deposit Insurance Corporation must have sufficient income to pay the losses.

The CHAIRMAN. That does not answer it.

Mr. CROWLEY. If it is necessary to give us the power to make the additional assessments, if that becomes necessary in order to keep the insurance fund sound, we should have authority to do that.

Mr. FORD. But that assessment cannot be of any particular effect in directly controlling an institution which wants to engage in unsound practices.

The CHAIRMAN. I did not mean that, but they can have the banks which are responsible, for speculations——

Mr. FORD. Any form of insurance tends to remove much of the incentive to observe sound practices.

The CHAIRMAN. Those banks, which are responsible for speculation, and which pass on their securities to the smaller banks, are the banks who under this proposed law have the greatest amount of insurance assessment to pay; and my theory is that if those banks know that assessment is not going to be increased, and there is not the tendency on their part to keep it straight. That is what I had in mind.

Mr. JONES. But the general proposition is that wherever you give insurance carelessness and speculation will actually increase, unless have strict supervision. We have that exemplified in the automobile business. For instance, the man whose automobile is insured becomes careless, even if the rates are punitive, so that in my State certain localities have to pay more than other localities. We do not even have a flat rate.

The CHAIRMAN. Is not that the general principle? Upon your theory we ought to abolish the Deposit Insurance Corporation entirely.

Mr. FORD. The rates have gone up comparatively; and in some localities I think it is very difficult to—let me discuss this off the record.

Mr. HOLLISTER. Might I ask a question? Following out this principle, the desire to certain banks to get this insurance and the objection of certain other banks, is it not true that—or, let me ask you, rather, what kind of banks, as a general rule, object to the principle, or the possibiliy, of unlimited assessment?

Mr. CROWLEY. Well, I believe that all the banks, large and small, object to the unlimited liability. I do not believe that you should have an unlimited liability. I do not thing that Congressman Goldsborough, when he refers to unlimited liability, has in mind an entirely unlimited liability but the right to call for a second assessment in the event it becomes necessary.

Mr. HOLLISTER. Or a third or a fourth?

Mr. CROWLEY. Then you would be getting into an unlimited liability. Congressman Goldsborough only wants to give the Corporation the right to call for an additional assessment in any one year.

Here are the types of bank from which you would get your objections. There is the fellow who does not want any supervision at all.

Then, there are the fellows who feel that they do not want to contribute anything to general banking recovery or the reestablishment of confidence. In other words, they are willing that the other fellows should reestablish this confidence and feel that they will benefit by it as they have in the past. There are a great many business men who will not join trade associations. They want the other man to rebuild by his efforts and want to reap the benefits they have not helped to bring about.

Other banks are afraid of the cost of this thing. They are not in sympathy with the plan.

Now, my answer is this: The man who does not want it on account of the supervision is the man whose depositors need the protection. The man who is unwilling to come in and assist in rebuilding the banking system should be compelled to do it.

And the larger banker, who believes that he can live by himself, if he will only analyze what happened to him in 1933, will realize this: When we have trouble in the Northwest, that disturbance will gradually work east, and, at some time or other, may result in the breakdown of the banking system.

So, I say, if we could pass a law that would compel every bank in this country receiving deposits to become a member of the Federal Deposit Insurance Corporation, that would be the greatest contribution that you could make; and, when that was done, the Corporation should be given powers that would enable them to protect themselves.

Mr. HOLLISTER. I agree with you 100 percent.

Mr. CROWLEY. If we can build up this thing and get the depositors to take the position that they will only do business with a bank that has deposit insurance, then we will have gone a long way toward correcting the evils in our banking system.

Mr. GIFFORD. In line with what Mr. Hollister has said, there are, in my section of the country especially, a very great number of mutual savings banks, who are doing a very safe banking-deposit business, and who look with a great deal of concern on this proposition that they have got to insure the deposits in other sections of the country, where the banking is weaker. They do not look with very much feeling of happiness on the prospect that they will have to pay the losses on weak and improperly managed banks in other sections.

Mr. CROWLEY. What State do you come from, Mr. Congressman?

Mr. GIFFORD. It is my good fortune to come from the wonderful State of Massachusetts.

Mr. CROWLEY. Well, you have had a pretty good banking system in your State, but we have 47 other States; and I think it has been proven in the past that no State can live by itself. We are trying to take a national viewpoint.

Mr. GIFFORD. I am not opposing your viewpoint, but I am trying to reflect to you the feeling of those bankers in the United States who feel that they have a pretty good—let me discuss this a moment off the record.

Are the Massachusetts mutual savings banks under this?

Mr. CROWLEY. No; they are not.

Mr. GIFFORD. Why are they not under it?

Mr. CROWLEY. They have a fund of their own.

Mr. GIFFORD. Do you say that is improper?

Mr. CROWLEY. I do not believe that any State fund that we have analyzed up to date is successful or sound. I think that under any crisis it would not be a success.

Mr. GIFFORD. Will you explain to the committee, to save me from having to explain it further, why it is that the mutual savings banks of Massachusetts prefer to insure themselves rather than to come under this Federal deposit-insurance plan? Tell the committee what you found to be their condition.

Mr. CROWLEY. Well, in the first place, you have 2 State deposit-insurance funds in the East. You have 1 in New York and you have 1 in Massachusetts. Now, neither one of those funds, in our estimation, are insurance funds at all, because of the fact that, by their very nature, they are insuring in a limited area. If banks in those systems had any loss of any great size, they would have to assess one another. They have no capital structure to speak of and they would have no way of paying out losses if they were to have any large demand upon them.

Secondly, mutual savings banks have restricted withdrawals as demands became heavy.

That is what has happened in your mutual savings bank systems, and that is why your mutual savings bank losses are less than the losses in the commercial field, because they restrict their withdrawals. That is the reason why in Massachusetts they have a fund that they call the insurance fund, but which, in realty, is not a fund that will stand analysis as to its soundness.

Mr. GIFFORD. Now, will you answer my question? What reason have they given you for their refusal to join the Federal Deposit Insurance Corporation?

Mr. CROWLEY. The only reason we have from Massachusetts is that they have a fund of their own.

Mr. GIFFORD. And you challenge that fund as not being a sound fund?

Mr. CROWLEY. Correct.

We have made analyses of the funds set up in the past. The outcome of a great many of them has been disastrous, because you cannot have adequate insurance where the banks are going to insure each other in such a limited area. It is just unsound.

The CHAIRMAN. Is not this the fact about it: Any insurance system for success depends upon a spread of the risk?

Mr. CROWLEY. That is correct, Mr. Chairman, you must also have an adequate capital structure.

The CHAIRMAN. Well, not necessarily a capital, because we have mutual insurance systems, do we not? Mutual insurance is really the cheapest system of all, is it not, for the simple reason that it does not require any capital structure? They simply pay what losses they have when they occur, and there is no waste. Is not that the mutual plan?

Mr. CROWLEY. That is correct; but I much prefer having a reserve that you can fall back on. You should not have to fall back upon special assessments for ordinary losses.

The CHAIRMAN. I am not speaking about that, but I am just speaking about the principle of insurance; and the mutual insurance is the cheapest insurance there is, if you acknowledge the liability and propose to make good.

In connection with what Mr. Gifford has said, our history shows, does it not, that the attempts to set up insurance systems for deposits in the several States have failed?

Mr. CROWLEY. Yes.

The CHAIRMAN. Because of the fact that the units were too small?

Mr. CROWLEY. That is right.

The CHAIRMAN. You do not have now an epidemic of yellow fever all over the United States, like we used to have in certain centers. The same principle is illustrated by the San Francisco fire. Now, in such cases the losses are absorbed by diversifying?

Mr. CROWLEY. That is correct.

The CHAIRMAN. And what you are doing with the banking system under the Federal Insurance Deposit Corporation is for the purpose of protecting the depositors by spreading the risk throughout the country?

Mr. CROWLEY. That is right.

The CHAIRMAN. This happened, did it not, Mr. Crowley, during the period of distress: The mutual savings banks and the big banks and everybody else ran to the Federal Government, with their hands up for assistance?

Mr. CROWLEY. Except Massachusetts. The mutual savings banks in Massachusetts did not.

Mr. GIFFORD. I want to challenge the chairman's argument. Massachuetts and New England claim that within themselves they have that greatly diversified situation, where they can invest in those diversified things, while in those great agricultural areas they are limited in the investments they can make to a certain kind of investment only. So it does not mean solely geographical diversification.

Mr. CROWLEY. Mr. Congressman, let me say this to you: I am awfully sorry this discussion has gotten down to districts or regions, because it is rather embarrassing, but your Massachusetts and New England mutual savings banks made the same mistakes, the same proportion of mistakes, perhaps, as the banks in other parts of the country.

Some of your New England banks went out into the Northwest and Southwest for investment in mortgages. They were looking for larger yields. They were looking for 8 or 10 percent returns on farm mortgages; and, naturally, now they have a large percentage of assets that——

The CHAIRMAN. They went into the Southeast and Southwest, too, as well as the Northwest.

Mr. CROWLEY. A very large percentage of their bonds are not productive of income.

Mr. GIFFORD. I challenge that statement also.

The only trouble with our mutual savings banks in Massachusetts was that they had over 7 percent, which was their legal limit; and I will say to you, as to our mutual savings banks which were closed up, that there was an edict went forth from Washington——

Mr. CROWLEY. Do you mean to say that the mutual savings banks could have continued right on paying without any restrictions?

Mr. GIFFORD. Oh, no; they would have to go on for 3 months. In fact, there was an order received by them to withhold deposits.

Mr. CROWLEY. I cannot go into the details of that; but let me say this——

The CHAIRMAN. Let me interrupt you. It should be said right here—and I do not say this in criticism or unkindness—the fact remains that big banks, railroads, and even life-insurance companies, finally came to the Federal Government for a place of refuge and for assistance; and the Government had to open up the Treasury of the United States in order to enable them to carry on. That is the record, is it not?

Mr. CROWLEY. I do not pretend to know much about insurance. But I do know that, with very few exceptions, the banks, the mutual savings banks, and all of them, were very happy to have the pressure taken off on March 6, 1933; and that, perhaps, while they will not directly say this, yet a lot of them have benefited more by having had Federal deposit insurance than, perhaps, they will admit.

Furthermore, Mr. Congressman, in reference to the banks taking aid from the Reconstruction Finance Corporation, it is true that in the very beginning a few banks did take capital aid from the Reconstruction Finance Corporation to be helpful; but the vast majority needed every dollar they could get from that source. If it had not been for the R. F. C. and the F. D. I. C., your banking system never could have recovered. There was nowhere else that the banks could go to get the capital aid which was necessary.

And I may add a little off the record.

Mr. FORD. Would not this little couplet apply:

> When the devil was sick, the devil a monk would be;
> When the devil got well, the devil a monk was he.

Mr. CROWLEY. Yes.

Mr. GIFFORD. That little pleasantry does not cure the situation.

Now, I ask sincerely, if the mutual savings bank does not join the Federal Deposit Insurance Corporation, there is a reason for not doing so and there must be a fear of the thing? New England has a feeling that no matter what the Federal Government does, we will pay very greatly in excess of what we ever get; and I think it is right to bring out here that, if they have that fear, there is a real foundation for it.

Mr. CROWLEY. Of course, Mr. Congressman, there are always bound to be differences of opinion as to questions of that sort.

The CHAIRMAN. Mr. Crowley, I want to ask you another question. You gave us yesterday an estimate of the burdens that would have been necessary to meet to take care of the losses to depositors in commercial banks during the 70-year period since the passage of the National Banking Act; and you gave us the comparative losses as between national banks and State banks.

The fact is that until recently there have not been many serious efforts at strict regulation and supervision as to State banks?

Mr. CROWLEY. That is correct, sir.

The CHAIRMAN. It is a fact, however, that in most of the States now we have developed systems of regulation and supervision that represent marked improvement and progress.

Mr. CROWLEY. Well, I think that there has been considerable improvement in the supervision of the State banking systems; but in many respects there is still a long way to go.

The CHAIRMAN. That is what I am asking you. It is a very different story from what it was during the first 50 or 60 years of our banking experience; so that same condition would not be reflected in the future?

Mr. CROWLEY. I think that is correct, Mr. Chairman.

The CHAIRMAN. It could not be. Now, I want to ask you another question. You estimated in that statement, as I remember it, that one-third of 1 percent would have taken care of all the losses, for banks of all types, during that 70-year period; and that one-eighth of 1 percent of the deposits would have covered all losses, exclusive of periods of panic.

Mr. CROWLEY. That is right.

The CHAIRMAN. Those figures, of course, are based upon operations which were, in the first place, without effective supervision—certainly as to the State banks?

The CHAIRMAN. And without modernized regulation as to the national banks?

Mr. CROWLEY. That is correct, Mr. Chairman.

The CHAIRMAN. And they also represent the experience of a period during which there was no insurance of deposits.

Mr. CROWLEY. That is correct.

The CHAIRMAN. So that, for the future, great allowances should be made for the improvements we have made in regulation and supervision and, also, for the operation and effect of successive deposit-insurance funds, should there not?

Mr. Crowley. That is correct, Mr. Chairman.

The Chairman. Now, what is the percentage of losses since the effective date of deposit insurance, as to banks that have been insured?

Mr. Crowley. To answer your question will take quite a little figuring. We had some thirty-six billions in deposits and we have had $2,847,000 of deposits in closed insured banks. It will take quite a little figuring to get the exact percentage of loss in insured banks.

The Chairman. The losses will be $356,000, will they not?

Mr. Crowley. Yes.

Mr. Reilly. Well, certainly no one anticipated those losses, with the exception of the activities of the Corporation, so that, as far as I am concerned, the amount of the losses which have accrued up to this time do not afford at all a basis for the actuarial experience required in order to estimate what the assessments should be.

The Chairman. I agree fully with that.

Mr. Reilly. Let Mr. Crowley take just a minute on that question.

The Chairman. I want to ask you another question.

Mr. Reilly. I want him to answer my question.

Mr. Crowley. Mr. Congressman, perhaps I had better make sure what you have in mind. You asked me what question?

Mr. Reilly. I asked whether the amount of the losses that have accrued up to this time, since the inauguration of the Federal insurance system, afford any adequate basis for establishing the actuarial experience required to estimate what assessments will be required.

Mr. Crowley. I get it now.

It is quite true that we should not have had, and we have not had, normal losses yet. But the success of this Corporation depended upon the rebuilding of your banking system. If that had not been done, you would have had no Federal Insurance Deposit Corporation, because the demand would have been so great that the Corporation would have become insolvent and you could not have reestablished confidence.

Now, I do not believe that for some time the banking system of this country has been in better shape than it is today, and that means that we are starting out on quite a clear basis, Mr. Congressman. I think that the income should be determined by our experience of the past, so that we may build reasonable reserves for the future.

Mr. Goldsborough. I am in accord with your statement, but, in view of the fact that in these other estimates of percentages, which we are undertaking to bring down to date, we have our experience recorded in figures, I think that the picture should be completed by giving the percentage of losses by totaling the deposits since the Federal Insurance Deposit Corporation Act became effective. If you have not those figures now, you may insert them in the record. I realize that they may require considerable calculation; but let us complete the picture.

Mr. Crowley. Mr. Congressman, will you take my statement and turn the pages to the chart entitled "All Commercial Banks, 1865–1934."

Mr. Goldsborough. Let me make a suggestion. We have been over all of that. All I want is that you take a pencil and figure out this percentage of losses for the record, so that the figure will be available to us. You can do that. All I want is to have those figures in the record to complete the picture.

Mr. CROWLEY. We will put that in the record for you.

(See p. 27 of hearings of Feb. 28.)

Mr. WILLIAMS. Is it not a fact that prior to the bank-failure epidemic, prior to this panic, that bank losses were very nominal throughout the history of this country?

Mr. CROWLEY. You mean after the washing-out of the weaker institutions?

Mr. WILLIAMS. No; I mean beginning before this panic, that the bank failures for a period of 25 or 30 years had been practically nominal?

Mr. CROWLEY. They have always been reduced after such periods. It is just like anything else; you wash out your weaker people; you have losses and have destitute people in the community. That same thing is true in the effect of the recent readjustments.

Mr. WILLIAMS. Do you have any figures of the losses to bank depositors in national banks from the beginning?

Mr. CROWLEY. Will you please answer that, Mr. Thompson?

Mr. WILLIAMS. I refer to the national-bank situation.

Mr. THOMPSON. We estimate that the losses to depositors will amount to about $1,000,000,000. We can only give you a figure that is partly estimated, inasmuch as the liquidation of the banks that are still in the hands of receivers has not been completed. We have had to take the value of the remaining assets and estimate what the total recoveries will be.

Mr. WILLIAMS. What proportion was the wash-out you spoke of, of the banks that did not reopen? What percentage of the banks closed have been allowed to reopen?

Mr. CROWLEY. Do you mean what percentage did not reopen, Mr. Congressman?

Mr. WILLIAMS. You know, we have overdrawn this matter of bank failures, stating that the banks immediately after that time should make such a remarkably good showing and then, in the next breath, saying that they were in an awful condition.

Mr. CROWLEY. The thing that has happened to your banking system has been the rebuilding of confidence and, also of capital structures. For instance, the Reconstruction Finance Corporation has invested $1,000,000,000 in the capital structures of banks and, in addition to that, there has been, I presume, four or five hundred million dollars in local contributions to capital structure.

Mr. WILLIAMS. Oh, I know there has been a lot of this overdrawn—this scare that the banks were in such terrible condition.

Mr. CROWLEY. What was the capital structure of all the banks in the country? About $6,000,000,000 on June 30, 1934. I think you will find that, with everything that has been contributed, there has been, perhaps, a billion and a half dollars, or over, put into the capital of our banking system since 1933. This has been used chiefly to write off losses rather than to increase the book capital of the banks.

Mr. WILLIAMS. But weren't there a lot of these banks that, if they had been let alone, could have worked themselves out?

Mr. CROWLEY. There are always banks which, if let alone, might be able to work themselves out.

Mr. GIFFORD. Now, we in New England, let alone, we are working ourselves out.

Mr. CROWLEY. The assets are improving, Mr. Congressman, all the time.

Mr. WILLIAMS. Right in that connection, while they are talking, Mr. Chairman, how many of these banks altogether opened up without any assistance? Most of them were able to open after what we called the bank holiday. How many of them opened, what proportion of them at least, opened without help from some source?

Mr. CROWLEY. There were 15,000 banks, Mr. Williams, and between five and six thousand have been given aid by the Federal Government; and that does not include some banks that have made their own contributions to the reestablishment of capital structure.

Mr. WILLIAMS. I was wondering if you had the figures of those banks whose capital structure was built up by local capital, independently of the Government.

Mr. CROWLEY. I do not think we have that figure; but we are assembling it and will have it soon.

Mr. WILLIAMS. The question that I was interested in was from the other end of it. You might say what was the number that were able to reopen without any help.

Mr. CROWLEY. I would say possibly 50 percent, Mr. Congressman.

Mr. BIRDZELL. May I make this contribution, further, to complete that thought? Many of the reorganized banks have been capitalized quite largely by their depositors, through waivers of deposit liability or the conversion of deposit liability into preferred stock, or something of that kind, so that some of the banks that were reopened in reorganized fashion really had depositors' losses included in their capital.

Mr. WILLIAMS. Yes; but that is the same thing as building up their capital structure through local contributions.

Mr. GIFFORD. The banks in my section all reopened, but, after the reopening they were forced to create a larger capital structure simply to mark off temporary losses that represented merely temporarily decreased values, and many of these 5,000 banks that they talk about having had Government aid got money from the Reconstruction Finance Corporation that they did not need at all, just to allay the fears of the people.

Mr. CROWLEY. You mean by that, Mr. Congressman—what do you mean when you refer to "temporary losses"?

Mr. GIFFORD. Well, our banks claim that the bank examiners were so severe that they demanded mark-downs or charge-offs of so much that they have to have a larger capital to offset that.

Mr. CROWLEY. Do you mean that they made them take out bond depreciation and things of that nature?

Mr. GIFFORD. I know of particular real-estate matters where the examiners required mark-downs for temporary losses.

Mr. WILLIAMS. Let me ask this question in that connection: In the temporary fund that is now established for nonmember banks, what percentage of those banks that are in the fund were permitted to come in without building up and strengthening their capital structure?

Mr. CROWLEY. The national banks and State member banks, you understand, came in automatically.

Mr. WILLIAMS. That was not the question. I asked about the nonmember banks. Were they permitted to come in without building up or strengthening their capital structure?

Mr. CROWLEY. We have some 8,000 nonmember State banks, and we have rebuilt or have in process of rebuilding close to 4,000 of these banks.

Mr. WILLIAMS. In other words, only half of them were able to come in without rebuilding their capital structures?

Mr. CROWLEY. That is right.

Mr. CLARK. Following out that line of inquiry: you said that 50 percent did not need help to reopen because of the confidence the public had in them. Isn't that correct, that a large part of them had to have help because confidence had to be reestablished, rather than the financial structure? If everyone had reopened automatically and the public had been in the frame of mind it was just before the holiday, there is no way of knowing what percentage of the 50 percent could have withstood the shock?

Mr. CROWLEY. The first thing you had to do was to reestablish confidence.

Mr. CLARK. And then, after you did that, 50 percent could reopen; and in 1933 we had approximately 6 billions of capital in our banking structure?

Mr. CROWLEY. That is correct.

Mr. CLARK. And there were approximately 31 billion dollars that we set up in the form of liquid assets. That made a total collectible, assuming the capital was sound, of 37 billion dollars and there were 57 billion dollars of deposit liabilities. That left 20 billion dollars actually frozen.

Now, had those banks at that time had the rediscount privilege, of taking a large part of their frozen assets to some place where they could have gotten money on them, as a matter of fact, we would not have had much more than 5 billion dollars of frozen stuff in the banking system.

Just roughly and approximately, how close is that to correct?

Mr. CROWLEY. Of course you would have been able to have postponed this thing by loaning the banks money.

When the Reconstruction Finance Corporation was originally set up it was with the idea of lending money to the banks in order to meet that withdrawal. But the way it worked out, on account of the whole economic crash, it in reality only preferred one depositor over the other. When the banks finally did have to close the assets of many of them were pledged for bills payable, and the depositor who was an unsuspecting individual was left with the frozen assets.

There is only one thing that rediscount is good for; that is, to take the place of liquidity; but it can never take the place of soundness.

Mr. CLARK. I understand that; but the terrible crash might have been held off.

Mr. CROWLEY. You might have carried it along for a while; but throughout the whole economic system the values were shrunk so much that the assets in fact were not there. You might have had all the rediscount privilege that you wanted; but, if you did not have the values there, it would not have prevented the crash. At best you would merely have deferred it.

Mr. WILLIAMS. If they had had a chance to rediscount this paper on real estate and other securities that ordinarily are good securities, would not that have kept the values from shrinking, the fact that they had that privilege?

Mr. CROWLEY. You mean the forced liquidation that forced values down?

Mr. WILLIAMS. Yes.

Mr. CROWLEY. That always has a tendency to force values down.

The CHAIRMAN. Gentlemen, we cannot finish today, and we want to put other witnesses on the stand to go over the technical features of the bill; and I have an idea that we might meet again about Tuesday morning and resume this discussion, and unless there is something to interfere with that we will adjourn.

Mr. BROWN. I would like to just get a little more information on section 8.

In your statement, Mr. Crowley, you said that a rate of approximately one-third of 1 percent would cover all losses that have occurred during the past 70 years to depositors. What I am interested in is this: How do you arrive at one-twelfth of 1 percent as being an adequate figure? I assume, of course, that you take into consideration the fact that you are speaking of all losses on page 19 of your statement; whereas, in the bill, in your recommendation, you are speaking of losses on deposits of $5,000 or under. But is a rate of one-twelfth of 1 percent adequate in view of the experience of the past 70 years?

Mr. CROWLEY. I do not think that the banking experience of the past 70 years is necessarily a fair criterion, for the reason that I do not believe this Government should assume the responsibility of the supervision of the banks if our system should be the same as it was throughout the last 70 years.

In other words, I do not believe that our banking system is correct if we are going to have the same proportionate amount of losses as in the past.

Now, we will not have those losses if we do not let our banking system build back to that 30,000 banks again. One of the biggest defects in our banking system has been that we have had too many banks, and we have had a great many banks that could not employ the proper kind of management.

We arrived at the one-twelfth of 1 percent in this way: we do not believe that one-twelfth of 1 percent will build large enough reserves for the Deposit Insurance Corporation for the future, but the earning capacity of the banks right now is very low. We are interested, first, in the banks having sufficient income themselves so that they may take their losses currently and so that they may build reserves for the future. That is the greatest protection to the Deposit Insurance Corporation.

I would rather give up 50 percent of our income and have the proper supervisory powers than to have $5,000,000 or $10,000,000 more income and not have the proper supervisory powers. I think the success of this thing comes back to, first, the proper safeguards for this corporation to protect itself. The banks must pay a fair share of this income. A contribution from other sources to help to build our reserves might be considered.

Mr. BROWN. Assuming that we are unable to improve the banking system, then what, based upon the experience of the last 70 years, should the rate be in order to be adequate? In other words, what percentage would it have to be to cover losses up to $5,000 deposits, on the basis of the experience of the past 70 years?

Mr. CROWLEY. Take out, if you will, those last 4 years.

Mr. BROWN. Yes; take those out.

That is, for all banks.

Mr. CROWLEY. One-eight of 1 percent will take care of all deposits except those in banks which closed during the years of banking crises.

Mr. BROWN. No. That is for all deposits. That is not for the deposits of $5,000 and under.

Mr. CROWLEY. It is one-tenth of 1 percent for the deposits of $5,000 and under.

Mr. BROWN. That is one-tenth of 1 percent instead of one-twelfth of 1 percent?

Mr. CROWLEY. That is right.

Mr. BROWN. It strikes me that your figures are very reasonable.

Mr. CLARK. I do not want to go back to your original point, but I wish that Mr. Crowley would be so kind as to confer with his associates and, when he comes back Tuesday, tell us if he would have any objection to such an amendment as Mr. Goldsborough proposed and which was mentioned for discussion, whereby, in addition to the fixed liability at one-twelfth of 1 percent, the Deposit Insurance Corporation might, at any time when, in its discretion, the Corporation decided that it was necessary, levy an additional assessment of one-twelfth of 1 percent in any one year.

Frankly, I want to go along with the Corporation just as far as I can, because of the views that I have expressed, and I would like to know, at your next appearance here, whether your Corporation would or would not be interested in the amendment proposed by Mr. Goldsborough.

(Thereupon, at 12:30 p. m., the committee adjourned until Tuesday, Feb. 26, 1935.)

BANKING ACT OF 1935

TUESDAY, FEBRUARY 26, 1935

House of Representatives,
Committee on Banking and Currency,
Washington, D. C.

The committee met at 10:30 a. m., Hon. T. Alan Goldsborough presiding.

Mr. Goldsborough. The committee will come to order. Judge Birdzell, Mr. Steagall is out of the city this morning, which is the reason why I am occupying the position that he usually occupies.

Judge Birdzell, you will proceed in your own way, please; and it seems to me that it would be better for you to complete your statement, and if it is agreeable to the members of the committee, we will have it that way.

Mr. Williams. I think that that would be the most satisfactory way of handling it, the more orderly way.

Mr. Goldsborough. All right, Judge.

STATEMENT OF L. E. BIRDZELL, GENERAL COUNSEL, FEDERAL DEPOSIT INSURANCE CORPORATION

Mr. Birdzell. Mr. Chairman and gentlemen of the committee, we have reached a stage in the insurance of bank deposits where we contemplate going onto a permanent basis, and we are at some advantage now in planning for permanent deposit insurance because we have had more than a year's experience with deposit insurance under the provisions of existing law, which provided for temporary insurance.

We thought that we would be remiss in our duty if we did not bring to your committee all of the information that has become available to us by reason of our experience with the temporary plan; and we thought, too, that we would be remiss in our duty if we did not bring to you gentlemen suggestions for legislation which in our opinion will improve the plan for permanent deposit insurance as outlined in the Banking Act of 1933.

In all of our consideration of the matter, we have been brought repeatedly to the conclusion that Congress planned wisely in planning for permanent insurance, and when you consider the conditions in which the permanent insurance provisions of the Banking Act of 1933 had to be framed, frankly we marvel at the completeness of the plan that was written into that law.

I have circulated to the members of the committee a parallel print containing in one column the proposed act as contained in title I of the proposed banking act of 1935, and in another column the provisions of the existing law.

If you have read that print carefully and made comparison, I think you will be impressed with the fact that we have followed very closely the plan of the existing law in outlining a plan for permanent insurance in the proposed law. There are places where it would seem that we had taken out of the existing law subsections and completely rewritten them, but if you will follow the text in the instances where that appears to have taken place, you will find that, after all, we have followed very closely the ideas as they were expressed in the existing law.

I want to tell you very briefly why we considered that it was necessary to make the number of changes that are proposed to be made in this proposed act. In the first place, when we consider this legislation we must consider it from a historical standpoint. The deposit-insurance features of the Banking Act of 1933 were features that were written into a bill that was under consideration prior to that time, known as the "deposit liquidation act." It provided for a deposit liquidation-corporation, which was to be capitalized by a Federal Government subscription, and also by subscriptions to the stock of that corporation by the banks which were members of the Federal Reserve System. That corporation was to be authorized to loan money upon the assets of closed banks, and to purchase the assets of closed banks, the primary purpose being to provide for the liquidation, and speedy liquidation, of those banks in the interests of the depositors.

Upon that structure was really superimposed the provisions for permanent deposit insurance. That act had contemplated application only to Federal Reserve member banks, and consequently when the insurance features were added, it was at first contemplated that only Federal Reserve member banks would be insured. Later the provision was made for extending the insurance to nonmember banks voluntarily; that is, they could come in by voluntary application.

It was contemplated that a deposit liquidation corporation could be conservatively operated, and consequently it would be in a position to make money—that is, it would make a fair return upon the capital employed in that particular business. Consequently provision was made that it should pay to the Federal Reserve member banks a dividend on the capital thus employed.

I think, gentlemen, that you will probably agree that if you were considering a corporation to insure deposits in banks generally, and limited to that, at the expense of the banks, or at cost to the banks, that you would not have had in mind any provision for dividends on the stock that would be purchased by the banks in that same corporation, because they would get the benefits of it automatically as the costs were kept down.

So the dividend provisions of that act are not strictly applicable to a corporation that limits its functions to the insurance of bank deposits.

Since that act was intended to apply to banks which are members of the Federal Reserve System, and since permanent insurance was provided according to a certain schedule whereby all deposits would be insured in some amount—you are familiar with the schedule; $10,000 insured 100 percent, up to $50,000 insured 75 percent, and above $50,000 insured 50 percent—provision was made in that law for subrogation rights of the corporation in case it went in and paid off a closed bank, paying out to the depositors according to that schedule, and that law provided that if the corporation paid off the depositors in the closed banks, the corporation should succeed to all of the rights of the depositor against the closed bank.

So, you see, the corporation would enjoy the right to subrogation to the extent of all of the claims of depositors against the closed bank.

Now, during the progress of the passage of that law there was added to it, as you know, subsection (y), which provided for the insurance of bank deposits in a temporary fund which should be operative prior to the time when the permanent plan would become operative, and that insurance was limited to $2,500, and subsequently increased to $5,000.

There was no change made with respect to those provisions of law embracing the rights of the corporation to be subrogated to the rights of depositors upon paying off, but I think you will agree with me that a subrogation provision that gives to the corporation the right to be subrogated to the entire claim of the depositor against the closed bank, where all of his deposit is insured to some extent, is not appropriate and should not be applied where we are only insuring his deposit to a limited extent, as $2,500 or $5,000.

So it was necessary to change the subrogation provision of the existing law. In fact, you gentlemen may remember that in the act passed last June, provision was made for changing that subrogation feature, and it was approved by the House, but, unfortunately, it was stricken out in the conference, and never became a part of the law. I indicate that history to you, that we have deposit insurance superimposed upon a corporation originally intended to be a deposit liquidation corporation. I give you that history so that we may better have in mind the necessity for some changes if the functions of the corporation are to be limited to insurance, as we think they should be.

You gentlemen may recall that last year, when the extension of the temporary plan was under consideration, the Corporation was pointedly asked by gentlemen on this committee why it had not exercised its functions as a liquidation corporation, because both functions were expressed in subsection (a) of that bill, and you will recall that the Corporation presented to your committee, I think, satisfactory evidence that the liquidation function, so far as the banks were concerned, was being performed quite satisfactorily by the Reconstruction Finance Corporation. All of the money was being advanced on the strength of the assets that it was thought could be advanced upon a sound basis, but to make assurance doubly sure your committee recommended the amendment of the Reconstruction Finance Corporation Act, which would authorize that Corporation to proceed with liquidation loans upon a more liberal basis than it had in the past, and the recommendations of your committee became a part of the law.

So that the liquidation end, as applied to banks that had already closed, is practically taken care of now by the Reconstruction Finance Corporation, and for that reason subsection (a) has been changed by the omission from it of that language which was especially applicable to the function of loaning money to member and nonmember banks that had closed for the purpose of making those funds available to depositors.

Now, I do not know in what manner you gentlemen may desire to consider this act; that is, whether you want now to take the time to go through it section by section, but I can very briefly, I think, indicate to you the main changes that have been made, and then I will be very much pleased if I might be of any further assistance to the committee by way of answering any questions that may occur to you.

I just explained the reason for the omission in subsection (a) of the provisions relating to the loans to member banks.

Mr. SISSON. What section is it you are referring to?

Mr. BIRDZELL. That is on the first page, subsection (a).

The next section deals with the management of the Corporation, and is changed in one respect. Our Corporation is operated by a board of three directors. The Comptroller of the Currency is one director. The Chairman of the Corporation spends all of his time directing the affairs of the Corporation, and frequently the Comptroller may be at some remote part of the country when it is necessary to have a meeting of the board; and in order to have a quorum, it is sometimes necessary to wait until the Comptroller's return or, possibly, call in the Deputy Comptroller.

Sometime ago I furnished to the board of directors an opinion to the effect that in the absence of the Comptroller the Deputy Comptroller could function, but that opinion is based upon inference, and it ought to be provided expressly in the law that in the absence of the Comptroller a Deputy Comptroller may function in his stead as a member of our board.

The remainder of what material you find on page 4 and page 5 consists of definitions, and those definitions have been made with a view to convenience in constructing the remainder of the act, to remove any ambiguity, and so forth. I think it is not necessary to point that out, except that that is all new matter, and it is there for the purpose of facilitating the drafting of the remainder of the act.

I do want to call attention to paragraph 11 on page 5, where we have defined the term "deposit":

> The term "deposit" means the unpaid balance of money or its equivalent received by a bank in the usual course of business and for which it has given or is obligated to give unconditional credit to a commercial, checking, savings, time, or thrift account, or which is evidenced by its certificate of deposit, and trust funds as provided in paragraph (5) of subsection (h) of this section, together with such other obligations of a bank as the board of directors shall find and shall prescribe by its regulations to be deposit liabilities by general usage.

Then there is a proviso which I am skipping here, and then it is provided:

> The board of directors may by regulation further define the terms used in this paragraph.

All that there is in the existing law by way of defining deposits is simply the use of the term "deposit." We have questions arising, for instance, as to whether or not the uncollected funds of a bank that on a given reporting day may amount to many hundreds of thousands of dollars in the case of a large bank are a deposit.

You are familiar with the fact that as items are deposited in a bank for collection they are deposited under an arrangement whereby, while credit is immediately given, that credit cannot be drawn upon until the item is completely collected. Is that a deposit as of that time or is it only conditionally a deposit?

We have seen fit to clarify that in this expression here by considering only the credits which have been made unconditionally.

Uncollected funds at any particular date are not a deposit liability, although it may be more or less appropriate that reserves be calculated on such funds.

For our purposes, the uncollected items are not considered deposits, and we thought it well to have that definition in the law, but we think that Congress cannot, in an enactment of this character, so define the term "deposits" as to cover every conceivable situation.

In the existing law we are referred to the definition of "deposits" according to the Federal Reserve Board. The Federal Reserve Board defines deposits for purposes of fixing reserve requirements. Under this provision, our definition of "deposits" may be independent of the definition of the Federal Reserve Board.

Take an item like cashiers' checks, for instance. If we said that a cashier's check is a deposit, maybe we would be imposing by definition artificially and arbitrarily on given types of transactions. If a bank issues its cashier's check to pay its rent, for instance, the one to whom that check is issued may have no account in that bank at all, and the account upon which it is drawn is the account of the bank itself. There is no reason why a cashier's check given for a purpose like that should be considered a deposit liability.

When it comes to paying off the deposits of a bank, a cashier's check, however, may be purchased by a depositor and used by him the same as he would if he had purchased a draft. In that event, that type of cashier's check should be considered a deposit liability upon the closing of the bank and also for purposes of assessment. I give you that merely to show you that it is necessary to have some leeway for the board of directors to define deposits within the terms of the law, and it would be extremely difficult to put all of the definition into an act of this sort.

Mr. Wolcott. You say in this provision: "The board of directors may by regulation further define the terms used in this paragraph."

Do you not think it would be better to qualify that to the extent that you just mentioned?

Mr. Goldsborough. Would it be feasible for you to defer that inquiry until he gets through with his statement?

Mr. Birdzell. Do you want me to answer that?

Mr. Wolcott. No; go ahead.

Mr. Birdzell. The next change that I would call your attention to is the change that you will find on page 8.

Under the existing law, it is the duty of the Comptroller of the Currency, in the case of national banks and of the Federal Reserve Board in the case of the Federal Reserve member banks, to certify those banks as being solvent in order to qualify them for membership in the permanent fund.

In view of the work that has been done by way of building up capital structures, and in view of the character of supervision of the banks in the national bank and Federal Reserve system, we have thought that that provision is now altogether unnecessary. However appropriate it might have been if this act had been put into effect a short while after the banking holiday, we think it is no longer necessary, and so all banks which are members of the Federal Reserve System now come into the fund without any further certificate on the part of the Comptroller or on the part of the Federal Reserve Board.

The State banks, nonmembers of the Federal Reserve System, that are now members of the fund, likewise come in on the strength of the examinations previously had and on the strength of their membership in the temporary fund.

Under the existing law, the nonmember banks, to qualify for membership in the permanent funds, would have been required only to have subscribed for stock. In the new set-up, since we are not providing for any dividends on stock—we are not providing for bank ownership of stock at all—they come into the permanent fund automatically.

Then, with respect to banks coming in subsequently, if a bank be not a member of the Federal Reserve System, if you will look on pages 8 and 9 you will find that provision is made for banks which are not members of the system to come in, and as to national banks which may not be members of the fund, they come in on the same basis. National banks which are not members of the temporary fund are national banks located in the Territories, for instance, in Hawaii and Alaska. These are national banks which are not members of the Deposit Insurance Corporation and not members of the Federal Reserve System.

Mr. HOLLISTER. Did you not skip new matter on page 6? You are taking this up consecutively, are you not?

Mr. BIRDZELL. Yes.

Mr. HOLLISTER. You were discussing the definitions ending up on page 5. Did you not skip all of that matter on page 6, with respect to the capital stock?

Mr. BIRDZELL. Did you have something that you wanted to inquire about on that?

Mr. GOLDSBOROUGH. May I say that Judge Birdzell exlained that he would just go over this in his own way.

Mr. BIRDZELL. I was only calling attention to some of the main features.

Perhaps I should say a word with respect to that change in the capital structure of a corporation.

Mr. HOLLISTER. I do not want to interrupt your flow of thought.

Mr. BIRDZELL. I think it is well to call that to your attention.

Mr. HOLLISTER. I thought that you might explain the whole thing as you went along.

Mr. BIRDZELL. Provision is made on page 6, at the bottom of the page, for doing away with the dividends on the stock, and a capital set-up is provided, whereby the capital stock of the corporation is treated as consisting of the shares subscribed for prior to the effective date. That includes the $150,000,000 subscription by the Federal Government, and the $139,000,000 subscription by the Federal Reserve banks. That stock is declared to be of nominal or no par value, and provision is made for the exchange or reissue thereof, and the consideration received for the capital stock may be allocated to capital and to surplus in such amounts as the board of directors shall prescribe, and such stocks shall have no vote and shall not be entitled to the payment of dividends.

The class B stock, the stock for Federal Reserve banks, was not entitled to dividends under the existing law, but the Government stock, the $150,000,000, plus the class A stock which would be subscribed for by the banks upon becoming members of our corporation, would be entitled to dividends, and those are the features that are changed.

The provision made for the allocation of the capital to capital and surplus is, we think, appropriate in view of the fact that these funds are supplied for the use of the Corporation for insurance purposes, and if a time should come when it would be necessary to utilize some of the surplus funds of the Corporation in meeting losses, we would not want the Corporation to be operating with an impaired capital, and that could be avoided through proper allocation.

Now, in making provision for the entry of new banks or newly applying banks into the Deposit Insurance Corporation, provision is made for the board of directors passing upon the qualifications of those banks for membership in the Corporation. That, we think, is a very necessary provision in the interest of having the Corporation function upon a sound basis. Through that, of course, reasonable protection ought to be given to the insurance funds of the Corporation.

A different test is laid down in this law from that laid down in the existing law. This law, as it will come into effect, we anticipate, much more than a year after the temporary plan started in operation, could appropriately provide that the banks have sound capital. The test of solvency laid down in the emergency period in the original act was a test of solvency for an emergency period where banks were permitted to insure their deposits without regard to the existence of a sound or legal capital structure.

If you will turn to page 9, in the middle of the page, paragraph 2, you will find this language:

> Before approving the application of any such State nonmember bank, the board of directors shall give consideration to the factors enumerated in subsection (g) of this section and shall determine, upon the basis of a thorough examination of such bank, that its assets in excess of its capital requirements are adequate to enable it to meet all of its liabilities as shown by the books of the bank to depositors and other creditors.

Likewise, the fore part of that deals with certificates by the Comptroller with regard to a national bank, and he must likewise certify to the Corporation with respect to a newly chartered national bank and the same factors are to be enumerated in the certificate that is to be given. These factors to be considered by the board of directors and the Comptroller are the financial history and condition of the bank, the adequacy of its capital structure, its future earnings prospects, the general character of its management, the convenience and needs of the community to be served by the bank, and whether or not its corporate powers are consistent with the purposes of this section.

That follows largely the provisions of the present national bank law with respect to the chartering of new national banks by the Comptroller of the Currency. Mr. Crowley has already explained in his statement the practical necessity for some such requirement as that.

The next section, or, rather, the paragraph on page 10, deals with the assessment. The assessment rate prescribed there is one-twelfth of 1 percent upon the total amount of liability of the insured bank for deposits, using the term deposits as used in the previous section, which I read to you a moment ago. That is based on the average at the close of business on the last days of June and December, and those dates are chosen by reason of the fact that there is always a call by the Comptroller of the Currency on those two dates. It is convenient, of course, to have the certificates to our Corporation based upon those same calls.

The assessment plan provided in the existing law should be contrasted with this. Under the existing law banks becoming members of our Corporation and insuring their deposits are required to subscribe for stock in the amount of one-half of 1 percent of their deposit liability. They must pay immediately one-half of that, which makes one-fourth of 1 percent on their entire deposit liability. Thereafter there are no stated payments to be made.

The obligation for further payments is expressed in this fashion: As the banks close, it is the duty of the Corporation to set up on its books an account wherein it will place the estimated debit balances. When any bank closes the Corporation is required to make an estimate of the ultimate amount of loss and that will be a debit balance. There is provision for the adjustment of that debit balance. Later on, if there is a greater loss than anticipated, more is charged to it; if there is less, a credit is given, and when the aggregate of those debit balances reaches one-fourth of 1 percent of the deposits in all of the banks that are insured, another assessment is levied of one-fourth of 1 percent.

So that the successive assessments under the existing law cannot be anticipated. An assessment would be made on the first of July of this year, and there might not be another one for 2 years, or there may be another one in 10 months.

Under this proposed plan an assessment is fixed at a certain figure. It is due at a certain time and the payments are to be made at a certain time.

Mr. DIRKSEN. Does the last portion of that subsection contemplate a different rate for mutuals than for other banks?

Mr. BIRDZELL. It contemplates giving to the Corporation the power to prescribe a different rate for mutuals. You gentlemen who listened so patiently during our hearings last year will remember that very frequently the question of how this proposal or that would affect mutual savings banks, and their attitude, came up. I remember that you listened very patiently one day to the president of the National Association of Mutual Savings Banks, and I think that we all became impressed at that time with the fact that mutual savings banks did create more or less of a problem in relation to any activity of this sort, and the problem is to deal with them in a way that is fitting to their particular function.

To illustrate, in the Banking Act of 1933, you made mutual savings banks eligible for membership in the Federal Reserve System, and yet I think that there are no advantages to be gained by membership in the Federal Reserve System that can be enjoyed by mutual savings banks when they become members of the System. I think that you gentlemen were generally impressed with that a year ago.

Furthermore, the type of investments of mutual savings banks, and the character of their supervision, have been such in this country that it has been asserted—I am not an economist and I am not asserting this in an authoritative way—but it is asserted by some that on account of limitations as to investments and on account of the character of supervision of mutual savings banks, and the type of business that they do, they are a favored risk. I am not saying that Congress ought to recognize that they are a favored risk from an insurance standpoint, but possibly, in view of their characteristics, it is proper to allow them to be considered in a class by themselves, separate and apart from commercial banks, and to give a limited discretion to a board that is constantly confronted with the problems presented from that particular group——

Mr. FORD. Might I make an observation there?

Mr. GOLDSBOROUGH. Mr. Ford, it was agreed when we began that we would postpone the question until he had finished.

Mr. BIRDZELL. The thought is that there are limitations with respect to the character of their investments that do not obtain with respect to commercial banks, and on account of that the mutual savings banks have argued that they have a more favorable experience than the commercial banks with respect to failures. I am not expressing any opinion as to whether or not the arguments of the mutual savings banks in that respect are sound. That is for the economists and the statisticians to consider.

There is one provision in that subsection dealing with the assessments that I want to speak of. That is on page 12 with regard to trust funds. You may have noted earlier that in defining "deposits" express reference was made to trust funds as elsewhere defined and provided for, and that reference is here on page 12.

We have found the banks quite concerned, and, of course, we have been seriously concerned, with the problem as to the protection of uninvested trust funds. Many national banks have trust departments. Many trust companies do a trust business exclusively, and some of the trust companies do both a trust business and a banking business. In the transaction of their business, there will be on hand at any given time a considerable volume of cash that will be uninvested. They say that that cash is trust funds, and not a deposit, but if a bank closes, I fear the situation would be the other way from the standpoint of the patrons of that trust company.

From the beginning we have required banks to report as deposits any amount of trust funds that were on hand and uninvested, because we felt that in the event of a closing we would be liable for those deposits.

Now, among trust companies, in doing their ordinary business, it is the practice of many of them to establish relations with commercial banks, so that they will deposit large amounts of money, uninvested trust funds, in those commercial banks. That relationship is not like the ordinary correspondent relation of one bank with another, one commercial bank with another, and, furthermore, in the event of the closing of a bank, that fund cannot properly be treated; that is, that particular kind of deposit cannot properly be treated as belonging to one depositor because it belongs to all of those who are patrons of the trust company and who under their various interests would be entitled to that cash.

So that we have provided here for the insurance on trust funds in a way that we think meets that situation. If a trust company be a member of our Corporation, and if in the transaction of its trust business it has idle funds which it places with some bank, that bank, being the bank where those funds are deposited, should report the entire amount of those deposits, and in the event of anything happening to the bank where such funds are deposited, we should look to the trust company, likewise a member of our Corporation, to establish a beneficial ownership of those various trust funds in that individual bank. Provision is made for the bank paying the assessment on those trust funds, and in event of the failure of a bank containing such funds, we will look to the various trust estates in the trust company to determine the ownership and extent of the claim that may be made on the closed bank.

I could outline that more in detail, but I think that that is enough to give you an idea.

Now, there is a discretionary power, or, rather, a power of a supervisory nature, expressed at the bottom of page 12, in paragraph 1 of subsection (i). It reads, in part:

> Wherever the board of directors shall find that an insured bank or its directors or trustees have continued unsafe or unsound practices in conducting the business of such banks or have knowingly or negligently permitted any of its officers or agents to violate repeatedly any provision of this section or of any regulation made thereunder, or of any law or regulation made pursuant to law to which the insured bank is subject, the board of directors shall first give to the Comptroller of the Currency in the case of a national bank or district bank, to the authority having supervision in case of a State bank, and also to the Federal Reserve Board in case of a State member bank, a statement of such violation by the bank for the purpose of securing a correction of such practices or conditions. Unless such correction shall be made within such period of time not exceeding 120 days as the Comptroller of the Currency, the State authority, or Federal Reserve Board, as the case may be, shall require, the board of directors, if it shall determine to proceed further, shall give to the bank not less than 30 days' written notice of intention to terminate the status of the bank as an insured bank, fixing a time and place for a hearing before the board of directors or before a person designated by it to conduct such hearing, at which evidence may be produced—

and so forth.

I read that to you to show you how the board proposes to secure corrections of dangerous practices in banks. In the first place, I call your attention to the fact that we do not deal directly with the bank. If we have a complaint as to the practices of a State bank, while we have a report of that bank, a report of the examination upon which the complaint may be based, we take that up with the State supervisory authority in an attempt to get a correction from there, but we are not altogether dependent for our protection upon the action of the State supervisory authority, for, obviously, if the correction should not be made, the Corporation ought not to be subject to the continuing hazard of the operation of that bank. So provision is made whereby the Corporation, after ample time for correction and after hearing, can terminate the relations of the bank with the Corporation.

Provision is made, of course, for the continuing protection of the depositors, even after the bank shall have terminated.

Mr. DIRKSEN. Is not 2 years a rather long time for that?

Mr. BIRDZELL. Possibly it is; it may be a little longer time than is needed, although we think we would rather err on the side of having the time too long than too short, because any law of this sort ought to be so constructed that it will deal absolutely fairly with depositors, and we can conceive of cases where depositors might not be able to obtain information with reference to the status of the bank within any short period of time.

I think that we can pass those provisions, for our present purposes at least, because this discussion is apt to become altogether too long.

There is one change that I would like to call attention to, on page 15, in the fourth paragraph, subsection (j). Provision is made there that when suits of a civil nature at common law or in equity may be brought in which the Corporation shall be a party, they 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 the Corporation as defendant in any such suit may, at any time before the trial thereof, remove such suit from a State court into the district court of the United States. That is for the purpose of securing uniform interpretations of any provision of this act of Congress.

There is a similar provision with respect to the Federal Reserve banks.

Another feature that perhaps I should have mentioned earlier, but it is appropriate to mention it here, is that the existing law was constructed upon the principle that apparently did not contemplate examinations of banks by the Corporation, because it was to be limited in the first instance to banks which are members of the Federal Reserve System. When Congress provided for the temporary insurance, in (y), it authorized the Corporation to examine the nonmember banks in order to admit them into the temporary fund, and it authorized them to examine those banks as often as it might deem necessary for its own protection.

Now that we contemplate a permanent insurance extended to nonmember banks, it is of course appropriate that there be an express provision in the permanent act authorizing the examination of banks, so that is provided for in the eighth paragraph, which enumerates the powers of the Corporation, where before it was contained in subsection (y). There is further provision made in paragraph 2, below that, on page 16.

Then, on page 17, there is express provision for access by the Corporation to the examinations made by the Comptroller of the Currency, and also to the reports of examinations of any Federal Reserve member bank.

There is one other provision that I want to speak of, on page 18, in subsection (1). If you would read the existing subsection (1) and the new subsection (1), you would find that they are practically the same, although on account of the other changes that had to be made with reference to stock; for instance, there were frequent references to banks which are class A stockholders, and that reference runs all through subsection (1), eliminating provisions for class A stock made it necessary practically to rewrite subsection (1), but the present subsection (1) is to all intents and purposes the same as the original. The language is much the same, with the exception that the subrogation right which I explained a moment ago is expressed differently in the proposed subsection (1). Upon paying the insured deposit liability to a depositor, we are subrogated only to that portion of his rights against the bank which he would have had by virtue of the deposit which we paid to him.

An illustration would, of course, make that clear. I have a $10,000 deposit in a bank that has closed. This Corporation can only pay me $5,000 on account of that deposit. What rights shall I give to the Corporation in order that I may get my $5,000 insurance? Shall I give the Corporation my rights arising on the whole $10,000, or only with respect to the $5,000?

Under the terms of this act that we are suggesting, I give my rights only to the extent of $5,000, and I retain the right to dividends as to the remaining $5,000. Under the existing law, I would have to give all of my rights to the Corporation in order to secure my insurance.

Then one other significant change is made with reference to the means of making available or the vehicle for making available the insured deposit liability to the depositors. We use a term here that we call a transferred deposit. We authorize a transferred deposit credit to be set up either in a new national bank or in any other insured bank in the locality, giving to the board of directors a discretion to utilize an existing bank in the community rather than to do the artificial thing of setting up a new national bank in the community. If the board does set up a new national bank, it is operated just the same as the new national bank would be operated under the existing law, and the board has the same discretion with reference to whether it shall receive deposits or not, with reference to whether it shall be capitalized or not, that it has under the existing law.

Now, the subrogation right that we speak of is expressed on the top of page 20, if you are interested particularly in that.

One further feature with regard to the pay-off provisions generally. Under the existing law, there is no limitation, apparently. We may find it difficult to find a depositor determined to make a claim. In fact, we have had to advertise already for depositors to come in in some instances and make their claims. We should not be subjected to a continuing liability. We step in at the closing of the bank, and we are ready and anxious to pay out the insured deposit liability in that community so that the community will scarcely realize that there has been a bank failure, but we ought not to be subject to a continuing liability of those who do no come in within a year's time and file claims with us.

So provision is made for a year's statute of limitations, and that does not mean, of course, that the depositor loses all of his rights if he does not come in and claim his share. He loses all of his right to insurance, but he still has his claim against the bank, and if we are the receiver of that bank, we will have to treat him the same as other creditors are treated.

Now, it seems to me that I have covered all of the principal changes.

Do you think of anything more that I ought to touch on, Mr. Crowley?

Mr. CROWLEY. I think that you might explain to them a little more in detail about this liquidation in pay-off, the reason we want to bring it in here, to shut off that expense.

Mr. BIRDZELL. Yes. Mr. Crowley reminds me of one change in connection with the pay-off feature that I should have commented upon, but which I omitted to mention.

Where, under the existing law, we set up a new national bank, there is just one thing that we can do with that bank, and that is to keep it alive for 2 years. To keep it alive for 2 years may involve a lot of useless expense. After that bank has served its purpose, and paid off 90, 95, or 99 percent of the insured liabilities in that community, we ought to be given discretion to fold it up and say to the people that have not come in, " You may present your claim at the district office of the Federal Deposit Insurance Corporation ", because we have offices in most of the Federal Reserve districts, or we ought to be able to say to them, " Present your proof to the head office of the Insurance Corporation." There is no need, in other words, of requiring that this bank shall be kept in operation for 2 full years, so provision is made here whereby as soon as the active period is over in that locality, if there is no further need for that institution there, we can deal with it in the manner that I have just indicated in the interest of reasonable economy.

Mr. HANCOCK. Is that what you propose in the new act?

Mr. BIRDZELL. Yes.

Mr. HANCOCK. I thought that you were asking Congress to relieve you——

Mr. GOLDSBOROUGH. Let him finish his statement, please.

Mr. HANCOCK. I should not have asked that question now, but I have such a different impression from him about that, that I thought he might be mistaken about it.

Mr. BIRDZELL. I hope that I have made it clear that we may operate a pay-off in a particular case without setting up a new bank at all.

Mr. HANCOCK. You did not make that clear.

Mr. BIRDZELL. If I did not make it clear, I want to do so. When I spoke of the transferred deposit, I said that the transferred deposit may be set up either in a new bank or in an existing insured bank. If, for instance, the community is one where there may be a desire to set up a State bank, or where there may an existing, operating State bank that is insured, we can set up in that existing, operating State bank, or in a new State bank that may be at once capitalized and become insured, transferred deposits to the credit of all of the depositors in the old bank, and to the extent of the insured amount of their deposits—that can be done, and that is a new feature. There is one other feature that Mr. Crowley suggests.

The act as it is proposed will become effective upon its approval, which will mean that immediately the permanent plan may be put into effect; but provisions are inserted in the act that will enable every bank, whether it desires to come into the permanent plan or not, to have the benefit of insurance on its deposits until July 1st, as provided in the existing law. In other words, while this act may become effective as a permanent insurance plan immediately upon its approval, any bank that is not a member of the Federal Reserve System that desires to withdraw may do so upon giving notice within 30 days after approval, but its deposit will continue to be insured until the 1st of July of this year.

One other provision with respect to Federal Reserve membership. Provision is made in the existing law whereby nonmember banks may enjoy the benefits of insurance in this Corporation until July 1, 1937, without becoming members of the Federal Reserve System. Our experience up to date with insured banks is a strong indication to us that two types of banks, at least, which we have in the fund, will not find it to their advantage, except for some wholly artificial reason, to ever become members of the Federal Reserve System, and those two types of banks are mutual savings banks and Morris Plan or industrial banks.

So we propose in this act to amend the provision with respect to Federal Reserve membership so as to exclude Morris Plan banks, industrial banks, and mutual savings banks from that requirement; and that will mean simply this, that commercial banks desiring to continue insurance after July 1, 1937, will be required to join the Federal Reserve System.

Mr. DIRKSEN. May I ask a question at that point?

Mr. GOLDSBOROUGH. I would like to proceed in accordance with seniority, on one side and then the other. Mr. Hancock.

Mr. HANCOCK. I am not sure that he is through.

Mr. GOLDSBOROUGH. Are you through?

Mr. BIRDZELL. Perhaps I ought to comment on this, that there is one provision of law—it is paragraph 5 on page 32—under which we can require banks to protect themselves against loss through insurance—fidelity insurance, burglary insurance, and that sort of thing. It reads:

> Each insured bank shall provide such protection and indemnity against burglary, fidelity, and other similar insurable losses as the board of directors, by regulation, may require adequately to reimburse the bank for such losses. Whenever any insured bank fails to comply with any such regulation the Corporation may contract for such protection and indemnity and add the cost thereof to the assessment otherwise payable by such banks.

We can give you an illustration of a bank in operation today wholly by reason of the fact that it does have burglary insurance. A large amount of money was taken from that bank. The insurance company is contesting the claim. We looked into the claim, and we think that it is a good one against the insurance company, but the company contends that it is not liable for more than about one-eighth of the loss. If they are not liable for the loss, that bank is insolvent today.

In view of the fact that its deposits are insured, and in view of the fact that the bank's attorneys and we feel that that bank has a fair prospect of recovering from the insurance company, that bank is operating today.

We think that we are entitled to whatever protection can reasonably be required of banks against losses that we know to be rather of frequent occurrence—defalcations, burglary, and the like.

We have also made provision in here to protect State banks against robbery, and so forth, where those banks are members of this Corporation. You gentlemen would be surprised, perhaps, to know that in a number of instances officers operating State banks have written in to us and suggested that some provision ought to be in the Federal law which will operate as a deterrent to bank robbers, because they say that their local authorities are absolutely at a loss to deal with those situations and that bank robbers take advantage of that and consequently rob the State banks, with almost immunity from prosecution.

The experience is different with regard to the Federal Reserve member banks, and the insured banks want to be given the same protection that is accorded now to the Federal Reserve member banks, so that the criminal features of the law in that respect have been extended to cover insured banks.

Now, I would be glad, indeed, if I may assist the committee any further by answering questions that might be based upon any feature of the proposed act.

Mr. GOLDSBOROUGH. Mr. Hancock, have you any questions that you want to ask at this time?

Mr. HANCOCK. I do not know. What is the pleasure of the committee as to proceeding? How much longer are we going to sit?

Mr. GOLDSBOROUGH. We will proceed to half past 12, I presume, unless there is some objection on the part of the committee.

Mr. HANCOCK. There are two or three questions that I would like to ask Judge Birdzell.

I am very frank to say that I have not given the time and thought to this proposed legislation that I do intend to give to it; but based upon the statement made the other day by Mr. Crowley with respect to the amount of assessment on the banks, as I understand the new law, the Corporation would have the right to levy an annual premium of one-twelfth of 1 percent on the total deposit liabilities. Is that correct?

Mr. BIRDZELL. The act itself does that.

Mr. HANCOCK. Is that discretionary with the Board?

Mr. BIRDZELL. No; that is the assessment rate that is prescribed in the law. There is provision, however, that would give the Board a discretion to lower the assessment at some future time, if experience seemed to warrant it.

Mr. HANCOCK. What do you mean, exactly, by lowering the assessment, Judge?

Mr. BIRDZELL. Suppose, for instance, that we went on for 2 or 3 years and added very materially to our reserves through assessments collected, and suppose that we had added, we will say, $75,000,000 to our funds available to meet losses. Suppose further that we had had favorable experience all the way through; and suppose that we should come upon a day when the banks were not earning, so that they might complain—this assessment would take substantially, you see, 1 percent on the entire capital of the bank; and suppose that they would say, "Your reserves are up; your experience is favorable; it is a hardship for us to meet this; can you not reduce the assessment for this particular year?" or for a particular 6 months' period. It is collected in two installments.

Mr. HANCOCK. Under the law, how much could you reduced?

Mr. BIRDZELL. Not more than 50 percent.

Mr. Crowley. Let me say something about that to Congressman Hancock.

I do not think that this provision, where you might have a right to reduce the assessment, could be hoped to be operative for a great many years. The Corporation should build up its surplus. I do not think that the board would look with favor toward reducing the assessment in the event it got a surplus of only $75,000,000, because I do not think that is adequate.

Mr. Hancock. The point that I am trying to bring out is that I got the impression the other day, from the statement presented by Mr. Crowley, that it was the judgment of the Corporation that the banks should not be responsible for all of this insurance protection.

Mr. Crowley. I think that that is correct, Mr. Congressman.

Mr. Hancock. That is the phase of this that I want to discuss with you, to find out how much protection you think should be furnished by the banks and what contingent liability you think should exist against the Government.

Mr. Crowley. I think this, Mr. Congressman, we must correct the evils of the past. If we are going to have the same loss ratio that we have had in the last 12 years, then I do not believe that the banks can carry that load themselves. I cannot conceive of this Congress or any other Congress not recognizing the necessity of correcting some of the abuses of the past. If we can correct and strengthen our banking system, then the amount that might have to be asked from some other source may be a very nominal amount, maybe nothing at all. If, however, we are to have a crisis again like we had in 1933, this fund could not take care of the demands upon it. I think that the losses of this fund will be nominal in the next few years. In the meantime, the Corporation should continue to build its surplus, so that in 10 or 20 or 25 years from now, if you have trouble like we had, perhaps, with some of our smaller communities, our fund would be sufficient to take care of the demands without calling on the banks for an additional burden at a time when they are under as heavy a load as they can carry.

Mr. Hancock. I, of course, appreciate the splendid purpose behind your viewpoint there, but what I am thinking about is this, that your statistical department has evidently made exhaustive studies in order to arrive at a fair assessment, and one that would be protective, and it seems to me, from my recollection of your statement the other day, that you said that to protect the depositors in all failures that had occurred from 1864 to 1934, it would have required an assessment of one-third of 1 percent, and to eliminate from that period what we might term the panic years, it would have required one-eighth of 1 percent.

Mr. Crowley. That is right.

Mr. Hancock. Now, you arrive at an assessment of one-twelfth of 1 percent.

Mr. Crowley. As I understand it, if you eliminate the periods of depression, I think that our figures show that one-tenth of 1 percent would take care of those losses on a $5,000 limit.

Mr. Hancock. I fully appreciate the wisdom and desirability of keeping the rate as low as possible to prevent it from being burdensome to the banks, especially today, but now we are engaged in writing a permanent law, and the suggestion has been made here that it is not the purpose of the fund to protect the depositor. Am I correct?

Mr. CROWLEY. I do not think that is correct, Mr. Congressman. What I really said was this, that if we were to be given certain supervisory powers we could protect ourselves. You might go back to 1920, when you had 30,000 banks. We lost nearly 15,000 banks from 1920 to 1933. A great many of our overbanked conditions have been washed out.

If we do not make the same mistakes as before and do not let this overbanked condition come back again, and if we can protect ourselves by going into a weakened institution and perhaps buying the assets or absorbing losses in order that mergers can be brought about, we are going to get away with a much lower loss. If we are given power to protect ourselves from loss, then I believe that this corporation can get along with a reasonable income. On the other hand, if we are just going to drift as in the last few years, then I do not believe you can assess against the good banks sufficient money to take care of the weaker banks without crippling the capacity of the good banks to write off their losses currently.

When it is all said and done the strength of the fund depends upon the banks being so well run and their earning capacity being sufficient to allow them to take their losses currently in place of letting them accumulate. I think everyone will agree that a good many banks permitted their losses to accumulate. Some of these banks even paid dividends, whereas they should have written off their losses.

I think that this fund should eventually build a sufficiently large surplus so that in the ordinary regional depressions—not a depression like 1933—this fund could pay its losses promptly without making an assessment against the Government or the banks.

Mr. HANCOCK. I notice that in the new act you propose to vest discretion in the board of directors with respect to the allocation of your capital fund—and I am just asking these questions in order that we may have a record before us. I am wondering if, in making that request, there is an implied suggestion that a situation might arise whereby you would prefer to resort to that fund in paying your losses rather than to levy an assessment?

Mr. CROWLEY. No. Our assessment of one-tenth of 1 percent or one-twelfth of 1 percent will bring us in from 30 to 39 million dollars a year. Supposing that during the first 2 years, before you built up any surplus, you should have a serious failure. If we were to pay that loss, we would pay it out of capital and immediately have an impaired capital. I do not think it makes any difference to the Government whether they have a no-par-value stock or $100,000,000 capital and $200,000,000 surplus, or whether they have that all in capital, because that money was given to us for the purpose of aiding us in paying losses. Only to have the income from that money, while it is helpful, is not enough. In other words, the psychological effect of our Corporation would be better if eventually we had $100,000,000 capital and $500,000,000 surplus——

Mr. HANCOCK. Yes; I understand that thoroughly.

It was my impression that, to begin with, that capital fund was not to be used to pay losses. Is that correct?

Mr. CROWLEY. I do not know what else they gave it to us for, then.

Mr. HANCOCK. My understanding was that it was more or less for back-log or reserve.

Mr. CROWLEY. It if was not a reserve for losses, what was the purpose of giving it to us?

Mr. HANCOCK. Under the original act, of course, you had the right to expand three times the amount of the capital structure.

Mr. CROWLEY. Yes; but when you get to the point where you are expanding and borrowing, that does not create confidence. That you would only do in case of dire necessity.

Mr. HANCOCK. Surely the capital upon which you expand your credit should be the last thing that you would touch.

Mr. CROWLEY. That is the reason why we are asking for a reduction in the capital, so that we do not touch that capital. That is the reason why we do not want to impair our capital.

Mr. HANCOCK. What is going to happen to the amount of $139,000,000 that we took away from the Federal Reserve banks and allocated to your Insurance Corporation?

Mr. CROWLEY. Well, as I see it, it does not change their position any. One hundred thousand dollars worth of stock in a corporation that is worth $100,000, and that has no surplus, or $100,000 in a corporation with $10,000 capital and $90,000 surplus, does not affect the real value of our investment.

Mr. HANCOCK. You probably did not catch my point. I understood that a trade arrangement had been made whereby the Federal Reserve System would sell its stock to the Treasury Department. Do you know anything about that?

Mr. CROWLEY. I do not recall.

Mr. HANCOCK. Is it not a fact that the Federal Reserve System has sold $20,000,000 of that stock to the Treasury?

Mr. CROWLEY. That is in your industrial loan act of last year.

Mr. HANCOCK. That was an indirect way that they had of doing it. Just one other feature at this time, Mr. Crowley.

One of the most important and attractive features of this act to me, to begin with, was when our chairman emphasized that under the law, in event of a failure, the Corporation would immediately set up a new institution, so that the business of the community could go along smoothly. I recognize that there may be times when to do that would be futile, when it would be improper, and when it would be unwise, but I think that it would have a very serious effect if the board here should decide, as a matter of policy, not to carry out the original provision with respect to that section. Of course, there would be no sentiment in a community to set up a new bank on the failure of a bank, but in time every community would want the assistance of this Corporation in building up a new banking structure in that community, and I do hope that this board will not act arbitrarily in that matter in worthy cases.

Mr. CROWLEY. I do not think there is any doubt but what the board is sympathetic with the idea of giving to every community a bank as long as that community needs that bank. Let me tell you what our experience in the past has been. For instance, we paid off at Pittsburgh. Pittsburgh already has a great number of banks.

We have stayed there for several months now, and an expense is accumulating against us every day. We went into Indiana and we paid off an institution there. That community has sufficient banks all around it. There are a great many instances in the cities where you have two or three banks and where two banks can take care of that community well.

Mr. HANCOCK. I know that the board has been acting wisely and has done splendid work, but can it not be assured in some way that where there is only one bank in a community, the Corporation would always replace the closed institution?

Mr. CROWLEY. Let me say to you that I think you have to take some of this on the faith of the Corporation. The Corporation now has operated for some 15 months, and I think the great majority of the small bankers feel that we have been very sympathetic with them in trying to understand their problems. You men are here every single year. If the Federal Deposit Insurance Corporation gets too autocratic in some of these things, you men will immediately put something in the law to stop that abuse.

Mr. HANCOCK. Nothing that I have said has suggested that I feel that way.

Mr. CROWLEY. I understand that.

Mr. HANCOCK. Now, here is one other point that I want to clear up, and then I am through.

Could not some arrangement be made with the insured member banks whereby they would agree with the Corporation that the unexpended balances in trust funds were actual trust funds, and not deposits?

Mr. CROWLEY. Judge, that is your end of it.

Mr. HANCOCK. I have had a number of complaints from North Carolina on that particular point. Why would it not be proper and perfectly legal for the officers of a bank to enter into an agreement with you which would clarify the question as to whether they actually constituted deposits or not?

Mr. BIRDZELL. Then, if the bank should fail, and the owner of those funds should come to make claim against the Corporation, what would we say to the owners of the funds?

Mr. HANCOCK. You would just say what the bank officers had said to you.

Mr. BIRDZELL. Yes; but——

Mr. HANCOCK. If they had enough confidence to put their money in the bank that was manned by those officers, they certainly ought to be forced to rely on their agreement.

Mr. BIRDZELL. But it is not the agreement of the depositor. It would be the agreement of the bank, and the depositor would be in the position of having his claim unsatisfied. It would be hard for him to distinguish between what he had coming from the bank in the shape of uninvested trust funds and what he had coming from the bank on his savings account. Furthermore, there would come a time when it would have to be otherwise treated.

Take this situation: Say that it is a national bank that operates a trust department. The trust funds may be deposited from the trust department into the commercial department of the bank, and they may be utilized just as all other funds of the bank are utilized, in channels of commerce. Now, when the funds are placed at the disposition of the commercial department of the bank, or when they might be deposited in another bank, certainly the persons that are beneficially interested in those funds should be entitled to protection, and certainly also they become deposits just like all other deposits in the bank, and they are used as such.

Mr. HANCOCK. That is all.

Mr. GOLDSBOROUGH. Mr. Hollister.

Mr. HOLLISTER. With respect to the issue of notes and debentures of the Corporation, the existing law provides that they may issue two or three times the amount of the capital.

Mr. BIRDZELL. Yes.

Mr. HOLLISTER. They are not guaranteed by the Government, although they are tax exempt.

Mr. BIRDZELL. Under the proposed law they would not be.

Mr. HOLLISTER. Is that in the proposed law?

Mr. BIRDZELL. Yes; that is in the proposed law, although I did not cover it.

Mr. HOLLISTER. That is what I thought, that there is no guarantee whatsoever of that kind, either in the existing law or in the new law.

Mr. BIRDZELL. But the Treasury is authorized to purchase them.

Mr. HOLLISTER. The Treasury is authorized to, but the Treasury might not purchase them. But there is no guaranty by the Government of those debentures?

Mr. BIRDZELL. You are correct.

Mr. HOLLISTER. Under the existing law, where there is a provision that three times the amount of capital may be issued in bonds and debentures, those debentures can be sold to better advantage because of the unlimited assessment provision, for as long as losses may be assessed continually against the banks, there can always be built up a protection in the Corporation for those who buy the debentures.

Mr. BIRDZELL. That is correct.

Mr. HOLLISTER. But under the proposed law, with a limitation of one-twelfth of 1 percent a year, it is difficult for me to see the possible market of those debentures outside of the Treasury. Here you have a debenture that is not guaranteed by the Government, even though it is nontaxable. Under a set of disastrous circumstances your capital aud surplus might be completely wiped out.

Mr. BIRDZELL. There is a further market provided for those debentures, the Reconstruction Finance Corporation, to the extent of $250,000,000.

Mr. HOLLISTER. Yes; but that would require action by the Government. I am not saying that it is wrong, but I am merely trying to get at the change in the whole idea. The original idea was a debenture which was a sound proposition for private capital, because of the fact that it had behind it the whole banking system of the country, under the unlimited assessment idea. Now you have a debenture which it seems to me has no private market whatsoever, but is solely valuable insofar as the Reconstruction Finance Corporation or the Treasury would care to invest.

Is not that the case?

Mr. BIRDZELL. Yes.

Mr. HOLLISTER. It really ceases to be a private obligation to be sold in the market.

Mr. CROWLEY. It is true that if we had to issue debentures to private borrowers up to three times the capital, undoubtedly the condition would be such that you could not find a ready market. It might be possible that you had $300,000,000 in securities and that you might only want to borrow $50,000. Of course, you could sell debentures on that kind of a collateral provision.

Mr. HOLLISTER. Of course, the theory in selling debentures would be to get additional funds in order to satisfy the demands of the Corporation, and if conditions should arise where it would appear to be necessary for the Corporation to sell debentures, under the new law it seems to me that the average private investor, when he would realize that the only thing back of these debentures is the possibility of collecting one-twelfth of 1 percent annually, would say, "Notwithstanding the nontaxable feature, that is hardly a thing that I am interested in."

Mr. CROWLEY. That is true if you had a critical situation.

Mr. HOLLISTER. But would you be selling them unless you had a critical situation?

Mr. CROWLEY. No; unless you would be doing it for some short-term borrowings. Suppose that you had $3,000,000 in securities and the market might be temporarily down. That would not affect your borrowing as long as you had adequate collateral. However, if we got to a point where we had an emergency, and we had to issue 4 or 5 million dollars of debentures at that particular stage, I do not believe that the open market would absorb those debentures unless you had the Government guarantee. The fact that the Secretary of the Treasury would come to our rescue if we had that kind of a condition, however, gives us some confidence.

Mr. HOLLISTER. I am not presenting the view that it is wrong. I am merely trying to bring out that, after all, if such debentures under the new law should be issued, some kind of governmental agency, the R. F. C. or the Treasury, would have to take them.

Mr. CROWLEY. We have $250,000,000 that the R. F. C. have earmarked for our corporation.

Mr. HOLLISTER. On page 5, in section 11, as to obligations payable outside of the United States, that affects only a few banks and is put in there because of the foreign competitive situation, is it?

Mr. BIRDZELL. It affects banks that have European branches, or branches in outlying possessions, like Puerto Rico.

Mr. HOLLISTER. Was that not included in the bill that passed the House last year, but which never got through the Senate?

Mr. BIRDZELL. No; that is the old law.

Mr. HOLLISTER. Section 11, on page 5?

Mr. BIRDZELL. Where is the provision that you are referring to?

Mr. HOLLISTER. The proviso at the bottom, which reads:

> *Provided*, That any obligation of a bank which is payable only at an office of the bank located outside the States of the United States, the District of Columbia, and the Territories of Hawaii and Alaska shall not be a deposit for purposes of this section or be included as a part of total deposits or of an insured deposit.

Mr. BIRDZELL. That was in the omnibus bill, which did not get through.

Mr. HOLLISTER. And that is there because, if they had the cost of the insurance to add to their operating cost, they would be in a bad competitive situation in a foreign country?

Mr. BIRDZELL. Yes; that is the purpose of that, if I understand your question, and that provision there is consistent with the provision in last year's omnibus bill.

Mr. GOLDSBOROUGH. Mr. Williams.

Mr. WILLIAMS. To my mind, there are two very fundamental things in this bill.

First, I am thinking about what you are going to do with some 8,000 nonmember banks that are not in the permanent insurance plan, and which will not be under the provisions of this bill.

In the second place, there is the question of a limited liability.

Now, it is not contemplated, is it, that there will come a time when these insurance deposits will not be paid in full?

Mr. CROWLEY. You mean that these funds will not be sufficient?

Mr. WILLIAMS. Yes.

Mr. CROWLEY. It is my honest judgment that if you will give to this Corporation the supervisory powers that we have asked for, that this Corporation should be able to keep itself solvent, barring unforeseen accidents.

If this country cannot operate a banking system so that the depositors will not suffer losses that may break this Corporation, then there is something distinctly wrong with your banking system and your monetary system. That calls for a corrective measure far beyond the powers of the Federal Deposit Insurance Corporation.

Now, I believe that this Corporation can operate and pay to depositors their losses with any kind of normal conditions.

Mr. WILLIAMS. That is perhaps true.

Mr. CROWLEY. I hope it is true.

Mr. WILLIAMS. I am not so much concerned with the power of the Board to reduce this assessment as I am with the power to raise it in case it is necessary, in order to take care of the liabilities of the Corporation.

Mr. CROWLEY. You understand that while the Corporation would look with favor on all of the revenue that you can give us, nevertheless you cannot have an unlimited liability or a liability so large that in times of stress you may weaken your entire banking structure.

Mr. WILLIAMS. Then your whole system, at the very time that it is needed the most by the depositors of the country, breaks down?

Mr. CROWLEY. I think that is where supervision comes in—to prevent that.

Mr. WILLIAMS. You have the supervision which will do it.

Mr. CROWLEY. Correct.

Mr. WILLIAMS. But why not, if you say that you can administer the law in such a way as to prevent those losses by the discretion and the power that is in the Board, increases the assessment in case it is necessary?

Mr. CROWLEY. I think that there is a danger that deposit insurance might break down the private initiative of men who are trying to operate these institutions. We have a great many banks that we are insuring almost 100 percent. Men operating these banks will not have the same incentive as those which are operating banks only 5, 10, or 15 percent insured.

Mr. WILLIAMS. Of course, you agree that we do not need any insurance as long as there are no bank failures.

Mr. CROWLEY. I think that you will always have a certain number of bank failures, but it is like anything else—like your hospitals or your railroads or anything. If you have an epidemic in Washington where everyone in Washington is sick, your hospitals are not large enough to care for them. You cannot build this fund large enough to pay out 16 or 19 billion dollars overnight.

Mr. WILLIAMS. Then it is based upon the idea that you may have a condition where you could not pay out?

Mr. CROWLEY. I think everyone will agree that we could not pay out our entire liability at one time.

Mr. WILLIAMS. What other contingent funds have you in mind if the assessment fails? What else would you do?

Mr. CROWLEY. We have our right to borrow from the Treasury. That is all we have.

Mr. WILLIAMS. You are assuming, now——

Mr. GOLDSBOROUGH. You do not mean the right to borrow? You mean that the Treasury is authorized to loan if necessary?

Mr. WILLIAMS. You mean that under this act the borrowing power is confined to the Treasury Department alone?

Mr. CROWLEY. And to the $25,000,000 from the R. F. C.

Mr. WILLIAMS. Under this act, are private individuals permitted to lend you money on your debentures?

Mr. CROWLEY. Yes; they are permitted to do it.

Mr. WILLIAMS. If they want to?

Mr. CROWLEY. Yes; if they want to?

Mr. WILLIAMS. If there is a private field for the investment, they are permitted under this law to invest in your debentures?

Mr. CROWLEY. That is correct.

Mr. WILLIAMS. You have that power?

Mr. CROWLEY. That is right.

Mr. WILLIAMS. What is the purpose of allocating the capital structure of that institution to surplus?

Mr. CROWLEY. I do not think that allocation of capital has anything to do with the right of borrowing.

Mr. WILLIAMS. It is the intention to use that in case of need to pay the losses?

Mr. CROWLEY. Yes. We may take——

Mr. WILLIAMS. The idea back of it is that the money that is received from the Federal Reserve banks and from the Treasury should be used as a reserve fund to pay these losses, rather than from the banks themselves?

Mr. CROWLEY. That is correct.

Mr. WILLIAMS. Now——

Mr. CROWLEY. Let me answer that. I think the Government, when it licenses a bank and establishes a banking system, assumes a responsibility to the depositors, and when it created this Corporation I think that it assumed a responsibility for the protection of the depositors. I do not believe that any man argues that we should continue to permit losses to occur as has been the case in the last 12 years.

Mr. WILLIAMS. Nobody will contend that, I think, but you expect, by reason of your regulatory powers, and by reason of reports made to you, and your inspections, to regulate, within reasonable grounds, the banking activities of the country and to prevent these failures?

Mr. CROWLEY. But, Congressman, we do not guarantee to prevent failures entirely. We hope to reduce the number of failures.

Mr. WILLIAMS. That is so, and the very purpose of all this insurance, according to my idea, should be to guarantee, in case of failure, the payment of the depositors in full.

Mr. CROWLEY. I think that is correct, but I do not see any way in the world that you can draft a bill or that you can give us sufficient funds, so that you could say that at all times, regardless of whether you have a complete collapse of your banking system, this Corporation could pay the losses of all depositors.

Mr. WILLIAMS. Could you conceive of a complete collapse in the banking system of this country now, under the supervision of your Corporation and of the Federal Reserve system?

Mr. CROWLEY. All that I can say to you is this: I believe that under our rebuilding program, the banks as a whole are in the best shape that they have been in a great many years. With the proper kind of supervision we should not have the losses that we have had in the past.

Mr. WILLIAMS. Now, merely to furnish a factual background, there are about thirty-six billion and a half in deposits now, are there not?

Mr. CROWLEY. That is correct.

Mr. WILLIAMS. What part of that is in time deposits?

Mr. GOLDSBOROUGH. Would it be agreeable for you gentlemen to come back tomorrow morning?

I want to say to the members of the committee that there is a gentleman here from California who has to go back tonight, and he and Mr. Ford have both asked that he be allowed to put a statement in the record.

Mr. Adams, will you come up here, please?

It is very important, Mr. Adams, that the members of the committee get to the floor of the House as quickly as possible, and I am wondering if you could limit your statement to 10 minutes, and then give to the members of the committee the written statement which you left with me the other day.

STATEMENT OF EDSON F. ADAMS, PRESIDENT FARMERS AND MERCHANTS SAVINGS BANK, OAKLAND, CALIF.

Mr. ADAMS. I think that I would have to read the statement, Mr. Chairman, in order to make it clear. If I did not do that, I do not think that they would grasp it.

Mr. GOLDSBOROUGH. You will proceed, then.

Mr. ADAMS. It appears quite necessary at this time that the Banking Act of 1933 and Federal Deposit Insurance Act be amended covering certain important matters as they now injuriously affect banks doing a strictly savings bank business and, also, mutual savings banks of the Middle Western and Pacific States which are not numerous enough to protect themselves by establishing a savings-deposit guarantee under State authority, as has been done in the State of New York.

Briefly, the main changes requested in the present laws are as follows:

First, savings banks, doing no commercial business, and mutual savings banks should be placed in a class or group by themselves instead of being required to join in guaranteeing deposits in banks doing all types of banking.

Second, savings banks should be granted the right to obtain interest on deposits with approved commercial banks of reserves and surplus funds awaiting the demand for savings bank loans.

Third, savings banks and mutual savings banks should not be forced to join the Federal Reserve System to obtain insurance, since they do no commercial business, and, therefore, are not able to avail themselves of its facilities.

Fourth, savings banks in the West should be granted the right to allow depositors to use checks against short-notice savings accounts, in order to protect their term-savings accounts against competitors. State savings banks in California have had this right for many years.

As to savings banks guarantee of all types of deposits, if the country is to have permanent-deposit insurance, the great criticism of the present act is that all banks are put together in one group, when their methods of business are, in many cases, diametrically opposed, some pay interest on practically all of their deposits, while others pay no interest on any deposits and therefore require entirely different handling of their resources.

It appears there should be two or three Federal Deposit Insurance Corporations, based on the actual liability involved, instead of one, with separate officers and garuanties for each corporation representing each group of banks, and with provision for representation on its board of directors; the commercial banks being placed in one group, the departmental banks in one group, and the strictly savings banks and mutual savings banks together in a separate group. In this way each member of each group would be insuring its own type of business, which would be the only fair way to handle it. Insurance for savings banks would command a very low rate compared with commercial and other types of banks. In California all savings-bank loans can be made only on the highest type of security and the classes of security and the conservative margins required are plainly stated in our bank act.

It is neither fair nor just to mutual savings banks and strictly savings banks, as operated under western conditions, to link them with departmental banks, commercial banks, and trust companies, where money is shunted from one department to the other, as the opportunity offers to play with the savings of savings depositors. Nor is this all. In many banks property taken in under foreclosure is thrown into holding companies owned by the bank's stockholders and manipulated so as to hide the fact that the bank is carrying property taken for debt, thereby weakening the bank and deceiving the public.

Real savings banks, operated as such, are a boon to the man or woman of small means. Conditions in the West are different from those in the Eastern States, hence codes, rules, and regulations should vary in each Federal Reserve district to conform to existing conditions or customs not in conflict with good savings-bank practices.

This is so not only in banking but also in other lines of business: For example, the first N. R. A. chief in California found that codes prepared to cover eastern conditions did not fit those in the West.

National banks under several administrations have been receiving the individual savings of the people and issuing savings passbooks showing deposits and the money so received credited to the depositor as a savings deposit, but here it ends. In practice, from here on, the money so received is put into and mingled with the other funds of the national bank, a commercial institution.

In a national bank the people's savings deposits can be loaned on notes of hand at will be the officials of the bank, and, if they choose, without any security whatsoever to protect the loan except the personal responsibility of the recipient of the loan.

In the interest of safety the money so deposited by savings depositors should be loaned without the borrower first putting up ample approved security to secure the money so loaned. In California the law governing State banks requires that no money received from savings deposits be loaned either by strictly savings banks, mutual savings banks, or by a savings department of a departmental bank except on ample and approved security. These provisions are apparently entirely ignored in the National Bank Act.

Mr. GOLDSBOROUGH. I do not believe that it will be possible for the members to stay, and each member has a copy of the statement that you are reading, Mr. Adams, and I am going to suggest, sir—and I want to be of every service that I can to you and your institution—that you just insert your statement into the record. I can assure you that every member of the committee will read it.

You have seen how they are leaving. I do not believe that you can hold them.

Mr. WOLCOTT. I am staying here merely out of courtesy to you, and I would prefer to read this in my office, if you are just going to read it. I understood that you were going to comment on it as you went along.

Mr. ADAMS. No; the comments are all in it, but I have some additions, in regard to other things.

Mr. WOLCOTT. My opinion is that that which is written you could put in the record without reading. We have some important legislation on the floor.

Mr. GOLDSBOROUGH. The members of the committee really do have to go on the floor, and, of course, if you were in a position to wait, we would be very happy to hear you in full. We are extending to you this courtesy because you have to get back to California.

Mr. ADAMS. I can wait until the end of the week, if there is no opportunity now.

Mr. GOLDSBOROUGH. I am not sure about it after Friday. On Thursday we will have to have the home loan bill on the floor, and I do not know what will happen.

I can assure you that you will receive just as much consideration if you will just allow that statement to go into the record. This committe is not going to overlook reading your statement.

Mr. ADAMS. I will tell you: I would like to submit copies of the letter from Mr. Parker S. Maddux, who is the president of the San Francisco bank——

Mr. GOLDSBOROUGH. Yes, sir; without objection, it will be inserted in the record.

Mr. ADAMS. And also from Mr. Richard M. Tobin, who is the president of the Hibernia Bank, San Francisco.

Mr. GOLDSBOROUGH. Without objection, they may go into the record at this point.

(The letters referred to are as follows:)

THE SAN FRANCISCO BANK,
San Francisco, Calif., February 6, 1935.

EDSON F. ADAMS, Esq.,
President Farmers & Merchants Savings Bank,
Oakland, Calif.

DEAR MR. ADAMS: You have exhibited to me a statement which you propose to submit to the chairman and members of the Banking Committee of the House of Representatives at Washington. In this statement you suggest four main changes to be made in the present banking laws of the United States.

The purpose of this letter is to assure you and the committee that this bank is favorable to all of the suggested changes.

Hoping that you have a pleasant and successful trip to Washington, I beg to remain,

Very truly yours,

PARKER S. MADDUX, *President.*

HIBERNIA BANK,
San Francisco, Calif., February 4, 1935.

Mr. EDSON F. ADAMS, *President,*
Farmers & Merchants Savings Bank, Oakland, Calif.

DEAR MR. ADAMS: I have carefully read the draft of your proposed " Statement to the chairman and Members of the Bank Committee."

The four objectives which you cite on the first page are all excellent, and I approve especially of the first three.

With best wishes for your success, I remain

Yours very truly,

RICHARD M. TOBIN.

Mr. ADAMS. I might say, in connection with these letters, that the San Francisco Bank has savings deposits of $151,224,000, and total resources of $167,847,098. They have 36,731 term savings accounts and also special savings accounts with checking privileges, 5,800; making total savings accounts 42,531.

The Hibernia Bank has savings deposits of $87,422,625, and the total resources are $98,593,230. They have 69,889 savings accounts.

The bank of which I am president, the Farmers & Merchants Savings Bank, has savings deposits of $7,877,094.96, and total resources of $8,385,636.68. We have 10,117 term savings accounts and 19,042 term school savings accounts and 2,317 special ordinary savings accounts, with checking privileges, making total savings accounts 31,476. In this bank, the percentage of deposits covered by Federal deposit insurance is 85 percent.

The Zion's Savings Bank & Trust Co. are also desirous of having some relief, as is shown by their letter to Mr. Frank B. Lanham, special representative, Federal Deposit Insurance Corporation, Washington, D. C. Their savings deposits amount to $13,103,232.13.

Mr. CAVICCHIA. May I suggest that the gentleman be given time to hand to you any other communications that he wants inserted in the record. If he does not have them now, he may hand them in later in the day.

Mr. GOLDSBOROUGH. That will be entirely agreeable, if there is anything else.

Mr. ADAMS. I would like to call your attention to this, that, of course, I have some other things here which go to support my proposition.

Mr. GOLDSBOROUGH. I am inclined to think that the mutual banks are going to be taken care of in this legislation. I do not believe that you are going to find any fault with that.

Mr. ADAMS. I am not a mutual. We are a stock bank, you understand, and we have been left entirely out of this bill. The only people that are referred to in this bill at all are the mutual savings banks and nobody else, and that puts us in California and in the West in a bad position. The Zion's Savings Bank & Trust Co., in Salt Lake City, are, as I have just indicated, in the same position.

Mr. WILLIAMS. Can you not come into the Federal Savings and Loan Insurance Corporation?

Mr. ADAMS. No, sir; not unless we join the Federal Reserve System, and we have no business in the Federal Reserve System. We can do no business with them.

Mr. WILLIAMS. I think that you are in error about that. The law permits any institution that can qualify to come in.

Mr. ADAMS. We have already joined in the temporary deposit insurance, you understand.

Mr. GOLDSBOROUGH. And you think that your assessment should be reduced?

Mr. ADAMS. Not necessarily, but we do not want to be made liable for all classes of banking.

Mr. WILLIAMS. I am talking about the Federal Savings and Loan Insurance Corporation. I do not know whether you understood me. The act passed last year by this Congress authorized building and loan institutions and savings banks of the country to have an insurance plan. What is the reason that the institution that you represent cannot come into that plan if it wants to?

Mr. ADAMS. Because we are not a building and loan institution, as their type of business is entirely different from that of a bank. The business which we do is of the same character, exactly, as the mutuals, only that we have stock instead of a mutual association.

Mr. WILLIAMS. But it includes not only the building and loan associations but the savings banks and mutual banks as well.

Mr. CAVICCHIA. As I understand it, Mr. Williams, the language of the act that you are referring to states " and other financial institutions ", which opens the door to this type.

Mr. WILLIAMS. It not only does that, but it mentions the very class of institution about which he is talking.

I think, Mr. Adams, that you will find that out upon investigation.

Mr. ADAMS. We have not been able to find that, and if we have to be brought in the Federal Reserve System, then we have to become a departmental bank, and we do not want to.

Mr. GOLDSBOROUGH. Let me see if this suggestion will be helpful to you: If you will insert what you have there in the record, and then have an amendment drawn up which meets with your views and hand that to Mr. Ford, he can then offer it, and we will consider it with other amendments.

Mr. ADAMS. I will do that, Mr. Chairman, but I wanted to say this, that you talked of national banks today, and they have savings deposits amounting to $6,053,020,000, and those savings deposits can be loaned out on unsecured notes, and there is nothing to prevent that, not a thing, and they are doing it, and we do not want to be tied to the tail of that kite, because we do not consider it a safe way of handling of savings deposits.

I have been in business for 40 years, and I think I know something about it.

Mr. GOLDSBOROUGH. Prior to today, I thought that your idea was that your assessment should not be as great as the assessment of a commercial bank.

Mr. ADAMS. It would not be under ordinary circumstances, if you took the liability into consideration.

Mr. WILLIAMS. As I understand you, you want Congress to set up another corporation, or an insurance company, simply to take care of the class of institutions that you represent?

Mr. ADAMS. No. This could be done by classifying us, possibly, with the mutuals, the outside mutuals which you brought in in your last amendment.

Mr. GOLDSBOROUGH. If your bank is really in the same class with the mutuals, insofar as your liabilities are concerned, I am certain that this committee will deal very justly with any amendment which may be offered, and I presume that you will want Mr. Ford to offer it, because, as I understand it, you only have 3 or 4 of these institutions in the United States.

Mr. ADAMS. There would be a great many in the United States, if they had the opportunity.

Mr. GOLDSBOROUGH. I understood you to tell me that there are two in California and one in Utah.

Mr. ADAMS. What I said was that the two banks in California had endorsed my propositions.

Mr. WOLCOTT. Are you under State supervision?

Mr. ADAMS. Under State supervision.

Mr. CAVICCHIA. I think that that matter could be taken care of by Mr. Ford, who is a member of this committee.

Mr. ADAMS. Yes. Shall I submit this?

Mr. GOLDSBOROUGH. Yes; and it will be inserted in the record and printed, and your amendment should be prepared and introduced, I presume, by Mr. Ford, from your State.

Mr. ADAMS. You mean these additional things?

Mr. GOLDSBOROUGH. Yes. They will be inserted in the record. Just hand them to the reporter.

The remainder of the statement is as follows:

By combinations and other manipulations, banks incorporated principally for commercial business have acquired the people's savings deposits, sometimes in amounts almost double their commercial deposits. In one instance, in a published statement, a national bank has approximately 260 millions in commercial deposits and approximately 460 millions in savings deposits, all dumped into the same pot and these savings deposits can be handled and loaned commercially, with all the attendant risks of commercial banking, while mutual savings banks and savings banks doing no commercial business, when loaning their deposits, must require ample security for all loans made. This condition of facts shows very clearly that banks having only saving deposits should be put in an independent group by themselves and not be forced to participate in guaranteeing unsecured loans of commercial banks.

As to interest on reserves of savings banks in correspondent banks, under the provisions of the Banking Act of 1933, mutual savings banks are allowed to receive interest upon their deposits (sec. 11, par. (b.)).

The Legislature of the State of California in 1933, with the approval of the State superintendent of banks, amended the State bank act. General provisions section 21 (1). This section practically follows section 19 of the Federal Reserve Act but allows savings banks to receive interest on their deposits with commercial banks.

SECTION 21. (1) No bank shall, directly or indirectly, by any device whatever, pay any interest on any deposit which is payable on demand: *Provided*, That nothing herein contained shall be construed as prohibiting the payment of interest in accordance with the terms of any certificate of deposit or other contract heretofore entered into in good faith which is in force on the date of the enactment hereof; but no such certificate of deposit or other contract shall be renewed or extended unless it shall be modified to conform herewith, and every bank shall take such action as may be necessary to conform herewith as soon as possible consistently with its contractual obligations: *Provided, however*, That this section shall not apply to any deposit of such bank which is payable only at an office thereof located in a foreign country, and shall not apply to any deposit made by a savings bank, nor to any deposit of public funds made by or on behalf of the State, or of any county, city and county, city, town, municipality or other public or municipal corporation of the State of California, with respect to which payment of interest is required under State law. * * *

There are 594 mutual savings banks in the United States, as of June 30, 1932, and they are located in the following States:

New England States 379, total resources	$3,711,220,000
Eastern States 195, total resources	7,047,074,000
Middle Western States 16, total resources	220,708,000
Pacific States 4, total resources	155,140,000
Total	11,134,142,000

It will be noted that 574 are located in the New England and Eastern States, with resources of $10,758,294,000, while the Middle Western and Pacific States have only 20, with total resources of $375,848,000, or approximately 3½ percent of the total resources of the mutual savings banks in the United States.

A law giving to the mutual savings banks of New England and Eastern States special privileges by not allowing strictly savings banks in the rest of the country to receive interest from commercial banks upon their deposits is unjust and unsound. In order to operate savings banks conservatively, so they will be able to pay withdrawals without affecting their loaning ability, it is very essential that they maintain sufficient balances in cash with banks duly authorized by the State banking department, as depositories. Unless a savings bank has the right to receive some interest from its depositories, the tendency would be to operate with as little cash as possible, in order to meet the interest to savings depositors, costs of operation, and other demands of the savings bank business. Under certain conditions of the money market, this might at times cause the hurried investment in securities and possibly would encourage loaning on a poorer type of real-estate security.

As to savings banks as members of the Federal Reserve System, the Federal Reserve System was inaugurated to develop the commercial banking resources of the country. Savings banks, properly operated, have practically nothing in common with the Federal Reserve System and it would be a great injustice to force them to join that System. They are not able to discount their loans with the Federal Reserve bank and therefore do not receive the main benefit accruing to commercial banks which are members of the System.

As to savings banks' depositors being allowed the use of checks to withdraw funds, the Federal Reserve bank, having in mind solely commercial business, would probably classify checking accounts against a certain class of savings accounts, on which checks are used as a convenient form of withdrawal, as being commercial business which would not be the case, as no commercial loans are made at all by savings banks in the State of California. It has been found in California, under western conditions, that a strictly savings bank, in order to function properly, must have this type of account. These accounts are opened principally for personal convenience by savings depositors, who prefer to do all their banking in one place. They are not of a type that require commercial accommodation. The balances are moderate and the checking service has been found to be a benefit to the depositor as well as to the savings bank. Also, frequently, people obtain loans from a savings bank, open checking accounts, and some portion of the money remains with the bank for a long period.

The savings bank of which I am president has over 2,286 accounts of this type, aggregating over $780,000, of which only 21 are above $5,000, and 275 between $500 and $5,000; 1,990 accounts are below $500, which goes to show that these accounts are in no way commercial accounts, but are opened for the necessary personal accommodation of our savings depositors; and it also shows that, in our western country, the ability to allow a withdrawal by check is extremely important and necessary to any savings bank doing only a savings-bank business. This class of accounts has a provision for a 30 days' notice, if the bank should require it.

Our State banking department for years has classified these accounts as savings accounts. Where there is strong competition by departmental banks, savings deposits would be transferred from strictly savings banks that do not have checking privileges, to other banks, and would force savings banks to open commercial departments at additional expense, without really wanting to do a commercial business, simply to accommodate and give personal checking service to its savings depositors.

With over 40 years of experience in the savings-bank business, I have observed that strictly savings bank operated by men versed in savings-bank administration prosper and serve the public in a better way than those left to be administered by highly specialized commercial bankers, whose main thought is the advancement of commercial business.

I therefore urge that your committee amend the present acts at this session of the Congress as outlined in the four changes enumerated, so that savings banks may safely continue deposit insurance and at the same time have reasonable protection in operating under western conditions.

Mr. CAVICCHIA. May I remind you, Mr. Williams, that one question that you asked was not answered, and I hope you will have an answer as to what will happen to those 8,000 banks?

Mr. WILLIAMS. Yes; I am going to go back to that. It is very important.

Mr. GOLDSBOROUGH. The committee will adjourn until tomorrow morning at 10:30.

(Thereupon, at 12:45 p. m., an adjournment was taken until Wednesday morning, Feb. 27, 1935, at 10:30 o'clock.)

BANKING ACT OF 1935

WEDNESDAY, FEBRUARY 27, 1935

House of Representatives,
Committee on Banking and Currency,
Washington, D. C.

Hearings on the bill above referred to were resumed at 10:30 a. m., Hon. T. Alan Goldsborough presiding.

Mr. Goldsborough. The committee will be in order.

Mr. Williams, will you resume your questioning where you left off yesterday?

STATEMENTS OF LEO T. CROWLEY, CHAIRMAN, AND L. E. BIRDZELL, GENERAL COUNSEL, FEDERAL DEPOSIT INSURANCE CORPORATION—Resumed

Mr. Williams. I believe that we agreed that the amount of deposits in the commercial banks of the country was practically 36½ billion dollars. The last question was, what part of that is in time deposits.

Mr. Crowley. I am told about one-third. That would be about 12 billions.

Mr. Williams. What character of time deposits does that involve? There are different kinds of time deposits.

Mr. Crowley. That includes, for instance, savings accounts and certificates of deposit, where they are not subject to check.

Mr. Williams. That means all of the accounts, does it, in which notice is required before they can be withdrawn; or, in other words, they are for a definite, fixed period and not subject to check at all?

Mr. Crowley. That is correct, where you have to give definite notice of withdrawal.

That does not include postal savings.

Mr. Cavicchia. Do I understand that your answer to Mr. Williams' question includes deposits in savings institutions?

Mr. Crowley. No, sir; it does not.

Mr. Williams. They are not included?

Mr. Crowley. Would you like some detail on that, Mr. Williams? We have some figures here, if you would like to have us read them.

Mr. Williams. As far as I am concerned, no; unless someone else on the committee wants it more definitely than that.

Mr. Cavicchia. Does that figure of 36½ billions that you gave include sums deposited in savings banks and mutual banks?

Mr. Crowley. No; it does not; just commercial banks.

Mr. Williams. During the last year, or after the passage of the deposit insurance law and before the creation of this Corporation, as I understand it, there have been orders issued by the Federal Reserve bank and by the Corporation as well concerning the interest charges to be paid both on demand and time deposits in various banks that are insured.

Mr. CROWLEY. That is correct.

Mr. WILLIAMS. What have been the savings to the banks of the country by reason of those orders and their following out the instructions that were given to them with reference to paying no interest on demand deposits and limiting the amount that they would pay on time deposits?

Mr. CROWLEY. I do not know that we can give that to you. That is in our testimony, Mr. Congressman, and we will give it to you.

Mr. WILLIAMS. Perhaps I have your statement on that, but let me see if I understand it. Do I understand from your statement that by reason of that action on the part of the banks in not paying interest at all on demand deposits and cutting down the interest paid on time deposits there has been a saving to the extent of 26 cents per $100 during the year 1934?

Mr. CROWLEY. As the banks became more liquid, and as the demand for money became less, the banks themselves declined to pay interest on daily balances. That was prior to the Banking Act of 1933 Then, Mr. Congressman, in the Banking Act of 1933 it was provided they could not pay interest on demand deposits, and we then showed a saving that had been brought about by not paying interest on demand deposits. A percentage of that saving was brought about by the legislation in 1933.

Mr. WILLIAMS. The fact remains that that was done, regardless of the cause of it, and that the banks during the last year have saved about one-fourth of 1 percent on their entire deposits by having cut down the rate of interest paid to the depositors?

Mr. CROWLEY. That is correct.

Mr. FOX. Our figures are based on national banks, and the data is available for the last half of 1933, the 6 months subsequent to the passage of the act.

That shows that the savings to all national banks because of the passage of the Banking Act of 1933, which reduced the interest on time deposits and eliminated the interest on demand deposits, was 28 cents per $100 on deposits, 2 cents of which was due to a reduction in the rate of interest on time deposits and 26 cents due to the elimination of interest on demand deposits.

Mr. WILLIAMS. Then, instead of 26 cents, it is 28 cents per $100?

Mr. FOX. That is correct.

Mr. WILLIAMS. Which would be between a third and a fourth of 1 percent on all of the deposits in the banks, which in figures would amount to how much?

(At this point Mr. Crowley handed a paper to Mr. Williams.)

Mr. WILLIAMS. I would like to have that in the record, to show how much the banks of the country have served by reason of reductions in the rates of interest paid during the last year.

Mr. REILLY. Have the banks been reporting how much money they saved as interest on time and demand deposits?

Mr. CROWLEY. The banking law of 1933 forbids that.

Mr. REILLY. I know, but before that did not they make a specific report of the amounts of money that they paid on demand deposits?

Mr. CROWLEY. Yes.

Mr. FOX. The national banks filed reports of earnings and dividends every 6 months, and in that report is the section which details their expenses, and there are three items in that section.

Mr. GOLDSBOROUGH. Will you proceed, Mr. Williams?

Mr. WILLIAMS. It would be a simple matter of calculation.

Mr. FOX. It is about $43,000,000 per year for national banks.

Mr. WILLIAMS. $43,000,000 for national banks alone.

Have you any data showing the amount that has been saved by the Federal Reserve members and the nonmember banks?

Mr. FOX. We could put the information in the record for the Federal Reserve member banks. We did not until this year have information on the nonmember State banks. Therefore, we could not give you that information.

Mr. WILLIAMS. Your statement of a saving of 28 cents per $100 is based on the record of the national banks alone?

Mr. FOX. That is correct.

Mr. WILLIAMS. How does that compare with the State member banks that you know of?

Mr. FOX. I will have to put that in the record later on.

Mr. WILLIAMS. You will put that in the record for us?

Mr. FOX. Yes, sir.

Total savings in interest paid on deposits by State member banks were at the rate of $30,000,000 per year. Expressed another way, the savings in interest expense to State member banks amounted to 29 cents per year for each $100 of total deposits.

Mr. WILLIAMS. And you have no information at all with reference to the amount that the State member banks have saved on that item?

Mr. FOX. No, sir. That is not available at all.

Mr. WILLIAMS. And it is a fact, is it not, that the State nonmember banks have followed the same policy as the member banks and the national banks in that respect throughout the country?

Mr. FOX. I think so.

Mr. CROWLEY. I think that is generally true, Mr. Congressman. In some States they have not.

Mr. WILLIAMS. Now, it is also true, is it not, that you issued an order—and I refer to your Corporation—limiting the interest on time deposits to 3 percent, and then later on formulated, at least, another order bringing it down to 2½ percent?

Mr. CROWLEY. That is correct.

Mr. WILLIAMS. But that was never put into effect, was it? Some controversy arose over the legality of it?

Mr. CROWLEY. That is correct. A year ago last December the Federal Deposit Insurance Corporation and the Federal Reserve Board fixed a 3-percent maximum. Then last December the Federal Reserve Board fixed a rate of 2½ percent, and we did likewise; and then the controversy arose, and we withdrew our regulation.

Mr. WILLIAMS. Then the practice that has heretofore prevailed throughout the country of paying in certain cases interest on demand deposits is a thing of the past, is it not?

Mr. GOLDSBOROUGH. May I suggest to you, Mr. Williams, that in my section, in the First Congressional District of Maryland, they are still paying 2½ percent?

Mr. Williams. But that is not a fact so far as the order of the Board is concerned?

Mr. Crowley. The order of the Board was drawn, but a great many of the banks, as the chairman says, have followed along on the 2½ percent.

Mr. Williams. And they are following that not by your order or direction but because of their own inclination and perhaps a desire to be uniform with the order of the Federal Reserve System?

Mr. Ford. One big banking group on the coast did not do that. They offered 3 percent; and all of the other banks came to me and asked me to come down to see you to change it, which I could not do.

Mr. Crowley. May I say this, on that matter of time deposits, first, that I think that history will show that prior to the Federal Reserve Board and prior to the Federal Deposit Insurance Corporation issuing their regulations, in years gone by banks paid as high as 4, 5, and 6 percent for what we would term "time deposits." They offered all kinds of premiums, like blankets and clocks and savings banks, and the banks which perhaps should not have paid those high interest rates were the ones that were the most apt to offer to the depositor an interest rate that was not sound.

Now, the same thing was true of demand deposits. For instance, a great many of your national corporations would have $25,000 or $50,000 balances, and the banks would bid for that business; and in reality in a great many instances it was not of any particular benefit, and that was considered as an unsound practice. That is the reason why in the Banking Act of 1933 you eliminated that abuse, because it was an unwise and unsafe practice.

Now, the same thing goes for interest on time deposits. What the supervisory agencies wanted to bring about was that a bank not only paid to these people a reasonable rate of interest but also gave them back their principal, because in a great many instances where the bank paid 4, 5, and 6 percent, the depositors lost a very large percentage of their principal.

Mr. Williams. Is it your idea now that your Corporation should have the power to direct the members of your Corporation not to pay interest on demand deposits and to limit their payments on time deposits to 2½ percent?

Mr. Crowley. I think it would be a great contribution to your banking system if we had that power. There might be given sufficient authority, perhaps, that we might take into consideration the various districts of the United States in regulating that interest. In other words, we might find that in the East they were able to put in one rate of interest and in the West another, and under those conditions the thing to do would be not to make it all uniform, because in some parts of the country they get a little more money for their loans.

Mr. Williams. But that idea is not contained in this bill?

Mr. Crowley. No; it is not; but if you will read the entire Banking Act of 1935, it does give that power to the Federal Reserve Board.

Mr. Williams. Undoubtedly. I think there is no question but what the Federal Reserve Board has it.

Mr. Crowley. And it covers all insured banks in the new act that has been presented to you.

Mr. WILLIAMS. Do you mean by that that the provision with reference to the Federal Reserve Act will cover all insured banks?

Mr. CROWLEY. That is correct.

Mr. WILLIAMS. And that is on the theory that they will now have to come into the Federal Reserve System?

Mr. CROWLEY. That is correct.

Mr. WILLIAMS. But on the theory that we are going, perhaps, to have a lot of them insured that are not in the Federal Reserve System, what will we do about them?

Mr. CROWLEY. I think that it would be very helpful to the banking system if that were made a part of the permanent insurance act.

Mr. BIRDZELL. If you will turn to page 65 of your printed bill, H. R. 5357, you will find a provision there relating to interest. Shall I read it to you?

Mr. WILLIAMS. I think from what you have stated about it, it is not necessary to read it.

The point that I am asking about it is that there are some 8,500 banks of this country that are not in the System; and it is at least my view that they will not be in it, unless they want to be, and what will we do with them with reference to this interest charge?

Mr. BIRDZELL. Do you understand, Mr. Congressman, that this provision of the bill on page 65 that I have directed your attention to will enable the Federal Reserve Board to regulate the interest rate for that portion of those 8,500 banks that is insured?

Mr. WILLIAMS. I did not so understand it.

Mr. BIRDZELL. That is the provision of the bill.

Mr. WILLIAMS. Regardless of whether they are in the Federal Reserve System or not?

Mr. BIRDZELL. Yes, sir.

Mr. CROWLEY. As long as they are insured banks.

Mr. WILLIAMS. The point that naturally arises in my mind is, why should the Federal Reserve Board have that authority rather than the Insurance Corporation, if they are not members of the Federal Reserve System?

Mr. CROWLEY. It is only just a matter of uniformity; that is all.

You might have a situation where the Federal Reserve System would have one rate for national banks, and the Federal Deposit Insurance Corporation would have another one for State banks. That was the reason, I believe, for putting it all under the Federal Reserve Board.

However, our Corporation would welcome an opportunity to regulate the interest rates of the nonmember State banks.

Mr. WILLIAMS. Now, during the period of time since the banking holiday, there have been a great many concerted efforts on the part of your Corporation, the R. F. C., and others to recapitalize and rebuild the capital structure of the various banks throughout the country. I believe that we went into that to some extent the other day.

Mr. CROWLEY. Yes, Mr. Congressman.

Mr. WILLIAMS. And we reached the conclusion that perhaps half of them had been helped in that way.

Mr. CROWLEY. There have been pretty close to 6,000, and there are some to be done yet, so you won't be far out of the way in saying that close to 40 percent have been helped.

Mr. WILLIAMS. I would like to have in the record the figures showing the capital structure of those banks, say, as of March 1, 1933, about the beginning of the bank holiday, and as it exists at the present time.

Mr. FOX. It will not be possible to give it for March 1, 1933, for State nonmember banks. It will be possible to give the book capital for State nonmember banks as of the 1st of January 1934, virtually before most of the aid had been put into the banks. However, the book capital will not necessarily reveal what has been accomplished.

Mr. WILLIAMS. Unless we had the capital structure existing at the time these processes were begun, you could not tell what had been done in that connection.

Mr. CROWLEY. That is very difficult for this reason: Suppose that you had a million dollars in deposits or in assets; you could not determine the position that your capital structure was in just from the books of your bank, because perhaps you had not taken out your losses, and perhaps you had not set up any reserve for bonds or for depreciation, and you really cannot tell that without an examination, don't you see? In other words, we could not tell what condition the banks were in in March 1933 until first an examination was made of them.

Mr. WILLIAMS. I understand that, except that you could get it from the books themselves; the capital is there stated, by the books.

Mr. CROWLEY. Yes; but that would be misleading.

Mr. WILLIAMS. I understand that it may be, but I just wanted to know what that was as shown by the books; in other words, what was the capital of the banks of this country.

Mr. CROWLEY. I think the capital was about $6,000,000,000.

We could get that for June 30, and that would be satisfactory.

Mr. WILLIAMS. Yes. What is it now?

Mr. CROWLEY. About 6 billion dollars.

Mr. WILLIAMS. Do you mean by that that the capital structure of the banks of the country has not improved any during the last year and a half?

Mr. CROWLEY. Here is what happened: We might have had 6 billion dollars in March or June 1933, as far as their books were concerned. Now, then, they may have had a billion and a half of losses there that had not been deducted. When we came along with our rebuilding program, we eliminated the undesirable assets, and put capital back in.

Mr. WILLIAMS. But did you not also, in the case of a great many of the smaller banks, increase that capital?

Mr. CROWLEY. Yes; but we increased——

Mr. WILLIAMS. I mean not only increased the physical assets, but that you increased the book value? In other words, you raised the capital in many cases from $50,000 to $100,000?

Mr. BIRDZELL. Just word with respect to that.

It has been quite a general practice where preferred stock has been issued and sold to the Reconstruction Finance Corporation for a bank that issued and sold that prefererd stock to make a correponding reduction of its common stock, so that while the new capital has gone into the banks, the book capital remains substantially the same as it was before. That is the reason why the present book capital does not show much change from the book capital as it might have been shown before the rehabilitation took place.

Mr. WILLIAMS. Now, let us get at it from this angle. How much in public funds from the Reconstruction Finance Corporation, and how much in private funds have been put into the banks to rebuild and strengthen the capital structure during the last 18 months, or since the bank holiday?

Mr. FOX. Approximately 1 billion dollars has been put in by the Reconstruction Finance Corporation for recapitalizing the banks, and we are now estimating what the extent of the local funds that have been raised was, and while we have only gotten replies from 30 States, it already amounts to about $300,000,000 additional.

Mr. WILLIAMS. It will, perhaps, then amount to a billion and a half?

Mr. FOX. At least.

Mr. CROWLEY. I would say much in excess of that, Mr. Congressman. When you take into account your local contributions, reorganizations, and things like that, it will run far in excess of a billion and a half dollars.

Mr. WILLIAMS. In other words, the capital structure of the banking system of the entire country has been very materially and very substantially strengthened during the last 18 months?

Mr. CROWLEY. Pretty close to 50 percent of the banks, before we get through, will be practically rebuilt.

You asked whether we aided in the increasing of capital. Where we have rebuilt the capital structures of a great many of these banks, we have tried through the Reconstruction Finance Corporation and local contributions to build their capital so that they would have a ratio between deposits and capital which was larger than the ratio that they had before.

Mr. WILLIAMS. I was just going to ask you what has been your policy with reference to trying to create capital and establish a definite relationship between capital and deposits. I understood you to say that you had been making an effort to establish some kind of a ratio between the capital and the deposits of an institution. That has been your policy, has it?

Mr. CROWLEY. That has been our policy.

Mr. WILLIAMS. What is the ratio?

Mr. CROWLEY. Where a bank has been able to go all the way through, even though its ratio of capital to deposits might be less than 10 to 1, we have not disturbed it. Those were banks that had been able to carry themselves through, keep their capital intact, had a good earning capacity, and could build reserves and surplus. Where we rebuilt a bank we tried to rebuild on a 10-to-1 basis.

Mr. WILLIAMS. What I am trying to get is a general picture of the bank situation in this country now as compared with what it was during the 10 or 12 years preceding the bank holiday. When did we reach the highest peak in the number of banks in this country? I want to get what happened during that period.

Mr. CROWLEY. We reached it in 1920 or 1921.

Mr. WILLIAMS. What was it in numbers?

Mr. CROWLEY. About 30,000 banks.

Mr. WILLIAMS. At the present time there are how many?

Mr. CROWLEY. 15,000.

Mr. WILLIAMS. In other words, we have half as many banks now as we had in 1920—later than that, was it not?

Mr. Crowley. About 1920 when your failures started.

Mr. Fox. 1921, exactly.

Mr. Williams. Yes; 1921 and 1922. And at that time the bank deposits were about 50 billions?

Mr. Fox. Thirty-eight and a half billions in 1921.

Mr. Williams. When they were at their peak?

Mr. Fox. When the number of banks was at the peak the deposits were not at their peak.

Mr. Williams. The bank deposits were at their peak about 1928 and 1929?

Mr. Fox. 1930; 59.6 billions.

Mr. Williams. Now, during that period from 1922 to 1932 there was the failure of some 11,000 or 12,000 banks, was there not?

Mr. Crowley. That is right.

Mr. Williams. Of all kinds and characters, in all sections of the country, I take it?

Mr. Crowley. More of them, Mr. Congressman, in the Northwest. Your early failures first came, I think, in South Dakota, and then in northern Iowa—the whole Middle Western country.

Mr. Williams. There were, of course, a number of causes for that. Is it your opinion that we were overbanked; that we had entirely too many of them?

Mr. Crowley. Yes; we had too many banks, Mr. Congressman, that could not make a sufficient return on their investments or could not set up reserves to take care of their losses. In other words, a bank that has a $6,000 gross income, from which it must pay its overhead and set up its reserves for losses, it remains very difficult for it, if it has a $2,000 or $3,000 loss in any particular year, to take it currently.

Mr. Williams. That was one thing; that there were too many banks.

Mr. Crowley. And also later, from 1930 on, our banks suffered terribly by bond depreciation and defaults.

Mr. Williams. It was due to another reason, to the fact that they had invested their money in securities of different kinds at inflated values?

Mr. Crowley. That was a contributing factor to the banking trouble, and, of course, your economic situation.

Mr. Williams. Was it not due to the fact that there had been rather loose supervisions on the part of the authorities of the State and Government?

Mr. Crowley. You have in this country, under the State system, 48 different types of supervision. It is very difficult to have State supervision that will be as efficient as where it is a long way removed from local pressure.

Mr. Williams. And there were other contributing causes to the enormous number of failures that we had during that time?

Mr. Crowley. I think that the large contributing cause, Mr. Congressman, was your economic collapse. For instance, in the Middle West, when your banking trouble started in 1921, that was the beginning of your agricultural trouble. You can say that as your agricultural trouble became more severe, your bank failures increased very materially. Furthermore, they were frozen up in farm and chattel mortgages and also in bonds that had depreciated to a point where they could not sell them without taking a severe loss, and they had nothing to charge their losses to.

Mr. WILLIAMS. It is the hope and the intention now to eliminate a great deal of that, is it not? This very act itself tries to furnish a market for long-term rediscount paper?

Mr. CROWLEY. That is correct.

Mr. WILLIAMS. And to avoid that situation in the future, and also by having supervisory control, regulatory control over these various institutions by your examinations and your reports, it is the hope to eliminate many of the bad practices that have existed before, is it not?

Mr. CROWLEY. That is right.

Mr. WILLIAMS. And, of course, it is also the intention further to prevent the establishment of any more banks where they are not needed?

Mr. CROWLEY. That is correct.

Mr. WILLIAMS. And by means of all of those things, you hope to avoid the recurrence of this condition which has come upon us and caused so many failures among these banks in the past?

Mr. CROWLEY. That is correct.

Mr. WILLIAMS. Now, I want to get back to this question: What are you going to do, if this act is passed as written, with the 8,500 banks that are not members of the Federal Reserve System?

Mr. CROWLEY. You mean as to what we are going to do with them in 1937?

Mr. WILLIAMS. Yes.

Mr. CROWLEY. I hardly think that that is a fair question to ask me.

Mr. WILLIAMS. You do not think that that is fair?

Mr. CROWLEY. I do not mean that personally.

Mr. WILLIAMS. The fact is that this law would provide for that, would it not?

Mr. CROWLEY. This law provides for them to join the Federal Reserve System in 1937.

Mr. WILLIAMS. We have had a Federal Reserve System in effect for 20 years, have we not?

Mr. CROWLEY. Yes.

Mr. WILLIAMS. And we have now 8,500 banks in the country that have not seen fit to join it so far?

Mr. CROWLEY. That is correct.

Mr. WILLIAMS. I notice that the expression is used throughout this act, "insured banks", and I understand that you have a definition of an insured bank in your bill, but there is not any such thing as an insured bank now, is there?

Mr. CROWLEY. I assumed that all banks that are insured are insured banks.

Mr. WILLIAMS. They are simply members of a temporary fund.

Mr. CROWLEY. That is correct.

Mr. WILLIAMS. And there has not been a bank that has come in and bought stock?

Mr. CROWLEY. No, sir.

Mr. WILLIAMS. And insured under the permanent policy?

Mr. CROWLEY. No, sir.

Mr. WILLIAMS. Now, when July 1, 1937, comes and this law is enacted, all of these nonmember State institutions that are now in the temporary fund will have to come into the Federal Reserve System or get out of the insurance corporation?

Mr. CROWLEY. That is the law.

Mr. WILLIAMS. I am very much concerned myself about the 8,500 banks, because they are scattered from one end of the country to the other, especially in the southern part of the country, and the rural sections and small communities, and I, for one, have not reached the conclusion yet that there is not a place in our system for a local independent, unit bank. I do not believe that they ought to be required, if they do not see fit to do so, to come into the Federal Reserve System. You have means provided in this very act by which you could supervise them rather strictly, by which you can examine them, and you have a provision by which you can put them out of the System if they engage in any unfair or unsound banking practices of any kind or character, but it does seem to me that we ought not to place in this bill a provision requiring them against their wishes to come into the Federal Reserve System in order to get the benefit of the insurance feature.

Mr. GOLDSBOROUGH. Mr. Cavicchia.

Mr. CAVICCHIA. Pursuing the line of thought that Mr. Williams has been following, I would like to ask this: Why force these 8,500 banks into the Federal Reserve System if they do not wish to join? Is it not protection enough to the stockholders and to the depositors that they are members of the insurance funds?

Mr. CROWLEY. I think the thought is, Mr. Congressman, that it brings about a greater unification of banking, and perhaps better control of your monetary system, if you have them all in the Federal Reserve System.

Mr. CAVICCHIA. Will it cost these banks any more to become members of the Federal Reserve System than if they had stayed out?

Mr. CROWLEY. They will have to pay for their stock, but it will not be a great burden.

Mr. CAVICCHIA. To get back to the elimination of interest on demand deposits, many insurance companies, as well as municipal authorities, used to have large deposits on which they received throughout the East something like 2 percent on demand deposits. Has not the fact that this interest has been terminated forced these people to go into the bonding field raher than to have the money on deposit on which they receive no interest?

Mr. CROWLEY. Well, of course, that is purely a matter of their own judgment. If an insurance company has a million dollars of excess reserves and it can find a place to employ it, I presume that it is good business for them to do it.

On the other hand, you cannot expect a bank to pay 1 or 2 percent on daily balances when the money is only lying there idle.

Mr. CAVICCHIA. Has there not been a great deal of complaint on the part of municipal authorities because they have lost this 2 percent on demand deposits?

Mr. CROWLEY. I think that that is correct, that there has been complaint, but I do not think it is justifiable. I mean by that that they might just as well wish for 4 percent as to wish for 2 percent when the banks cannot pay out the 2 percent. There is no rime or reason why I should, if I were in the banking business, take a $100,000 account from you and pay you 2 percent for it, and then leave it in the vaults or in the Federal Reserve banks and not employ it.

Mr. CAVICCHIA. That is true, because of the conditions existing now, but if a time should come when the banks can employ money to advantage and get good returns for it, if you pass this law they will not be able to pay any interest, because the law forbids it.

Mr. CROWLEY. Mr. Congressman, that is not in this law. That law was passed in 1933.

Mr. CAVICCHIA. But the fact is that we have that law.

Mr. CROWLEY. That is right.

Mr. BIRDZELL. One further suggestion there, Mr. Congressman. In the Banking Act of 1933, which forbids the payment of interest on demand deposits, exception is made where, under local law, State laws, interest is required to be paid on public deposits.

Mr. CAVICCHIA. Now, to go back to that 29 cents per $100 that has been saved through the law of 1933, does this 29 cents per $100 that the banks have saved in interest cover their costs of going into the temporary insurance fund?

Mr. CROWLEY. It would more than cover their costs on one-twelfth of 1 percent.

Mr. CAVICCHIA. In other words, the banks do not have to meet an unreasonable demand to join in your fund, inasmuch as they have saved 26 or 27 cents on every $100?

Mr. CROWLEY. I do not think that we have presented anything in which offers any great obstacle to the banking system of the country.

Mr. CAVICCHIA. You mean, so far as the extra cost is involved?

Mr. CROWLEY. That is correct.

Mr. CAVICCHIA. That is all.

Mr. GOLDSBOROUGH. Mr. Reilly, you were not here yesterday.

Mr. REILLY. I do not have any questions.

Mr. GOLDSBOROUGH. Mr. Cross.

Mr. CROSS. Now, Mr. Crowley, going back to the questions put to you by Mr. Williams, you said that the bank crash was started in the Western States. That was caused by falling prices of the commodities of the people who did business with those banks, was it not, and that caused falling prices in lands, did it not, and that reflected finally on the eastern sections and caused a decline in the prices of stocks, and that destroyed the purchasing power of the country and brought on your bank crash?

Mr. CROWLEY. I think that is correct.

Mr. CROSS. Now, under title II you say that you can get a sound banking situation, that tile II seems to be the key to the situation. The question is to keep up your prices, and in order to control prices that you should have a unified banking system. In other words, if you have a whole bunch of banks that are uncontrolled in the credits that they handle, if there are too many of them, they affect the whole structure, and if they do not come into the system where they can be regulated as to their credits, it directly affects price levels. Do you see the point?

Mr. CROWLEY. I agree with you that your bank failures were largely due to your economic collapse starting back in 1921.

Mr. CROSS. Surely.

Mr. Crowley. However, there were other factors such as overbanking conditions, poor judgment, or not being able to foresee that land values were too high, and things like that.

Mr. Cross. Was not the overbanking situation brought about by inflated credit, by abnormally high prices at that time of lands and the things that securities were braced on, and the banks figured that they could all make money, and everybody was taken into the banking business?

Mr Crowley. I think that is right.

Mr. Cross. And, of course, when the crash came, prices went down, securities went down, and they were all blown up.

In reference to the question of paying interest on checking or cash deposits, you remember that we had that question up, as you say, in 1933.

Mr. Crowley. Yes.

Mr. Cross. And the fellows that had big checking deposits the banks got competing for, and they were paying too much interest on them, and the mass of the little fellows knew nothing about that, and, in addition, the big fellows also knew what condition the banks were in, and they pulled their money out, but the little fellow got caught.

In other words, there was a vicious system brought about by the banks bidding on the checking deposits of the big fellows.

Mr. Crowley. That is correct.

Let me say one thing here, so that you will understand my viewpoint on the banking system. I think that the Federal Deposit Insurance Corporation must have these powers that we are talking about, but I do not want to go on record as saying that the entire State system should be eliminated. I think that your State system can be a very major factor in your banking system.

There are two types of banks in this country. You have your larger banks, which by the very nature of their type of business cannot afford to make the type of loans that are made in the small community, because it costs them too much money.

Your community bank does contribute to your local community a type of credit that I think is very essential in your whole financial picture, and I do not believe that it is necessary for us to eliminate in a wholesale way that type of bank. I think the think that we should be very careful about is that we do not get back to that overbanked condition, but we should do everything we possibly can to try to preserve the banks that we have now, as long as they have an opportunity of serving the people of those communities.

In other words, let us take a bank of $250,000 or $500,000 in deposits. To my mind, they can be a large factor in the local community and lend a larger percentage of their money locally in the future than they have in the past if they will only profit by their experience in the past in making those loans so that on maturity they will be reduced from time to time and not be permitted to become frozen.

Mr. Cross. Of course, those banks would not belong to the Federal Reserve System, and the danger of that seems to be that the Federal Reserve Board, not being able to control their credits or the landings of those banks, could not bring about the situation which you say is desirable.

Could this deposit insurance feature here be so administered so that at least your Corporation would have something to say about their credit activities?

Mr. Crowley. I think that as long as you have the State system, Mr. Cross, that the State authorities must have the primary responsibility for the supervision. Now, the only place where I see that we are entitled to supervise is where that supervision is necessary for the protection of our Corporation.

I do not like to get into the matter of the Federal Reserve, because I think that is a matter for Mr. Eccles, and I much prefer not to go into anything that would interfere with his end of this bill, if you have no objection to it.

Mr. Cross. Yes; I understand.

That is all.

Mr. Goldsborough. Mr. Gifford.

Mr. Gifford. I want to pursue the line of inquiry with reference to the part of this bill that deals with the examination of banks.

I wish I had with me letters that I have received, with respect to the fact that the Comptroller was out making speeches all over the country, calling on the banks to loosen up on their credit, whereas before that we found that the examining department of the Comptroller's office had put a great deal of fear into the bankers, so that they did not dare to loan.

The whole tenor of this bill is to get a pretty good grip on these banks by examination, and this assessment of one-twelfth of 1 percent would be sufficient so that you could control the conduct of the banks, and you want to force them to carry burglary insurance and other insurances, and, if they do not carry them, you order them and charge them up to the bank.

Now, as I read this bill, and after having heard your statement, you base a great deal of your possible success on your opportunity to make examinations just as often as you like, so that you may make the banks conform to anything that you may want them to do, and that sort of thing. Is not that asking a good deal?

Mr. Crowley. No; I do not think that there is a single thing in our bill that goes too far.

Let me say this to you, that, in the first place, the law that was passed said that we may take these banks in on a test of solvency. Now, we all know that a bank that only has sufficient assets to meet its deposit liability on any kind of a forced liquidation could not pay out its deposits. Furthermore, our whole trend of banking in this country is based on the theory that first the stockholder shall have an equity in this bank, because it is a capitalistic system. So that when we started in January 1934 after taking these 7,800 banks in, we were faced with the problem of going out to determine their position.

Now, our job, first, was to find out really what the condition was, and in order to find out what the condition was, we had to try to determine the value of their assets, and we were trying to do that, of course, at a time when values were at perhaps a very low ebb, and perhaps it was necessary sometimes to be pretty severe, but my own judgment is that when we classify an asset, a good asset in the bad column, that we perhaps classified as many bad assets in the good column.

Mr. GIFFORD. Do you understand that recently there has been a tremendous change in attitude on the part of bank examiners in the whole country, and instructions must have been given to them to have a different viewpoint?

Mr. CROWLEY. As far as Federal Deposit Insurance is concerned, there has been no change in the attitude of our examiners, because our whole program has been based upon, first, putting the banks in a sound position as far as capital is concerned. After you once get the banks in a sound capital position, then you may not have to use as severe a yardstick in a wholesale way as you had to at first.

Mr. GIFFORD. I am not criticizing your method of examination, but national bank examinations in the last 2 or 3 years. Do you not know that there has been a very great change in the method of making bank examinations lately, where slow loans in a bank have not been persecuted as formerly?

Mr. CROWLEY. I do not know what the policy of the Comptroller's Office is.

Mr. GIFFORD. Did you not see an article in the newspapers, to the effect that the President himself had severely criticized the strictness of bank examinations?

Mr. CROWLEY. Let me say this to you on the matter of the criticism of slow loans. You may criticize a slow loan if the bank has too large a percentage of them, or if the bank is badly frozen. The easing up of the criticism of slow loans has been due largely to the fact——

Mr. GIFFORD. That is all I asked, and you agree.

Mr. CROWLEY. Wait a minute—if it has been done.

Mr. GIFFORD. Has it been done?

Mr. CROWLEY. I presume it has, at least in places where the banks have such extreme liquidity that there is no necessity of forcing liquidation.

Mr. GIFFORD. Do you think that you could still hold these banks as members of your corporation if they are subjected to all of these things?

Mr. CROWLEY. We have had in here 22 State commissioners for conferences on the matter of examinations and related topics.

Let me say that in the matter of rebuilding capital, in the matter of local contributions, time after time we have had a State commissioner come to us and ask us to exert our influence, because on account of local conditions he could not do it, and he has asked the Federal Deposit Insurance Corporation to exert pressure in order to put that bank back in shape.

So far as that examining program is concerned, every State commissioner who wants a good State banking system will agree that if we are going to carry such a high percentage of liability we have to have ways and means of protecting ourselves.

Let me say this to you: That in the large percentage of the State banks we are insuring them better than 70 percent. I think that there are some 9,600 that we are insuring up to 80 percent. That is a tremendous responsibility.

Now, on the matter of burglary insurance, the reason we asked for that is that a good many of the States have no legislation at all that gives the Commissioner the power to force a bank to carry a reasonable amount of insurance on its officers or employees. Already, out of the 11 banks where we have paid out, we have had a very unfortunate experience. If they had had some adequate insurance, it would have helped the stockholders very materially.

We do not propose, you understand, to do that in the case of a wholesale majority and put an unnecessary burden on those banks. We must be reasonable in all of our demands.

Mr. GIFFORD. I am wondering what the cost of those things will be to the bank and what you insure them against?

Mr. CROWLEY. We certainly do not want to pay for all of their mistakes without having any right to try to get them to correct them.

Mr. GIFFORD. Do you want them to insure themselves against every conceivable thing, so that your corporation will not have any liability?

Mr. CROWLEY. No; but where they have not sufficient burglary insurance and protection and sufficient surety coverage on their employees, I see no reason why they should not carry it as a matter of protection to themselves and their own stockholders.

Mr. GIFFORD. Do you think that it is a fair treatment, and do you think that it is a safe treatment of a bank to demand of it a certain kind of report, and if it does not publish it in 5 days, to fine them $100 a day?

Mr. CROWLEY. I think that you are exaggerating that a little bit. The purpose of the authority to publish reports is this, that a great many of your bank statements in the past did not really show the true conditions of the banks.

Mr. GIFFORD. Whose fault was that?

Mr. CROWLEY. I think it was the fault of the entire system.

Mr. GIFFORD. Do you mean to say that our present national bank system is not sufficient to show the true condition of the banks?

Mr. CROWLEY. You take the old condensed statements gotten out by national banks and State banks for years; they did not show the market value of their bonds or the reasonable value of their loans.

Mr. GIFFORD. Did not they show the last demand of the bank examiner in connection with the market value of those things?

Mr. CROWLEY. Oh, no; that has never been in a statement.

Let me say this to you. I think that you are starting out on a different basis now. We are starting out anew, with the banking system practically rebuilt and values way down.

Mr. GIFFORD. Do you not see that you are adding considerably to the present burden of the banks by way of these examinations, and, secondly, that these examinations may be so irritating that many banks would rather not belong?

Mr. CROWLEY. No. The great majority of the banks give to our examiners every kind of cooperation, and do not seem to be irritable because we are trying to get a true picture of their institutions.

Mr. GIFFORD. Then your answer would be that they would not object to these things?

Mr. CROWLEY. A certain percentage, yes, would object, but I do not believe that that is the answer. Our corporation was set up for the protection of depositors, not for the protection of the bankers. We are trying to cut the losses to the depositors and of this corporation down to a minimum, and that is what our job it.

Mr. GIFFORD. And, in order to protect the depositors, you want to get control of the banks?

Mr. CROWLEY. You can call it control or what you please, but we are insuring 80 percent of the deposits in 9,600 banks in this country, and we have to do whatever is necessary to cut down their losses, within reason, of course.

Mr. GIFFORD. My question is really friendly. I am simply asking you if these irritating things that you are asking for are not lessening the number of banks that might belong.

Mr. CROWLEY. I do not think so.

Mr. GIFFORD. Are your examiners under civil service?

Mr. CROWLEY. No; they are not.

Mr. GIFFORD. Are the national-bank examiners under civil service?

Mr. CROWLEY. There are no bank examiners under civil service.

Mr. GIFFORD. Do you train them so that they all use about the same methods, or do you tell them that they must not follow any fixed rule but use their own judgment in the case of, say, a bank that has too many slow loans in proportion to the assets?

Mr. CROWLEY. Let me say this to you, that bank examiners are like any other human beings. Some are good, and some are bad; and, as far as their classification is concerned, you understand that after they make their classification, it is reviewed again in supervising office by a reviewing committee, and even the reviewing committee may make a mistake.

Like any other persons who get some authority, there is always a certain percentage of them that become autocratic, but we try to be as sympathetic as we can.

Mr. GIFFORD. The Comptroller wrote me a letter stating that he had had but one or two cases where a bank had been dissatisfied with the examinations, and where it had asked for a reexamination. I wonder if that is because the officials of that bank wanted so badly to get rid of the examiner that they did not want to see him again?

Mr. CROWLEY. I do not know about that.

Mr. GIFFORD. Do you not think that when an examiner walks into a bank, it is a very irritating thing to the officials of that bank?

Mr. CROWLEY. No; I do not agree with you there. I think that the average examiner during this entire depression has certainly been very helpful to the bankers. However, as I say, there are exceptions to all rules.

Mr. BIRDZELL. May I add one word in reference to examinations? The Corporation is working on a program in which it has solicited the cooperation of the banking departments in all of the States on the matter of examinations for the very purpose of making the examinations a matter of as little burden to the banks as possible.

The program that we are working on contemplates that where a State law might require two examinations of a bank a year, that the banking commissioner would be authorized to accept the report our examination in lieu of one he might make himself, and also that provision be made so that the Corporation might receive the reports of examinations made by examiners of the State administration.

Mr. GIFFORD. You think that any more than two examinations a year would be irritating?

Mr. BIRDZELL. We would have two wherever the State law requires two.

Mr. GIFFORD. But you think that any more than two would really be an irritation?

Mr. BIRDZELL. I would think so.

Mr. CROWLEY. I think it would be unnecessary except in some unusual conditions.

Mr. BIRDZELL. I might say that that suggestion is being very favorably received in the various States.

Mr. GIFFORD. But you are asking us here for permission to make examinations just as often as you want to.

Mr. CROWLEY. If you restrict us as to how many times we can go in, there might be a condition where, in order to protect ourselves, we might have to go in at some other time. We might find a bank in a bad condition this morning that we were in last week, and we want to be able to go back and correct that. That is the reason why we cannot limit it.

Mr. KOPPLEMANN. In the light of what Mr. Gifford has been questioning you about, perhaps it would be in order to ask Mr. Crowley——

Mr. GOLDSBOROUGH. Mr. Koppelmann, we are attempting to take the Members in regular order.

Mr. KOPPLEMANN. I beg your pardon.

Mr. GOLDSBOROUGH. Mr. Spence.

Mr. SPENCE. When the banks joined the temporary fund, you levied an assessment of one-fourth of 1 percent on the insured deposits, did you not?

Mr. CROWLEY. That is corect.

Mr. SPENCE. And now the one-twelfth of 1 percent will be levied on the entire deposit liability?

Mr. CROWLEY. That is correct.

Mr. SPENCE. What will be the difference in the amount realized from the one-fourth of 1 percent on the insured deposits and one-twelfth of 1 percent on the entire deposit liability?

Mr. CROWLEY. We received about 38 or 39 million dollars under the one-fourth of 1 percent, and we will receive about 30 million dollars under the one-twelfth of 1 percent; but you understand, Mr Spence, that we could only call, during the temporary period, for an additional one-fourth, whereas one-twelfth is an annual premium payable each year, which must be charged to the bank's overhead.

Mr. SPENCE. You did levy the full assessment?

Mr. CROWLEY. No; only one-half of it. We never levied the other one-half.

Mr. SPENCE. What percent of the amount of deposits is now insured?

Mr. CROWLEY. Forty-four percent in all, but I think that we ought to read to you the insurance figures by size groupings, because that is very necessary for you to get the picture.

Mr. FOX. According to the total liability size groupings, banks with $100,000 or less in total deposits, of which there are 1,500 now insured, are insured up to 92 percent of their total deposits.

Banks in the next size grouping, from $100,000 to $250,000, of which there are approximately 3,600, are insured up to 87 percent of their total deposits.

Banks in the next size group, $250,000 to $500,000, of which there are approximately 3,100, are insured up to 83 percent of their total deposits.

In the next size grouping, $500,000 to $750,000, of which there are approximately 1,500 banks, they are insured up to 80 percent.

From $750,000 to $1,000,000, of which there are 950, they are insured up to 78 percent.

From $1,000,000 to $2,000,000, of which there are 1,600, they are insured up to 75 percent.

From $2,000,000 to $5,000,000, of which there are about 1,100, they are insured up to 70 percent of their total deposits.

From $5,000,000 to $15,000,000, of which there are only 630, they are insured up to 50 percent of their total deposits.

$50,000,000 or over, there are about 100, and all of those banks are insured about 26 percent.

Mr. BIRDZELL. For the record, where Mr. Fox said up to a certain percentage, the average is meant.

Mr. SPENCE. Since 1921, according to this statement, including 1934, there have been 2,548 national banks suspended and 11,004 State banks suspended.

What percentage of the national banks were suspended, and what percentage of the State banks?

Mr. CROWLEY. Of course, as you go down your ratio, your percentage always changes.

Mr. SPENCE. Was a great number of the State bank failures caused by insufficient supervision or because of the inherent weakness of the bank?

Mr. CROWLEY. I would say it was undoubtedly both.

Mr. SPENCE. In other words, there are a good many small communities where they have two or three banks and where they only need one. Is not that true of the State banks?

Mr. CROWLEY. That is right.

Mr. SPENCE. Did that not to a large extent cause the failure of those banks more than insufficient supervision?

Mr. CROWLEY. In a great many of your States, Mr. Spence, the State supervisors did not examine their banks with any great regularity. I have known of some States that did not examine some banks for 2 years, and possibly sometimes a little longer, and then a great many of the State laws did not give the supervisors perhaps sufficient authority over their banks, and in a great many instances, on the matter of licensing new banks, the Commissioner would decline a charter and perhaps then they would go to some board and the board would override the Commissioner and grant the charter in a community such as you are talking about.

Mr. SPENCE. I have received some letters from some of the smaller bankers, in State banks, and they say that they now see no advantage in becoming members of the Federal Reserve System.

What is your opinion about that, outside of belonging to the insurance fund?

Mr. CROWLEY. I think this, that if your Federal Reserve System is liberalized to the point that farm mortgages may be discountable, certainly there is going to be an advantage to bank in availing itself of that opportunity. In other words, in the matter of seasonal borrowings, or where they perhaps have a temporary sloughing off of deposits, there is an advantage to a bank in having some place where they may rediscount their long-term loans.

Mr. SPENCE. Do you think that that will overcome any of the other disadvantages that might accrue to them by reason of being a member?

Mr. CROWLEY. Mr. Spence, I do not like to get into a discussion on the Federal Reserve provisions at this time. Mr. Eccles is coming and he will present his information, and I am sure that we will all be together on it.

Mr. SPENCE. Did you give us the percentage of deposits in the insured banks?

Mr. CROWLEY. We just read it to you.

Mr. SPENCE. In numbers?

Mr. CROWLEY. On your bank closings? Do you mean the depositors?

Mr. SPENCE. Yes.

Mr. CROWLEY. It is over 98 percent. Almost 99 percent of all of the depositors in the country, including all the banks, are insured up to $5,000. In other words, their balances are under $5,000.

If you were to take all public funds out of your smaller banks where they are insured 95 percent, I think you would find perhaps only one account in such a bank that was more than $5,000.

Mr. SPENCE. You think there is a justification for including all of the deposit liability of the bank within the scope of this program?

Mr. CROWLEY. Yes; for this reason, that I think that the responsibility of the Federal Deposit Insurance Corporation and their contribution, as I said many times here, cannot be the paying out of that loss. People generally have lost confidence in the banking system on account of the severe losses that they have had during the last 12 years, and while the Federal Deposit Insurance Corporation has had a psychological effect in the way of restoring confidence, we must not do anything that is going to destroy that confidence in the Corporation. Otherwise you are again going to have losses and withdrawals from your financial institutions.

I think that Federal Deposit Insurance is the only vehicle in the banking system that can help to correct this, and I think that it is a long-term proposition over a period of a great many years, and that the banks generally can well afford to make their contribution to it for the benefit of the entire banking system. I do not think that it is unreasonable in any degree.

Mr. SPENCE. It not only insures the $5,000 liability, but it has an effect upon all of the depositors in the banks?

Mr. CROWLEY. That is right.

Mr. SPENCE. Just one other question. On page 12 of your bill, in reference to new banks, it says:

> Notwithstanding any other provision of law, its franchise, property, and income shall be exempt from all taxation now and hereafter imposed by the United tSates, or by any Territory, dependency, or possession thereof—

and so forth.

That would exempt a bank building.

Mr. CROWLEY. No. That is where you set up a Federal deposit bank during the time that the local stockholders are raising money in your own community. Just as soon as the local stockholders come in and take things over, then it becomes regular, taxable money.

Mr. BIRDZELL. The term "new bank" is defined in the first section of the act, and it is confined only to a new national bank set-up.

Mr. SPENCE. You do not contemplate that that bank will lend money on real estate? Is that your idea?

Mr. CROWLEY. It should not during our term of office. We would not buy any real estate. Ours is really a bank that carries on during the interim in a community where they need banking facilities until the local people can take its place.

Mr. BIRDZELL. It can make no investments except in Government bonds.

Mr. SPENCE. That is all.

Mr. GOLDSBOROUGH. Mr. Wolcott.

Mr. WOLCOTT. I notice that the proportion of the losses of banks other than national banks seems to be materially less than the proportion of losses of national banks. Could that be due to the fact that there are so many small units in State banks?

Mr. CROWLEY. You mean in the State system?

Mr. WOLCOTT. Yes.

Mr. CROWLEY. Yes. You take your number of failures, they are largely in your small State system.

We have an analysis of that, if you would like to see it.

Mr. WOLCOTT. As I understood you, the trust deposits were divided so that the trust company having deposits in a bank could have insured up to $5,000 each of their accounts as they carried them on their books.

Mr. BIRDZELL. If the trust company were a member of the Insurance Corporation?

Mr. WOLCOTT. Yes.

Mr. BIRDZELL. Yes.

Mr. WOLCOTT. With respect to public money, where a county or municipality determines on a particular bank as a depositary for its funds, that is usually kept in a lump-sum deposit?

Mr. BIRDZELL. Yes.

Mr. WOLCOTT. However, on their own books, they carry it as grades, highways, sewers, contingent, and so forth.

Would the municipality have this fund guaranteed as a lump sum, or would it be guaranteed according to the manner in which it was carried on the books?

Mr. BIRDZELL. According to the manner they are owned.

For instance, if a city carries its deposit in a bank, and it places its funds divided, we will say, for general fund purposes or for some specific purpose for which funds may be appropriated, so that it keeps its books separately, so that it can keep account of deposits withdrawn or deposited for particular purposes, nevertheless those are city funds and they must be combined for the purpose of insurance; but, on the other hand, school funds may be deposited by the same treasurer as deposits of city funds, and yet the schools, being a separate corporate entity, would separately own whatever funds were deposited and the school corporation could make a separate claim.

Mr. WOLCOTT. Let us take, as an example, a county where they have a general fund, and then they have a drainage fund, and they have a highway fund and a school fund, and then a fund into which go the collections made by the county treasury for the benefit of the townships, where the county treasurer acts on the matter of delinquent taxes as the agent of the township, your criterion is as to whether these funds are held to the credit of the distinct political subdivision and political entities of that county?

Mr. BIRDZELL. Yes. It may be different in the case of your drainage funds that you speak of, or your——

Mr. WOLCOTT. Irrigation district?

Mr. BIRDZELL. Irrigation district, or something of that sort, where that is a special-assessment district and as such would be the proceeds of special assessments levied. The same may be true of your highways. In that case the drainage district or the highway district would be considered a separate political entity.

Mr. WOLCOTT. Then, in order to get the full advantage of this insurance, the municipal corporation or the State legislature should provide that the school district and the drainage district or irrigation district, sidewalk district, or highway district should be considered to all intents and purposes a political entity of the county?

Mr. BIRDZELL. It would depend on whether or not they are in fact so. If they are, they are getting the benefit of insurance now.

Mr. WOLCOTT. The average county or municipality makes a separate levy for school purposes. They make a separate levy for highway purposes and for all of these different purposes, and carry them separately on their tax rolls.

Do you think that under that system they should be entities to the extent that each of these funds would be insured up to $5,000?

Mr. BIRDZELL. It depends upon whether the proceeds of the city tax for school purposes belongs to the city, or whether they have a separate corporate organization. If it be a separate organization, and the tax was intended for that corporation, then that corporation would own the deposits.

Mr. WOLCOTT. Of course, there is a great deal of overlapping there in their prerogatives, and the municipality or city or county always exercises a certain supervisory duty with respect to all of these other entities, and while perhaps specifically these funds belong to the district, at the same time they belong to the county and the county is made responsible for them.

Mr. BIRDZELL. The county might be merely the agent for collecting the funds. That is true in many instances, and it might be that they would employ one common treasurer who would have the control of the deposits, but nevertheless the funds, when they go on deposit, are certainly going on deposit to the credit of the particular municipality that is authorized to expend them. That being the case, they would belong to that municipality, and that municipality would be getting the benefit of the insurance.

Mr. WOLCOTT. The criterion seems to be whether any part of this fund which is deposited by the county or city treasurer is intended to have been deposited in connection with the credit which he gives that entity on his own books?

Mr. BIRDZELL. Yes; that is correct. We have even gone to the extent in some cases of giving assurance that sinking funds actually belong under the peculiar law that they be rated under to the holders of the bonds rather than to the municipality. There is one instance that we have come across where the ownership of the sinking funds is so definitely fixed by the State law under which they are collected that it can be said definitely that they belong to the owners of the bonds rather than to the municipality. It is a question of ownership in the last analysis.

Mr. WOLCOTT. Carrying out that same thought a little further, when the banks in Michigan closed an endeavor was made to interpret the law in such a manner that the funds of correspondent banks would be preferred. We found that under certain rulings of the State courts and of the United States Supreme Court, as I recall, they had no preferred status.

Mr. BIRDZELL. That is right.

Mr. WOLCOTT. Under the present law, or under these changes as contemplated, a small bank having deposits with a larger bank would only have $5,000 of its deposits insured?

Mr. BIRDZELL. Yes; that is correct.

Mr. CROWLEY. Do you mean $5,000 of public funds?

Mr. WOLCOTT. No. I mean a small bank in a city, we will say, of 30,000 or 35,000 in close proximity to a large city where there are large banks, and frequently, to safeguard their funds, they have amounts deposited with the larger banks. In my own case, if I may use it, we are located about 60 miles from Detroit. When the crash came, we found that our banks in Port Huron had deposited their reserves and the money that they were not using daily in the large banks in Detroit, so when the large banks in Detroit closed, all of the ready cash that our banks had to do business was what they needed to carry on their daily business, and their reserves were tied up. We found instances where some of our banks had their reserves in the Chicago banks, and I know of one instance where the cashier of the bank went to Chicago and drew out $80,000 of reserves and came back with them in his inside pocket.

Of course, that precipitated the national bank closing; no question about it, and I wonder if it would be feasible to provide for the isolation of those funds in some manner so that it would prevent the recurrence of a situation such as we had in Michigan, where one or two large banks are closed by arbitrary authority, and where it would not necessarily compel the closing of 500 other banks.

Mr. CROWLEY. We went into the matter of the entire bank deposits, and it is my honest judgment that that should not be touched until we have had an opportunity to study that thing a little further. There is a lot to what you have said, but we have only had 1 year's experience here, and perhaps next year from our experience we can make a recommendation to you that may correct that difficulty. It does increase our liabilities, as you know, tremendously, if we take on the entire bank deposits.

Now, on the question of public funds, Mr. Wolcott, there has been perhaps more damage done by banks taking on too large a percentage of public funds. In your average size bank your large account can give us more trouble than where you have a diversification of deposits, where your withdrawals are more or less uniform. If you had, for instance, a bank of $250,000, and you have one account of $750,000, you have really got to carry excessive reserves to take care of that large account, because you do not know when it will go out on you.

So there is a lot of danger in banks taking too large a percentage of their deposits in large accounts, which accounts will always cause you trouble unless you have your investment in conformity with the size of your accounts.

Mr. Wolcott. I brought that out merely because I wanted to know whether, in the future, we could work out some plan so that these fellows would not be isolated by the closing of a bank in one case, which is always the case in connection with a branch-bank system, but should not be the case with our present system, where it affects 40 or 50 others in that locality.

Mr. Crowley. That is a matter that we have already given quite a lot of thought to, and it should be studied for another year, I think.

Mr. Wolcott. When a corporation terminates its connection with the Federal Deposit Insurance Corporation, there is a provision in section 1 (5) on page 13 of your print that provides that the corporation may publish notice of such termination and the bank, meaning the assured institution, I assume, shall give notice of termination to its depositors in such manner and at such time as the board of directors may find necessary.

Of course, it is my thought in that particular that whenever a bank withdraws from the fund, they are not going to rush out and advertise the fact, and I wonder if we should not make this notice mandatory, or specifically provide in this act the manner of the notice and the time for giving notice by the bank which was withdrawing, rather than to leave it to the board of directors of these banks as to whether or not they will give any effective notice.

Mr. Birdzell. You understand that the "board of directors" there means our own Corporation, not the board of directors of the bank?

Mr. Wolcott. Possibly that clarifies that whole situation.

Mr. Crowley. Here is the reason why. On the matter of notifying depositors, we might have a bank, Mr. Wolcott, that we were having considerable trouble with, and that we were going to expel from the fund. We would notify the State supervisor, who would notify the bank of the particular difficulty. What we want to do is to stop the bank from doing anything that may affect an innocent depositor, because there are banks that are perfectly willing to stay in here during this recovery program and which, after confidence has been restored and we get on a normal condition again, will perhaps want to get out because they do not want to have any part in the whole banking system.

Mr. Wolcott. I think that perhaps my objection to that language is answered by section 10 of your definition, which says:

> The term "board of directors" means the board of directors of the Corporation.

One more question, please. In the Federal Reserve Act, there is a provision that national banks may loan on real estate up to 75 percent of the value. I wonder whether that does not affect some of the effectiveness of the Federal Deposit Insurance Corporation?

Mr. Crowley. In the Federal Reserve provision, Mr. Wolcott, there is a provision that those mortgages shall be eligible for rediscount, which, of course, puts a little different complexion on it.

Mr. Wolcott. You think that that clause is adequate protection so far as your fund is concerned? I know that that is out of your scope.

Mr. Crowley. It is out of my scope a little bit, and I think that the Comptroller should talk on his national banks. There is no question but what in the past, in your State systems, where they were permitted to take mortgages, and where you had your shrinkage of values, it affected their conditions materially.

Mr. Wolcott. I understand that back in 1923 they amended the National Banking Act to increase the amount that a national bank could hold on real estate from 25 percent to 50 percent. Now there is a school of thought which lays all of our industrial ills on the doorstep of that policy which allowed the banks to invest so heavily in real estate that they created a condition of insolvency on the real-estate market, and I wonder if we are not just contributing to the recurrence of a bank crash by increasing this still further from 50 percent to 75 percent, and, if so, of course we all are vitally interested in whether or not the Federal Deposit Insurance Corporation would be in a position to meet such prices brought on by a slump in the real-estate market.

Mr. Crowley. I think there is a lot to what you say, and it all depends, in my mind, as to what provisions you make in the Federal Reserve Act for it. If they cannot rediscount those, there is a great danger of a bank being frozen.

Mr. Brown of Michigan. Even if they did rediscount those mortgages, the primary loaning bank would still be responsible to the Federal Reserve bank.

Mr. Crowley. Oh, yes; it would be bills payable.

Mr. Brown of Michigan. I do not see that that would clear up the situation that he is discussing.

Mr. Crowley. Here is what it would do: It would just place a long-term loan in a position that they might borrow on it the same as on their eligible paper. It does not place the same stigma against a long-term loan if it is eligible for rediscount that it would have if it were not eligible.

Mr. Wolcott. Here is another point in respect to that same question. There is no restriction made upon the funds which might be used for investment in real estate at 75 percent of its value, and they might take long-term real-estate paper and invest commercial funds in it, and your commercial deposits are guaranteed under the fund.

Mr. Crowley. I think it does this: It means that they have to pay off each year, reducing the principal, and that is the limit to the amount of funds that they may employ in the mortgage field.

Mr. Wolcott. Yes; but we allow them to take 20-year commercial paper up to 75 percent of the value of the real estate.

Mr. Crowley. Yes; but it must be amortized.

Mr. Wolcott. Nevertheless, it is a long-term investment.

Mr. Crowley. There is no question that it puts it in the same position as a bond.

Mr. Brown of Michigan. I am a little bit disturbed about what might be a duplication, or even a triplication, of the duties performed by your corporation, the Comptroller's office, and the Federal Reserve Board.

Now, in your very clear statement which you gave to us on the first day, and of which we all have copies, you said on page 26—

In the future the Corporation should devote a large part of its efforts to the maintenance of sound conditions among the insured institutions.

Now, it seems to me that that clearly defines just what the duty of the Comptroller of the Currency now is. Am I right about that, or wrong?

Mr. CROWLEY. Do you mean in the case of a national bank?

Mr. BROWN of Michigan. Yes.

Mr. CROWLEY. The only authority that we have, Mr. Brown, over a national bank or a State member bank is that we have the power to put them out of the fund just the same as a State bank, after notifying the Comptroller and the Federal Reserve Board, just as we notify the State supervisor.

Mr. BROWN of Michigan. I think that your power is greater than that. You not only have the power to put them out of the fund, but upon your determination that they should be out of the fund, the statute is mandatory that both a member of the Federal Reserve System and a national bank shall then be suspended. Is not that true?

Mr. BIRDZELL. That would be correct.

Mr. BROWN of Michigan. If you once determined that a bank cannot remain a member of your fund, then the Federal Reserve Board must suspend that bank and the Comptroller must appoint you as receiver.

Mr. BIRDZELL. No; the Federal Reserve Board must see that the bank is no longer in the Federal Reserve System, and in the case of a national bank, of course it would result in liquidation.

Mr. CROWLEY. You understand, the Federal Reserve Board has no authority to appoint a receiver for a State member bank.

Mr. BROWN of Michigan. I understand that. It will appoint your Corporation, or, if you do not care to take it, some other suitable person as receiver.

In other words, in the power that you have asked, you will have absolute authority in your board of directors to suspend any bank in the United States if it is a member of your Corporation.

Mr. CROWLEY. I do not think that there is any duplication there. I think that we are the only ones that have that power.

Mr. BROWN of Michigan. Of course, the national bank department has that power with respect to national banks.

Mr. CROWLEY. There is no particular reason why we should not have the same control of putting a bank out of the fund, be it a Federal Reserve member bank or a State bank, if they are not conducting themselves in a manner that is going to give to this Corporation the usual safeguards.

Mr. BROWN of Michigan. Well, I think that is true, but I am saying that that gives you the same power that the Comptroller now has over national banks and that the Federal Reserve Board now has over Federal Reserve banks.

Mr. CROWLEY. No; the only power that the Federal Reserve Board has over a State bank is that if they do not conduct themselves properly, they may put them out of the Federal Reserve System, but there they stay.

Mr. BROWN of Michigan. That is right.

Mr. CROWLEY. Now, then, the power that we have over the State banks is just the same as the Federal Reserve Board has over the

State banks, but we carry ours further, and we ask for the power also over a national bank, that we may put them out of the fund.

Mr. BROWN of Michigan. But it does seem to me that we certainly have a duplication there of power. In the temporary plan or the permanent plan as it now exists, for instance, in the matter of examinations of banks, you have to accept the examinations of the Office of the Comptroller.

Mr. CROWLEY. That is right.

Mr. BROWN of Michigan. And the only examinations which you are empowered to make now under existing law are examinations of nonmember banks.

Mr. CROWLEY. That is correct.

Mr. BROWN of Michigan. Now, on page 18 of the bill, I think it is, you ask for the power to examine all banks——

Mr. CROWLEY. No.

Mr. BROWN of Michigan (continuing). With the consent of the Comptroller.

Mr. CROWLEY. May I explain that to you, Mr. Brown?

Mr. BROWN of Michigan. Yes.

Mr. CROWLEY. The reason for that is this. Supposing that the Comptroller or the Federal Reserve Board has a bank which is in difficulty; under our law, we have asked you for the authority to buy assets for the purpose of mergers. We may wish to go in with the Comptroller or the Reserve Board and make an examination to know the position of the bank, in order to try to determine upon a program that will prevent us from taking too great a loss. In other words, we will go into a bank with a million dollars in deposits and buy $250,000 of undesirable assets, and the Comptroller would merge that with $750,000 in another bank, and that would save us the liquidation of a million-dollar liability where we would be getting off with $250,000.

Do you get my point?

Mr. BROWN of Michigan. I get your point, but——

Mr. CROWLEY. In order to do that, we have to have the authority to go into a national bank, and we are only asking for that where the Comptroller is agreeable that we should go in with him on that proposition.

Mr. BROWN of Michigan. But it seems to me that even at the present time, under existing law, where we have a group of national-bank examiners under jurisdiction of the Federal Reserve Board, and a group of national-bank examiners under the jurisdiction of the Comptroller, each having different duties, we must bear in mind that we are here establishing a third group of national-bank examiners under your control, with power, I grant you, only upon the consent of the Comptroller, to examine national and member banks of the Federal Reserve System.

Now, my point is this, that it seems to me that the three departments ought to get together to see if we cannot consolidate you all into what seems to me to be a logical organization governing all the national banks of the United States. If we cannot do that, we at least ought to consolidate these three boards or bureaus into one examining division, that would have authority to examine for all three of these governmental bureaus, and it just strikes me that the legislation is ill-conceived in that respect. We have that provision now with respect to the Federal Reserve Board and the Comptroller's office.

Perhaps I ought to say that I think that your Corporation is an illogical Government organization or bureau to undertake that work, but it does seem to me that you are placing an unnecessary burden upon national banks and member banks and forcing them to pay the expenses of examinations which certainly will be more numerous than they have been in the past. It seems to me that you are by this act diversifying the power and authority that the Comptroller's office has over bank examiners.

Now, if this office is not the right office to handle the matter of the examination of national banks, let us turn it over to you or to the Federal Reserve Board, but let us not have three different groups of national-bank examiners.

Mr. CROWLEY. Mr. Brown——

Mr. BROWN of Michigan. I believe that it is illogical.

Mr. CROWLEY. I do not think that you would have any three groups of national-bank examiners, to this extent, that we have examined only State banks. Now, there is no way under the present law that anyone else can examine a State bank except the Federal Deposit Insurance Corporation and the State supervisor.

Mr. BROWN of Michigan. That is true; but let me interrupt you to say that if the law is enacted as you and your Corporation want it to be enacted, that is, with the elimination of nonmember State banks from the Federal Reserve Corporation, then the argument that you are just making would not apply?

Mr. CROWLEY. That is correct.

Let me say to you that there is no duplication of Federal examination at this time. I mean by that that the Comptroller examines the national banks, the Federal Reserve Board examines only the Federal Reserve member banks, and we examine only the State banks.

Let me add, on this matter of examination, that the Federal Deposit Insurance Corporation cannot be put off here all by itself and not be permitted to use the usual precautions that will be necessary in order to keep this fund sound.

Mr. BROWN of Michigan. You have all of that authority under the existing law.

Mr. CROWLEY. We have not the authority to do this. All of the help that we have had so far has been in going into the banks and working with the State commissioner and, by moral persuasion, getting the banks to build their capital, make their application to the Reconstruction Finance Corporation, and things like that.

Mr. BROWN of Michigan. When you made that statement I was inclined to disagree with you. You made it in your opening statement. On page 13 of the original act it provides " that such certification to the Corporation by the State banking commissioner that the bank is in a solvent condition shall, after examination by and with the Corporation, be entitled " and so forth. I grant you that great pressure was brought upon you to be liberal about that, but you had no legal right under the law to admit any bank that was not solvent, and, of course, that means solvent not only as to its deposit liability, but solvent as to its capital.

Mr. Birdzell. The definition of solvency is given in the act, and it says " whose assets are sufficient to meet its liability to depositors and other creditors."

If you will look further, that is the definition that we are revising in this new draft.

Mr. Brown of Michigan. You feel that until this serious question of what is going to become of several thousand nonmember State banks is solved, that we cannot very well set up a national bank examining department?

Mr. Crowley. I think this, Mr. Brown, that you have seen the opposition to your State banks in joining the Federal Reserve System——

Mr. Brown of Michigan. Yes.

Mr. Crowley (continuing). And over a period of 20 years 960 have joined. Now, if you put the 7,800 State banks virtually under a national examining supervision, I think that you would have the same objection that was expressed to their joining the Federal Reserve System.

I think that this whole matter must be taken step by step and corrected each year until you finally get the system that you wish.

Mr. Brown of Michigan. I may want to pursue that a little bit further, but, before we close I would just like to call your attention to one item on page 27 of the comparative print.

You will remember, Judge Birdzell, when the section of the law which was called the Steagall amendment was attached to the Federal Deposit Insurance law last spring, and that provided that loans to closed banks were to be made through the Federal Deposit Insurance Corporation.

Mr. Birdzell. Yes, sir; that is the way the House passed it.

Mr. Brown of Michigan. And when it got to the Senate and came back, our conferees agreed that it would go to the R. F. C.

Mr. Birdzell. Yes.

Mr. Brown of Michigan. You will remember that either your department or Judge Reed's department in the R. F. C. held that under the wording of the statute, loans to closed banks or the assets of closed banks could only be made on sale of all the assets. I do not remember whether that was your ruling or the ruling of the R. F. C.

Mr. Birdzell. That ruling was not our ruling.

Mr. Brown of Michigan. There was such a ruling, and I am sure that the gentlemen on the committee remember that ruling.

Why not clarify this language here, which is identical, so that you can make loans upon the assets in whole or in part? Do you not think that that amendment would be desirable?

Mr. Birdzell. There could not be any objection to that amendment at all.

Mr. Brown of Michigan. Because that ruling was made, so that you could loan on a part of the assets.

Mr. Birdzell. There would not be any objection to that kind of an amendment at all.

May I say, while we are on that subject, that that ruling was not made during the pendency of that bill in Congress last year. It was made subsequently, and it was not our ruling.

Mr. BROWN of Michigan. I think that you are a little bit unfair to the depositors when you require them to file a claim within 1 year. It is readily conceivable that a great many people may be away on trips, or something of that kind.

Mr. BIRDZELL. We have no objection at all to a longer period. The reason 1 year was suggested is because that is a sort of a prevailing contract limitation in insurance contracts, generally.

Mr. BROWN of Michigan. I understand it is.

Mr. BIRDZELL. And it was generally thought to be reasonable, but if the committee should think that a longer period should be provided for, 18 months or 2 years, all right.

Mr. BROWN of Michigan. I thought that perhaps we could clear it up by some language to this effect, that when the claim is clearly meritorious and not contested by the bank itself, the amount should be paid, but if it is a case where there is any contest about it, I would not object to a limitation.

Mr. CROWLEY. You understand that in a great many banks they accumulate a lot of very small balances, maybe of 38 cents or $1, or $2, or $5, and sometime or other we ought to be able to eliminate ourselves from that liability.

Mr. BROWN of Michigan. On page 27, in the matter of loans to banks concerning which you spoke a short time ago, Mr. Crowley, where you are going to bring about a consolidation in order to avert disaster, why do you limit that to July 1, 1936?

Mr. CROWLEY. For this reason——

Mr. BROWN of Michigan. Why should it not be permanent?

Mr. CROWLEY. What we would like to do is to operate it for a year, and then we will come back and give you the benefit of our experience and then have you extend it if you believe that it has been entirely successful. There is grave danger in paying the losses of these banks too easily. It might cause the banks to become careless; that is the reason we limit it so we can have a little experience to guide us in the future.

Mr. BROWN of Michigan. A little trial legislation?

Mr. CROWLEY. That is right.

Mr. BROWN of Michigan. I would very much like to see you give consideration to that matter of seeing that we do not have too many different groups of Federal examiners investigating these banks. I think that that is a serious question.

The CHAIRMAN. I want to ask if anyone else desires to interrogate Mr. Birdzell or Mr. Crowley?

Mr. DIRKSEN. Yes; I do.

The CHAIRMAN. Then we will meet tomorrow morning and resume this questioning at 10:30.

(Thereupon, at 12:45 p. m., an adjournment was taken until Thursday morning, Feb. 28, 1935, at 10:30.)

BANKING ACT OF 1935

THURSDAY, FEBRUARY 28, 1935

House of Representatives,
Committee on Banking and Currency,
Washington, D. C.

Hearings on title I of the bill above referred to were resumed at 10:30 a. m., Hon. Henry B. Steagall (chairman) presiding.

The Chairman. The committee will be in order.

I do not have before me the list of those who have already questioned the witnesses, but I believe that Mr. Dirksen indicated at the close of yesterday's session that he wanted to ask some questions.

STATEMENTS OF LEO T. CROWLEY, CHAIRMAN, AND L. E. BIRDZELL, GENERAL COUNSEL, FEDERAL DEPOSIT INSURANCE CORPORATION—Resumed

Mr. Dirksen. Mr. Crowley and Mr. Birdzell, in the comparative print, on page 33, I want to direct your attention for a little bit to the new language there, which states that no State nonmember bank, other than a mutual savings bank, or a Morris Plan bank, or a bank located in the Territories of Hawaii or Alaska, shall become or continue an insured bank after July 1, 1937.

Now, a State nonmember bank, of course, is not a member of the Federal Reserve System.

Mr. Birdzell. That is correct.

Mr. Dirksen. It means that these banks are going to be compelled to become members of the Federal Reserve System, or else the so-called " State nonmember banks " can have no insurance after July 1, 1937.

Mr. Birdzell. That is correct.

Mr. Dirksen. That is the proper inference from that paragraph?

Mr. Birdzell. That is correct.

Mr. Dirksen. First of all, the question arises in my mind as to why, if a State bank is solvent, and if it is sound, and it is so disclosed to be upon your own examination, such a bank should not be insured without having to become a member of the Federal Reserve System.

Mr. Birdzell. Mr. Congressman, that provision is in here in the form that it is because section 12 (b) as passed originally, in June of 1933, contained a similar requirement, except that the date was July 1, 1936; that is, nonmember banks were permitted to obtain the benefits of the insurance until July 1, 1936, without joining the Federal Reserve System. Then, when the temporary fund was extended for a year, that date was also set ahead a year, so as to give the nonmember banks the benefits of the insurance until July 1, 1937, instead of 1936.

Whatever the policy may be with respect to that question Congress apparently considered at the time the Banking Act of 1933 was under consideration here, and the Corporation has not suggested any change in that respect, because it does not particularly affect its operations. That is a matter of policy primarily for the consideration of Congress. There is an exception——

The CHAIRMAN. Let me interrupt you for just a moment.

Mr. BIRDZELL. The exception relates to the mutual savings banks and the Morris Plan banks. Our experience with regard to them shows that there is no likelihood of those banks finding a place in the Federal Reserve System, and we have suggested the amendment which would enable those banks to continue insurance without joining the System.

Anything that Congress may do with respect to other banks is something that we have no particular feeling about one way or the other.

The CHAIRMAN. Let me say this in that connection, that the provision in the Banking Act of 1933 requiring State nonmember banks, in order to avail themselves of the benefits of participation in the deposit insurance, to become members of the Federal Reserve System after July 1, 1936, was stubbornly contested. The House bill had no such provision, but provided for the admission of member banks and State nonmember banks without discrimination, but the Senate bill limited the insurance to member banks. The older members of the committee are familiar with the differences of opinion that obtained among the members of the conference committee, and I presume that you are, on that bill. This is the simple fact of the matter, that we found ourselves with the adjournment of Congress approaching, and the conferees deadlocked over two propositions, one of which was the provision providing that national banks should be permitted to have branches in all States where State laws permitted such branches. That provision, and the provision requiring membership in the Federal Reserve System after July 1, 1936, in order to participate in deposit insurance, were the two controversial points, and we fought those out down to almost the hour of adjournment.

Rather than see the legislation embodied in the so-called "Glass bill", which had been developed as a result of long hearings and labor on the part of Senator Glass and his committee in the Senate, defeated, and rather than to see the defeat of the insurance plan which in a former session of Congress passed the House, and which was embodied in the bill then under consideration, and which the conferees for the House were exceedingly desirous of adopting, we finally agreed to an amendment which would permit branch banking and we yielded on the provision requiring membership in the Federal Reserve System as a condition precedent to participation in the benefits of deposit insurance by nonmember banks.

Last year when the act was passed extending the temporary insurance, another compromise was reached respecting the privilege of nonmember banks of participating in deposit insurance by postponing until July 1, 1937, the date upon which they should be required to become members of the Federal Reserve System in order to participate in the insurance benefits of the Corporation.

Now, of course, all of those questions will arise again in this committee and in the House, and probably in the conference when this bill is to be passed upon later.

Mr. DIRKSEN. Mr. Chairman and Mr. Birdzell, let me point out what is bound to happen under this provision, which you have to read in connection with section 202 of this bill, in title II. Your paramount interest for the moment is in title I, but I suppose that every member of this committee has had the same experience that I have had in the last 2 years, where I helped or sat in on the reorganization of 12 or 15 small banks out in the central part of Illinois. We had to go to the depositors and take waivers of anywhere from 15 to 50 percent, and when these banks were finally reorganized, they had to issue in lieu of the amount of money that was waived by the depositors, so-called "deferred certificates", which are payable out of earnings, and there is not any other way to pay them.

Now, the Federal Reserve bank in Chicago maintains that those deferred certificates are a contingent liability, and they will not accept them, and they will not accept any bank which has those deferred or contingent liabilities outstanding.

You take a bank in a small town, say of 1,000 people, where they had to waive 50 percent of the deposits and in lieu thereof issue these certificates, which became a charge upon the earnings of the bank if and when earned; certainly a great many of these banks cannot even earn enough money between now and the 1st of July 1937 to get those certificates out of the bank. They are there as a definite charge upon earnings.

If then the Federal Reserve System does not accept those banks because these contingent liabilities exist, and if you do not give insurance to those banks because they are not members of the Federal Reserve System, then there is only one thing for them to do, and that is either to go out of business or otherwise try to get along without the benefits of insurance.

I might elaborate on that a little bit. You may remember that 41 percent of all of the banks in this country are in towns of under 1,000 people, and in section 202 of this bill you will notice——

Mr. BIRDZELL. What page is that?

Mr. DIRKSEN. That is on page 41, that particular section—you will notice that that section says that the Federal Reserve Board, in order to facilitate the admission of these banks, has authority to waive in whole or in part the requirements of this section relating only to the capital requirements of a bank.

Now, we have 2,900 banks in this country that have a capital of $25,000, and in those cases the Federal Reserve Board, under this section, has a right to waive those requirements if it desires, but it has no right to waive any requirement with respect to a contingent liability, and you are going to put those banks out of business under that section. Either they will have to become members of the Federal Reserve System, or not get insurance, and it constitutes a club which is going to have two effects, to put some banks in the Federal Reserve System that do not want to go in, and, secondly, there are some banks that will not be able to go in, and, if insurance is material to the stability, the soundness, and the continued operations of banks, they will have to go out of business.

Mr. BIRDZELL. I think that there is merit in the Congressman's suggestion, particularly with reference to the effect of the waivers that he spoke of. We have come across a number of instances where the depositors had waived a certain amount of their deposits and released the bank from any obligations so far as that liability was concerned, and that enabled the bank to reorganize.

The CHAIRMAN. Let me say a word right here in connection with what Mr. Dirksen just said, in order to bring the history of this transaction down to date.

It is not unfair to say that the conferees on the part of the House, when this bill was under consideration, would never have yielded in connection with this provision and permitted this provision to be enacted requiring State nonmember banks after the 1st of July 1936, to become members of the Federal Reserve System if they were to participate in the benefits of deposit insurance, if we had not felt that the Congress could be trusted before that time to enact proper legislation to extend the benefits of the Deposit Insurance Corporation to the nonmember banks.

Mr. REILLY. There will be two sessions of Congress after this one before that will become effective.

Mr. DIRKSEN. Before what?

Mr. REILLY. Before the 1st of July 1937 will be here, and I think that this discussion at this time is beside the issue, because Congress will later be in a better position to determine what should be done with State banks that do not come into the Federal Reserve System. We might pass a law today, and it might be changed in 2 years.

Mr. DIRKSEN. But, on the other hand, we are writing a permanent bill here now.

Mr. REILLY. It is permanent only until the next Congress sees fit to change it.

Mr. DIRKSEN. But it easier to try to get it right in the first place than to have to come along later and change it.

Mr. WILLIAMS. That is especially true when it should never have been in there in the first place.

Mr. DIRKSEN. Precisely.

Mr. BIRDZELL. If I may complete the statement that I started to make a moment ago, I think that I can shed a little light on this matter from the standpoint of its actual operation.

As the Congressman said in the case of those reorganized banks where there are deposit waivers and the depositors have some kind of a deferment certificate, but no claim against the bank, only against its earnings, we have reviewed in the legal department of the Deposit Insurance Corporation many hundreds of reorganizations where that element entered, and you will appreciate that such banks were not eligible for membership in the Deposit Insurance Corporation unless they were solvent. Whether deferment certificates of this type constitute liabilities of the bank, has much to do with whether that bank is solvent and, consequently, eligible. Wherever we became satisfied that the bank would not be liable for the amount of those deferment certificates, we held that the bank was solvent, and insured it.

Now, what attitude the Federal Reserve Board may take with respect to that same question I cannot tell you. I do know that there have been instances where banks have been reorganized on a deposit-waiver basis, where the Federal Reserve Board has questioned whether the banks had the unimpaired capital required under section 9 of the Federal Reserve Act; so that that is one of the things that is going to confront Congress in dealing with this question.

The Reconstruction Finance Corporation has taken very much the same view of that matter that we have taken in the Federal Deposit Insurance Corporation.

So the Congressman does raise a question that should be considered whenever this matter of Federal Reserve membership requirement is under consideration, and particularly where the capital requirements of section 9 are under consideration.

Mr. DIRKSEN. Then, Mr. Birdzell, as a general thing, is there any reason why a sound and solvent bank should not have insurance and continue to have it?

Mr. BIRDZELL. I do not want to suggest any reason why it is not entitled to insurance.

Mr. DIRKSEN. We have about 3,000 banks in this country that have been operated continuously for 50 years, a great many of them being State banks, and when a bank has a record like that, is there any reason why you should either force them into a system or not give them insurance?

Mr. FORD. If we are going to have a unified banking system, why not have one?

Mr. DIRKSEN. Why compel State banks to surrender all of the rights that they have, and crowd them into a system when probably they will not derive any benefit from it?

There are two or three banks in Missouri that have not missed a dividend for 20 years, and one of them a few years ago declared a dividend of 50 percent, and they never had occasion to use the Federal Reserve System. They do the banking business of their community, and they have never rediscounted paper, and their services have been adequate in their community.

Why force banks like that into the Federal Reserve System, when they do not want to go in, and it carries with it the additional burden of further examinations?

Mr. FORD. There are a good many things that a great many institutions do not want to do, and they have been allowed to run along in their own way, and as a result others have been the victims of their action.

Mr. DIRKSEN. That is beside the point, because those banks that you refer to cannot qualify for the benefits of the F. D. I. C. But now you bring in this alternative proposal, of either shoving them into the Federal Reserve System, or else they cannot get insurance.

Mr. FORD. Of course, my view at the present time is——

Mr. DIRKSEN. And no case has been made out to show why they cannot get it, if they can qualify.

Mr. FORD. I would like to have this put into the record, on the statement of somebody else, that there are supposed to be 8,500 State banks outside of the Federal Reserve System. Is that about right?

Mr. DIRKSEN. I think so.

Mr. FORD. I would like to have a study made to see what percentage of those banks and to what extent they were strengthened by the R. F. C. in proportion to the banks that were in the Federal Reserve System.

Do you get my point?

Mr. FOX. That is in the testimony.

Mr. BIRDZELL. That study has been made.

The CHAIRMAN. That is something that I have been wanting.

Mr. FORD. I want that study made in a way so that we can make an independent study of that situation.

The CHAIRMAN. Let us have it as it is; let us not let those figures be played up in a way so that they do not depict the real situation.

Mr. FOX. They are on page 30 of Mr. Crowley's first statement.

Mr. DIRKSEN. I have one other question, and I think that I raised this question a year or two ago, with respect to the provision starting at the bottom on page 12 of the comparative print, subsection (i).

I understand from the full text of that section that banks whose insurance has been terminated will be compelled to pay assessments for an additional 2-year period, and that that coverage for an additional 2 years will be imposed upon them whether they will or not.

I think that that is quite long to require that period of 2 years, because in that same section the Corporation is given the power to require any kind of notice to be given, can give the notice itself or compel the bank to give the notice. You can send the notices by mail, or compel circulation of the notices in a newspaper for a month or two, and I should say that 6 months would be an ample time and that thereafter no further assessment should be required.

Mr. BIRDZELL. Two years may be too long, but I believe that 6 months would be too short.

Mr. DIRKSEN. Possibly so.

Mr. BIRDZELL. We do not want to be open to the charge of not dealing in good faith with depositors of banks, and we would rather err on the side of having that period too long than on the side of having it too short. It is a matter of judgment.

Mr. DIRKSEN. Of course, in the metropolitan centers a little longer time might be required, but in a community of 1,000 people, and almost half of our banks are in towns of that sort, for all practical purposes a week would be ample notice.

Mr. CROWLEY. I do not object to cutting it down from 2 years to some extent, but it should be a long enough time so that there can be no doubt in our minds but that the depositor has had plenty of time in which to make up his mind as to whether or not he wants to keep his money in that bank. Furthermore, if the bank is an institution that has been doing things which caused us to put it out of the fund, there is a question as to whether we should not give them ample protection for a long period of time, to enable them to correct their practices and again quality for insurance.

I do not think that the judge or any of us has any objection to any compromise in that particular, but the time should be long enough. I do not see that it is any great hardship to the bank to have a period of 2 years, and it is a great benefit to the depositor.

It is also of great benefit to the Corporation. These banks that are badly managed, these banks that should be put out of the fund, should have some string on them until you know that the depositors have had that opportunity to which I have referred.

The CHAIRMAN. Let me say this, please, in this connection, and I do not want to prolong this discussion unnecessarily, that the Deposit Insurance Corporation was never established, nor was the plan of insurance deposits designed, nor in my judgment should it be used, for the purpose of settling any quarrel between the nonmember bands and the member banks. Some believe that we should have a unified banking system, and if that view has enough support to express itself in legislation, let those who believe in a unified banking system in this country devote their efforts to that purpose, but let it be fought out on its own merits; and if we are not to go the whole way and adopt a unified system, let us leave the matter of membership in the Federal Reserve System for State nonmember banks to be determined by the nonmember banks themselves, as provided in the Federal Reserve Act. If a State bank wants to join the Federal Reserve System and finds it desirable, if the inducements are such that the State bank wants to come in, let it come, but with all of its rights under its charter issued by the State in which it does business.

This question of insurance on bank deposits ought not to become involved in any way with the permanent policy respecting a unified or dual banking system. I have my views about that, but I do not think that they have any proper place in legislation affecting bank deposits.

What we are trying to do here is to protect the public against bank failures and against the horrors that have attended bank failures heretofore, and let that legislation be dealt with on its own merits, and leave this question of membership and nonmembership in the Federal Reserve System to be fought out in a normal way, on its own merits.

I believe in membership in the Federal Reserve System, but undoubtedly there are banks that do not want to join the Federal Reserve System, and certainly, as I see it, it is not necessary, and surely not indispensable, that every bank in the country should belong to it or be members on a definite date.

Mr. REILLY. Do you not think that the Congress of the United States will be in a better position 2 years from this time to decide the question whether we want a unified banking system, after we have had 2 years more experience, than it is today? That matter can well be deferred until 2 years from this time, when we can make a better final decision on it.

Mr. DIRKSEN. I think you are right, but this section would have to come out of the bill, because that is an instrument of compulsion to force them in.

Mr. WILLIAMS. And you ought not to wait until the last day to do that. I think that you ought to take it up right now, and give them at least 2 years' notice that we mean to make this a permanent policy, and not compel these State nonmember banks to wait until 2 years from now to see what they are going to be up against.

Mr. CLARK. I just want briefly to supplement what you said, if I may.

As I said the other day, regardless of politics I think that the Federal Deposit Insurance Corporation has the confidence of the people of this country. I know that it saved our West.

There has been some question as to whether or not the Federal Reserve System, at least as it existed in 1929, did not break down. There is a grave question in the minds of a lot of people in this country as to the soundness at all of the Federal Reserve System. Many of the small banks disapprove of it.

I do not believe that we should, under any circumstances, use a well-respected institution like this institution is, which has the confidence of the country, to club nonmember banks into a system which may not have the confidence of the country.

I just wanted to make that one observation.

Mr. FARLEY. In the figures that you have submitted, is there anything that might be a guide as to how many of these banks could not qualify, if this bill went through?

Mr. CROWLEY. I think that 72 percent of the nonmember State banks which are insured could qualify on their capital position now. In other words, in the rebuilding program that has been taking place, we have tried to base it so that they would have sufficient capital to be eligible under the capital requirement.

Mr. FARLEY. I do not know that this question is germane to the bill that we are considering here, but does your Corporation feel that there are still too many banks?

Mr. CROWLEY. No; I do not think that that is generally true now, Mr. Congressman. I think that the banks that have survived this depression certainly showed themselves pretty well able to take care of their situation. There may be certain isolated places where we are overbanked, but I think that as a general proposition the country can support the number of banks that we have now, if properly located.

The big trouble is that you may go much further than the banks that we have now, in extending new licenses.

Mr. FARLEY. Did this elimination of daily balances do the banking business any good?

Mr. CROWLEY. Do you mean the elimination of the interest on daily balances?

Mr. FARLEY. Yes; the elimination of the interest on daily balances.

Mr. CROWLEY. Yes; Mr. Congressman, it did.

The banks were faced with the problem of reducing expenses in proportion not only to their volume of business but also to the reduced rate of earnings on the business that they had. As I explained the other day, the elimination of interest on daily balances subject to withdrawal on demand was an important factor in reducing expenses.

Mr. FARLEY. Is there any demand that you know of on the part of the large, central banks that that provision be restored, so that they may pay interest on daily balances?

Mr. CROWLEY. I know of no demand from any source, either large or small.

Mr. FARLEY. When we put that into the law, there was a great deal of talk then along this line, that if we could hold this money in the smaller banks and eliminate that 2 percent on the daily balances, or any other percent, they would use the money at home instead of using it in the larger centers.

Has that worked out that way?

Mr. CROWLEY. Of course, that is a very hard question to answer, because there has been a very limited demand for new credit on account of your business depression. I do not know how that would work in normal times. I think that under the theory of the insurance of deposits, as I said yesterday, the banks might employ a larger percentage of their deposits in local loans, because I do not think they have to have that extreme liquidity through fear of runs that they might have had before.

Mr. FARLEY. I think that the intent of this bill—and I do not refer to you gentlemen personally—is further to eliminate banks, to get rid of a lot of banks that we now have. I am just wondering how many would have to go if we did it. Today we would lose 28 percent of them.

Mr. CROWLEY. In what way? Do you mean that we would eliminate 28 percent on account of joining the Federal Reserve System?

Mr. FARLEY. I mean that they could not get through.

Mr. CROWLEY. I do not like to get into the controversy on Federal Reserve membership, because that is another part of this bill; but I might say that I have always had enough confidence in legislative bodies, and I have enough confidence in you men to feel that when the time comes, if there are 2,000 or 3,000 banks in this country that cannot join the Federal Reserve System, certainly you are not going to put those banks out of our insurance system. I do not believe that you are going to put into liquidation 2,000 or 3,000 banks. From our own standpoint, all that we have to do is to be reasonable. If you were going to put 2,000 or 3,000 banks into our laps for liquidation, we would be the first ones to tell you how impracticable that was, because of the cost to ourselves. So I have a lot of confiedence that somewhere along the line that will be adjusted, so that the great majority of the State banks are going to be cared for.

Mr. WILLIAMS. There is one thing that I do not yet understand, and I want to get the record straight on it. You say that there are only 72 percent of these nonmember banks that can qualify?

Mr. CROWLEY. I mean by that, Mr. Congressman, that under the present Federal Reserve Law, they must have a minimum capital, and 72 percent of these banks already have sufficient capital to meet that requirement.

Now, under part 2 of this bill, the Federal Reserve Board is asking for authority so that they may waive that minimum requirement of capital.

Mr. WILLIAMS. Let me ask you this, then: Have you not already qualified more than 72 percent of them for admission into the temporary fund?

Mr. CROWLEY. Do you mean by the temporary fund, the Federal Deposit Insurance Corporation?

Mr. WILLIAMS. Yes.

Mr. CROWLEY. Of course, there are 7,800 State nonmember banks. You and I are talking about two different things. I say that there are 72 percent, Mr. Congressman, that are members of our fund now whose capital position is sufficient to joint the Federal Reserve System with the old provision governing capital requirements for Federal Reserve members.

Mr. WILLIAMS. I am not talking about the Federal Reserve. I do not know whether Mr. Farley was or not.

Mr. FARLEY. Your answer was just what I wanted.

Mr. WILLIAMS. I am talking about the number of nonmember banks that can qualify under the law as it is now and come into the temporary insurance fund, and automatically pass into the insured.

Mr. CROWLEY. There are only 1,100 banks, Mr. Williams, State banks, that are outside of our fund today, and our law calls for the 7,800 banks now members of our fund to automatically become members of the permanent fund.

Mr. WILLIAMS. They automatically pass in on the effective date of this law?

Mr. CROWLEY. That is right.

Mr. WILLIAMS. And that is more that 72 percent.

Mr. CROWLEY. Yes; but we are talking about two different things. That is 90 percent.

Mr. WILLIAMS. Now, you have already qualified that number of banks for the temporary fund, and qualified them for the permanent fund; that is, until July 1, 1937.

Mr. CROWLEY. That is correct.

Mr. WILLIAMS. Is there any reason why they should not pass right on into the permanent system after July 1, 1937?

Mr. CROWLEY. You mean, in our permanent system?

Mr. WILLIAMS. Yes.

Mr. CROWLEY. They would go into our permanent system just as soon as you pass this bill.

Mr. WILLIAMS. But they go out on July 1, 1937.

Mr. CROWLEY. My answer to that is this, Mr. Williams: As I said, I have enough confidence in Congress to feel that they are not going to force out of our insurance system 2,000 or 3,000 banks.

Mr. WILLIAMS. You see what my point is, that you have already qualified them, and they automatically pass into the system on the effective date of this law and will be members of the system at least until July 1, 1937, and my inquiry is why they cannot remain in the system after that date.

Mr. REILLY. I might suggest that that will depend entirely upon the judgment of Congress as to whether or not we shall have a unified banking system.

Mr. WILLIAMS. I am asking if there is any reason on the part of this Corporation why that cannot be done. If there is, we would like to have it, because that question will confront us from now on.

Mr. CROWLEY. I think this, that in dealing with that provision, you have to take into consideration your capital requirements and the advantages to your smaller banks of membership in the Federal Reserve System. That, to my mind, is entirely a matter for Congress to determine. As I said, unless you change the Federal Reserve law and liberalize it so that these banks can qualify, there will be at least 2,000 of them that cannot come in unless we build their capital structure up for them.

To put 2,000 banks out of the insurance fund would be a very serious matter.

Mr. REILLY. You said that about 1,500 nonmember banks are out of the insurance system.

Mr. CROWLEY. About 1,100.

Mr. REILLY. Why are they unable to come in and qualify?

Mr. CROWLEY. A very small percentage of these banks felt that they did not need it.

Mr. REILLY. What percentage of those banks that could come in did not come in?

Mr. CROWLEY. We do not know, exactly.

The CHAIRMAN. Of course, there is no way on this earth by which you can know how many banks failed to apply for participation in the deposit fund because they felt that they do not need it, or for other reasons. You do not know anything about those who did not apply.

Mr. CROWLEY. We made the best analysis that we could, but, of course, we cannot say that that is the reason.

The CHAIRMAN. You cannot analyze a bank that you never had anything to do with.

Mr. CROWLEY. Taking the 1,100 banks outside of the fund, their deposit liability only amounts to a little over $500,000,000, so, as a whole, they are very small banks. But there are two or three real large ones.

Mr. WILLIAMS. But that does not mean that they do not serve a useful purpose in their communities, and that they are not sound?

Mr. CROWLEY. That is correct.

I think this: That really the ambition of the Federal Deposit Insurance Corporation should be to get every bank in the Federal Deposit Insurance system, for the protection of depositors, even though they had to make some adjustments in order to get them in.

Mr. WILLIAMS. What percentage of the banks that applied for insurance have not been admitted?

Mr. CROWLEY. We admitted to the temporary fund all except 200 banks that made application, but what we did was this; we took them in, and then we rebuilt them afterward.

Mr. WILLIAMS. Then there have been about 200 out of all of these applications that have been definitely and finally rejected?

Mr. CROWLEY. Yes.

The CHAIRMAN. I want to ask something about that, Mr. Williams.

How many State banks that are nonmember banks belong to the Deposit Insurance Corporation and participate in the insurance?

Mr. CROWLEY. Seven thousand eight hundred, Mr. Chairman.

The CHAIRMAN. How many member banks, both national and State member banks, participate in the deposit insurance fund?

Mr. CROWLEY. Six thousand three hundred; that is, State and national member banks.

The CHAIRMAN. Now, you have 7,800 nonmember banks that participate in the Deposit Corporation?

Mr. CROWLEY. That is right.

The CHAIRMAN. Now, the Reconstruction Finance Corporation has supplied to those 7,800 banks $184,000,000 to replenish their capital, has it not?

Mr. CROWLEY. $256,000,000 up to February 1, Mr. Chairman.

The CHAIRMAN. And you supplied to national banks $465,000,000 through the R. F. C.?

Mr. CROWLEY. That is right.

The CHAIRMAN. And to your nonmember State banks, numbering 7,800, you have supplied $256,000,000?

Mr. CROWLEY. That is correct.

The CHAIRMAN. And, to your State member banks, numbering about 900, you supplied $238,000,000?

Mr. CROWLEY. That is correct—960 such banks, instead of 900.

The CHAIRMAN. So that to your 7,800 nonmember banks that are insured, the R. F. C. has extended $256,000,000, and to the member banks $703,000,000. That does not seem to indicate that your State banks involve any greater hazards or present any worse difficulties than your national banks or member banks.

Mr. CROWLEY. Just let me answer that off of the record.

* * * * * * *

The CHAIRMAN. What is the amount of the deposits of your national banks?

Mr. FOX. About 20 billions.

The CHAIRMAN. Is that for the national banks or for the members?

Mr. FOX. Just the nationals.

The CHAIRMAN. What is the amount of the deposits in your member banks?

Mr. CROWLEY. You mean your State member banks.

Mr. FOX. Twelve billions.

The CHAIRMAN. So that you have 32 billions of dollars of deposits in the banks that are members of the Federal Reserve System.

Mr. CROWLEY. That is correct.

The CHAIRMAN. What is the amount of the deposits in your nonmember State banks?

Mr. FOX. About $4,800,000,000.

The CHAIRMAN. Those figures are not what I thought they would be.

Mr. CROWLEY. Where you become confused a little bit is that we are talking only about State banks that are commercial banks. If you add the savings banks, that increases your total tremendously.

Mr. WILLIAMS. Let me ask one other question, and then I think I will be through.

In all of these figures respecting insured banks that we have before us, I think your latest report is as of last June. If we could get those figures right up-to-date, I would appreciate it, and I think that we ought to get them into the record.

What is the number of the national banks that are insured now, and I would like to have your figures the same as they are in your report, by classes.

Mr. FISH. May I ask a question?

The CHAIRMAN. I suggest that you supplement your statement by the figures that Mr. Williams asked for, and if you do not have them you can get them from the Comptroller's Office.

Mr. FOX. This is for January 31, 1935.

Mr. WILLIAMS. January 31 is all right.

Mr. FOX. Five thousand four hundred and sixty national banks.

Mr. WILLIAMS. Now, your State banks that are members of the Federal Reserve System?

Mr. Fox. Nine hundred and seventy-five.

Mr. Williams. And your State banks that are not members of the Federal Reserve System?

Mr. Fox. Seven thousand seven hundred and thirty-five.

Mr. Williams. And your Morris Plan banks?

Mr. Fox. That is included in that.

Mr. Birdzell. They are in the State nonmember bank figures.

Mr. Williams. The total, if you have it? Of course, that is just a matter of figuring it up.

Mr. Fox. Fourteen thousand one hundred and seventy.

Mr. Williams. Now, have you at this time the exact number of State member banks, commercial banks, that are not in the system at all?

Mr. Fox. One thousand and sixty-six.

Mr. Fish. This may already be in the record, but I have not attended the hearings regularly. If it is not in the record, I think it should be.

I would like to know the total amount of deposits that have been insured, and the percentage of the deposits that have been insured.

Mr. Crowley. In the entire banking system, or of the members of our fund?

Mr. Fish. I should think both. Can you tell that percentage?

Mr. Crowley. 43.49. In other words, of the 38½ billion dollars in deposits in the entire system, they are insured 43.49 percent.

Mr. Fish. Therefore, when you provide for an assessment of one-twelfth of 1 percent, it is one-twelfth of 1 percent of the total deposits, and not of the insured deposits?

Mr. Crowley. That is correct.

Mr. Fish. So it really amounts to about one-sixth of 1 percent of the deposits that are insured?

Mr. Crowley. That is correct.

Mr. Fish. I really wanted to clear that up in my own mind. I figured that on the basis of one-twelfth of 1 percent on the insured deposits, the assessment might be too low to take care of the situation except during normal times, but as long as it covers all of the deposits, it really amounts to one-sixth of 1 percent of the total deposits.

Mr. Crowley. Of the insured deposits.

Mr. Fish. I would like to ask you this—and I hope that it is not an embarrassing question—whether you could tell the committee who sponsored or wrote or originated title I?

Mr. Crowley. Well, I think that we can very safely say that it was our legal department and our statistical division.

Mr. Fish. And when you say "our legal department", you mean of the F. D. I. C.?

Mr. Crowley. Of the F. D. I. C., and the board of directors, and we did have some help from Mr. Ekern, who gave us some ideas on this thing. He is an insurance man, an insurance lawyer. Mr. Awalt and Mr. McGrath of the Comptroller's staff also gave substantial assistance.

Mr. Fish. Those are the facts that the committee ought to know. So far as I am concerned, I want to congratulate you. You did a very fine job.

Of course, I want to make it clear that I am referring to title I, and to title I only, in my commendation.

Mr. CROWLEY. I think that what I said about that was correct?

Mr. BIRDZELL. That is correct.

Mr. CROWLEY. May I put into the record here a statement as to losses of insured banks and losses in uninsured banks during the last year?

The CHAIRMAN. Let that come in in connection with your statement touching the same matter, at the proper place.

(The statement referred to is as follows:)

Licensed commercial banks suspending operations during the calendar year 1934

Item	Amounts per $100 of total deposits in active banks	Percent of item to total deposits in active banks
Deposits in suspended banks:	*Cents*	
All banks	10	1/10
Insured banks	.5	1/200
Estimated losses in licensed banks suspending:		
Total losses	3.6	36/1,000
Losses to depositors:		
In banks not insured	3.5	35/1,000
In banks insured	[1] .007	7/100,000
Losses to Corporation	.1	1/1,000

[1] More than ½ of this loss represented losses to depositors with restricted deposits in 1 institution

Mr. BIRDZELL. During the hearing questions have been asked concerning paragraph 5 of subsection (h) of the proposed draft relating to trust funds. That provision is new, and I am not surprised that the members have shown some curiosity about it, and, furthermore, it does deal with quite a technical matter.

Recently I had occasion to discuss the general subject of that subsection with the trust section of the American Bankers Association at their meeting in New York. The discussion is too lengthy, of course, to be reproduced here for the purpose of listening to it, but if the members would like to have the benefit of that discussion I would be glad to leave a copy of what I had to say with your reporter so that it may be put into the hearings.

The CHAIRMAN. Let me suggest, Judge Birdzell, that you incorporate so much of your statement on that occasion as you regard as helpful to the committee.

Mr. BIRDZELL. I think that it would be helpful. I could boil it down some——

The CHAIRMAN. You be the judge of that.

Mr. BIRDZELL. I will leave it with the reporter.

(The remarks of Mr. Birdzell referred to are as follows:)

ADDRESS OF HON. L. E. BIRDZELL, GENERAL COUNSEL FEDERAL DEPOSIT INSURANCE CORPORATION, ON FEDERAL INSURANCE OF TRUST DEPOSITS, AT THE MIDWINTER TRUST CONFERENCE OF THE AMERICAN BANKERS' ASSOCIATION, NEW YORK CITY, FEBRUARY 13, 1935

I am indeed grateful for the opportunity to participate in this conference of the trust division of the American Bankers' Association.

It is always a privilege for one who is daily concerned with problems that affect any group of his fellow citizens to be permitted to present the difficulties with which he is confronted and to gain from the group the viewpoint of those affected by the same problems and whose experiences are gained from a somewhat different angle.

One of the finest characteristics of our basic system of jurisprudence—the common law—has always seemed to me to be that it was founded upon custom, and that it has been sufficiently elastic to yield to the changing customs of society. If this be a virtue in our legal system, as I believe it to be, the virtue is emphasized with respect to that branch of our law which is broadly embraced within the term "law merchant." Much of that law, particularly that dealing with the rights, duties, and obligations of parties to negotiable instruments, was incorporated directly into our legal precedents by the definition and determination of established customs in the market places by those whose contacts and experiences were most immediate and reliable.

If in the formative stages of the law merchant Lord Mansfield was lead to right conclusions by empaneling juries made up of merchants and tradesmen, perhaps it is not too much to expect that even in this day we may proceed with greater assurance in dealing with questions peculiarly affecting a highly specialized branch of business if we seek the counsel and guidance of those who are most familiar with its processes. It is with this hope in mind that I venture to lay before you some of the problems that arise in the administration of the insurance provisions of the Banking Act of 1933 as they relate to the insurance of trust funds.

By way of introducing the discussion, it may be well to refer briefly to some purely elementary matters because of their bearing upon the main questions of interest and because of the principles that rest upon fundamental practices.

In this presence it is not necessary, of course, to speak of the history and development of trust business, nor to trace in detail its connection with commercial banking business. It is sufficient to observe that the banking functions and the trust functions of modern trust companies are and should be kept separate and distinct and to keep in mind at all times that there are certain advantages in combining the two functions under one corporate organization. The clients of a trust company find it convenient to avail themselves of services which can only be furnished by the banking department and, conversely, banking clients find it convenient to avail themselves of the trust facilities of their bank. These advantages have been recognized by the provisions of section 11 of the Federal Reserve Act, which authorize national banks to operate trust departments under the permission of the Federal Reserve Board.

The proper observance of the relations between the bank and its clients and the trust department and its clients requires, however, that the bank shall at all times function as a bank with respect to all funds coming to it in that capacity, while the trust department shall equally observe the fiduciary relation with respect to all funds coming to its trusts.

Under the Reserve Act and under laws existing in many of the States, a national bank or fiduciary company, by complying with stated requirements, may in effect become a debtor to its own trust department without entirely losing its character as a fiduciary. We have, then, one corporate entity sustaining a dual legal relationship with respect to a single account with a single client.

But the act and the Federal Reserve Board in administering it have due regard for the different relationships. The Reserve Board in fixing reserve requirements has provided in regulation D that a bank exercising trust powers need not maintain reserves against trust funds which it keeps segregated and apart from its general assets or which it places on deposit in another institution to its credit as trustee or as fiduciary. But if such funds are mingled with the general assets of the bank, under the authority of the Federal Reserve Act, it is provided that deposit liability thereby arises against which reserves must be maintained. This liability is classified as individual deposit liability rather than as bank deposits.

Assuming, in the language of the Federal Reserve regulation D, that the fiduciary keeps its trust funds segregated and apart from its general assets or that it deposits them in another institution, some might question whether the trust status is strictly maintained. Unless in addition to segregating them the funds of each trust be kept separate and be not mingled with the funds of any other trust, it could be plausibly contended in light of ample trust precedent, that a breach of trust had been committed for which the trustee could be charged. But any such requirement is so foreign to accepted methods for the proper handling of uninvested funds that it would be highly artificial to exact it. A story is told, however, of a trust officer in recent years exhibiting to an examiner his uninvested balances in cash, filed away in the vault, the funds of each trust being kept separate and apart in an effort to comply with the law. It may as well be expected that a warehouseman, in the case of grain or other fungible goods, would provide separate bins for the accommodation of each of his storage customers. It is to the credit, I believe, of the courts of New York that this latter artificiality was abolished many years ago.

Let us look now to some of the specific problems which arise out of the trust and banking relation as we seek to apply the insurance provisions of the Banking Act. Surely in the light of the provisions of the Reserve Act which facilitates the flow of trust funds into ordinary banking channels, there can be no serious question that funds thus legally entering the channels of commerce are deposits within the terms of the law! They are called deposits under the regulations of the Federal Reserve Board and under the existing law which provides for permanent insurance such regulations are controlling. These funds have been regarded as deposits during the temporary period. With this as a premise, how shall we answer the question as to the extent of the liability of the Federal Deposit Insurance Corporation for trust funds which are deposited in the commercial side of the same institution? Shall we regard the company as one depositor and say that the insurance protection extends only to $5,000 or, using the records of the insured institution as a guide, shall we say that each beneficiary is an owner within the terms of the law, and consequently, insured to the extent of $5,000?

Let us look to the law. After prescribing the percentages of insurance coverage based upon the net amount due an owner from a closed bank (and the same language applies to the limited amount insured under the temporary fund), the act says, "*Provided*, That in determining the amount due to such owner for the purpose of fixing such percentage, there shall be added together all net amounts due to such owner in the same capacity or the same right, on account of deposits, regardless of whether such deposits be maintained in his name or in the names of others for his benefit." From this it would seem that if the account be maintained in the banking department in the name of the institution or of its trust department as trustee that it is maintained for the benefit of those who appear upon the books and records of the insured institution to be the ultimate owners, and it is believed that the Insurance Corporation is so liable to each of such owners. The command seems to be clear that we shall determine the amount due, regardless of whether the deposit be maintained in the name of the owner or in the name of another for his benefit and where the records of the institution show for whose benefit the account is maintained the legal measure of insurance protection for each cannot be withheld.

Let us take a second hypothesis: Suppose an insured trust company should deposit uninvested trust funds in another insured institution, the records of the latter will not reflect the beneficial ownership of the funds deposited as in the instance above noted. This would seem to be a single deposit account to be insured as such in the depositee bank. The realization of this situation has led to a great many interested inquiries concerning the extent of the insurance coverage on such a deposit, and it has led further to specific requests that the coverage be extended to meet the practical requirements of the situation. Trust companies making such deposits and desiring to be insured to the same extent as where a similar deposit would be made in its own banking department have made a variety of suggestions. They have offered to pay the assessment upon the additional amount of insurance coverage which would result from a break-down of the deposit according to the interests as they appear upon their own books. (Bear in mind that the assessment is on the insured amount only and not on total deposit liability.) They have demanded, in some instances, that the bank open separate accounts for each trust or each beneficiary. They have offered to file schedules identifying the beneficiaries and showing the extent of their interests, if only they may be assured of corresponding protection. I think we can all agree that there are all but insuperable objections, either from a legal or a practical standpoint, to each of these proposals. Yet, it would seem that if both the initial trust company and the depositee bank be members of the fund, protection should be accorded in this case in the same measure as is given where the deposit be made by the trust company in its own banking department.

Recognizing the reasonableness of such oft repeated requests, the Insurance Corporation offers a solution during the period of the temporary fund based upon this principle: that where a fund member trust company made such a deposit in another insured institution, it would be recognized that the deposit was maintained by it for the benefit of those appearing upon its books and records to be the owners. This gives substantially the same protection to the initial trust company and its patrons as where a deposit is made in the banking department of the same institution. Concerning the assessment, in such case, it was recognized that while two insured institutions were interested there was in fact but one risk; consequently, provision was made for substantially one assessment. Some additional reasons for this will be mentioned later.

Time does not permit a discussion here of the minor details of this arrangement—details which are concerned with the manner of apportioning the interests of the various beneficiaries where deposits are made in several institutions and of the difference which results from exclusive allocation of the funds of each particular trust to one of several general trust accounts as distinguished from depositing uninvested trust funds in general trust accounts without such exclusive allocation—but an effort was made which has been attended with considerable degree of success to make appropriate provision for accommodation to the different methods of handling such transactions. It was necessary to recognize two fundamentally different methods of handling such trust deposits. Where it was the practice of trust companies to group uninvested funds or unexpended balances belonging to certain trust estates, and to deposit each group balance in one of several banks in which the trust company maintains general trust accounts the records of the company would be a sufficient guide in determining the beneficial interests represented in such deposits; but where deposits of trust funds might be made by the trust company without exclusive allocation according to groups of trust estates the interest of a beneficiary in any such deposits in a particular bank would be subject to determination only by applying a formula designed to allocate on a proportional basis. This explains why, in carrying out the general plan for the insurance of trust deposits, under the temporary fund it has been necessary to provide optional plans in order to determine the extent of the insurance coverage on such deposits.

If I may tax your patience sufficiently to enumerate some of the minor factors involved in our consideration of the general problem presented, let me suggest the following:

Filing a schedule of beneficiaries with the depositee bank would involve disclosure of confidential information. This, in some instances, would involve violation of law and it would be objectionable also from a purely business viewpoint. Owing to the constant shifting of interests, the account will be maintained actually for the benefit of persons not named in the schedule and the records of the depositee bank would not identify the owners nor the extent of their interests in the deposit. Where limited insurance is provided, with the depositor as the insured unit, the coverage should not be increased by introducing undisclosed beneficiaries.

Opening separate accounts for separate beneficiaries or trusts involves prohibitory service charges. The depositee bank many properly decline to accept the schedule or to open numerous small accounts.

The furnishing of schedules and certified statements of insured amounts involves examination of numerous trust instruments and a determination of difficult questions concerning vested and contingent interests and the like.

It would seem that any solution of the problem of protection of trust deposits made in the general circumstances outlined above should have regard to these factors to the end that the whole matter may be simplified and be brought into accord with rational practice.

It is believed that the proposed act which is now pending in Congress will acceptably meet this situation. It is there provided that "trust funds held by an insured bank in a fiduciary capacity whether held in its trust or deposited in any other department or in another bank shall be insured subject to a $5,000 limit for each trust estate and when deposited by the fiduciary bank in another insured bank, shall be similarly insured to the fiduciary bank according to the trust estates represented. Nothwithstanding any other provision of this section, such insurance shall be separate from and additional to that covering other deposits of the owners of such trust funds or beneficiaries of such trust estates: *Provided*, That where the fiduciary bank deposits any of such trust funds in other insured banks, the amount so held by other insured banks on deposit on the last day of the month preceding the filing of the certified statement required by paragraph two of subsection (h) of this Section for the purpose of such statement shall not be considered to be a deposit lability of the fiduciary bank, but shall be considered a deposit liability of the bank in which such funds are so deposited by such fiduciary bank. The board of directors shall have power by regulation to prescribe the manner of reporting and of depositing such funds."

Let us briefly note the salient features of this provision:

First, the doubt in the existing law as to whether trust funds while held by an insured fiduciary in its trust department should be considered as deposits is removed. It so considers them. To this extent it is open to the criticism that it is somewhat artificial. But there is no hardship in this because trust companies do not as a rule hold any substantial amount of trust funds for any length of time in a fiduciary capacity. They are either invested or properly utilized as bank funds. Besides, in the event of the closing of an insured trust company the Insurance Corporation could not otherwise give satisfactory answer to the demands of patrons who would have had no means of knowing whether their funds were in one department or another of the institution or deposited elsewhere.

Second, it treats each trust estate as a unit and obviates the necessity for any further break-down.

Third, it preserves the fiduciary status of the depositing trust company by expressly permitting it to be the claimant against the insured bank.

Fourth, it further preserves and recognizes the fiduciary relation and the rightful control of the trust company over the account by treating the insurance of such a deposit as separate from all other insurance for the trust company or for any beneficiary of the trust estates. The amount of the insurance is not affected by the circumstance that beneficiaries may likewise have accounts in the insured bank.

Fifth, in the event of a deposit by an insured fiduciary bank in another insured bank, it recognizes the singleness of the risk. The fiduciary bank is not required to report the amount of such deposit for assessment purposes, this being reported only by the depositee bank.

Sixth, further provision is made to enable the Insurance Corporation to know the extent of its liability.

I am not presenting to you statistics which will show what we all know to be the fact, that a very high percentage of trust funds consisting of uninvested cash and unexpended trust balances and fiduciary accounts generally go into the banking departments of trust companies and into commercial banks to be utilized in the channels of commerce to the same extent as other deposits. These funds, therefore, are properly to be regarded as deposits in any plan which has for its aim deposit protection. They have some characteristics, however, which are not shared by other deposits generally.

In certain circumstances security of one kind or another may be required at the point where they cease to be trust funds and become deposits, but not in all circumstances. Furthermore, they are deposited, as indicated by regulation D of the Federal Reserve Board, not as bank deposits but as individual deposits. By this it is meant to say that a trust company in its trust capacity does not deposit in a bank primarily to promote its trust business or perform its trust function. It does not establish a correspondent relation to facilitate its trust business in the sense that a commercial bank utilizes correspondents to facilitate the transaction of its banking business. Yet such deposits, except to the extent that they may be otherwise secured, are, in common with all other deposits, subject to the hazard which insurance is designed to cover.

It is believed that the characteristics just referred to as peculiar to this class of business warrants the special provisions in the law which have been set out above—provisions which are consistent with existing law and regulations concerning such deposits.

It has been suggested that in view of the security requirements such as are contained in section 11 of the Federal Reserve Act and which are designed to protect transfers of funds from the trust to the commercial side of a banking institution, such deposits might well be excepted from deposit insurance. Similar suggestions have been made from time to time with respect to deposits that are required to be otherwise secured—public funds and the like. The insurance provisions of the Banking Act are clearly intended to apply to all deposits, regardless of whether they be otherwise secured. But from the beginning Congress recognized that other security requirements might properly be relaxed to the extent insurance coverage was effected in the Federal Deposit Insurance Corporation, for it provided that deposits of Postal Savings funds in the banks need not be protected by collateral to the extent they were so insured. In following out the policy thus expressed in the Banking Act of 1933 some of the States are likewise relaxing the requirement for other security for public deposits and bills are pending in Congress to this effect with respect to funds other than Postal Savings funds.

It may well be questioned whether it accords with sound policy for banks to be permitted or required to give collateral security for particular types of deposits. The Supreme Court of the United States last year decided that the power to thus secure deposits generally was not an implied charter power of a national bank, and there are like decisions in a number of States applicable to State banks. Such arrangements, in the event of the closing of a bank, operate to create a privileged class of depositors and in the case of an insured bank they necessarily have an adverse effect upon the Insurance Corporation in that they cut down the amount to be recovered through subrogation to the claims of the insured depositors. Wholly aside from these considerations, however, it must be borne in mind that under the prevailing practice trust companies and trust departments find it advantageous to establish deposit relations with other banks which do not and perhaps which cannot offer security for the deposits, and it would seem to be preferable to establish a uniform rule for insurance coverage rather than engraft a more or less artificial exception. It is believed that such deposits should not be excepted from the insurance provisions of the law.

Trust companies which are not members of the temporary fund of the Federal Deposit Insurance Corporation, which are not members of the Federal Reserve System, and which confine their activities to trust business have likewise exhibited an interest in insurance coverage for such of their funds as are deposited in commercial banks. The problem with respect to these institutions is substantially the same as with respect to institutions which are members of the fund. They desire like coverage, but since they are not members of the fund the powers of the Corporation with respect to examination do not extend to them, and for this reason they are, with regard to their deposits, in the same position as any other depositor. Hence, the Corporation is not able to say to such a trust company that it is maintaining its deposit in a particular bank for the benefit of any specified beneficiary or beneficiaries, and to recognize such undisclosed beneficiaries would involve the introduction of undisclosed owners for the purpose of increasing the insurance coverage.

These companies are all, it is believed, eligible for membership in the fund, and eligible for membership in the Federal Reserve System, and as they may become members they will, of course, share in the benefits of the insurance
These companies are all, it is believed, eligible for membership in the fund,
the existing law. Until such time, however, the only arrangement for insurance protection with regard to them, which the Corporation has been able to suggest, has been that they are insured as one depositor within the limit fixed for one depositor, or if they should find it feasible to so arrange their deposit transactions that they may open separate accounts as trustee for a named beneficiary or for a group of beneficiaries, each separate account would be insured up to the limit of $5,000.

May I leave with you one final word with respect to the Federal Deposit Insurance? I think we can all agree that insurance of bank deposits came into the Federal law at a time when there was the greatest need for restoration of public confidence in the banking structure of our country. I think, too, that we can agree that the general acceptance of the principle has operated to restore and maintain that confidence. We are engaged in an effort to work constructively toward the end that there may never be in our country a repetition of the financial catastrophe that has accompanied the late persistent depression. We can work toward this end and succeed only, in my judgment, with the cooperation of all who are immediately concerned with the major problems presented.

I am glad to be able to express to you this morning the appreciation of the officers of the Federal Deposit Insurance Corporation for the attitude of helpfulness and for the constructive criticism which we have always had from the members of your group. I am personally and particularly grateful for the patience and fine spirit which was manifested by your president, Leon M. Little, on an occasion some months ago when he was good enough to respond to a request for a conference in Washington. If we go forward in this spirit it is our hope that we may all have a part in a great constructive enterprise.

I thank you.

Mr. Crowley. Are there any other questions?

Mr. Sisson. How are we proceeding, in order or out of order, if you will pardon this inquiry?

The Chairman. You are in order right now.

Mr. Sisson. We started out 3 or 4 days ago with the idea that we would make the rounds and give each member of the committee an opportunity to question the witnesses, but the way we are proceeding now, the younger member of the committee will be gotten to on the next Fourth of July.

The Chairman. As you know, I have been away, and when I came in yesterday morning, I thought that the hearings had been pretty well concluded. But let me say to you that everybody on the committee will be glad to hear you right now.

Mr. Sisson. I am not speaking for myself alone, nor in criticism of you.

One of the questions that has been raised here and discussed at considerable length this morning is the question whether the State banks should be required to come into the Federal Reserve System in order to be eligible to membership in the insurance fund, and whether the present provision of law as to when they shall come in, which is, I believe, July 1, 1937, should be changed in this particular bill at this time.

I want it understood, Mr. Chairman, that in anything I say I am not taking any position; I mean by that that I feel that it is not necessary from my point of view to take a position at this time. I do not know whether I have any definite opinion on the matter now or not, but it occurs to me, and I merely make this as a suggestion, that the statement made by Mr. Reilly has considerable merit. There will be two more sessions of Congress before that question becomes imminent, and perhaps we would be in a better position to pass on that after having had a greater fund of experience either at the next session of Congress or the second session of Congress from now, and for the reason stated by Mr. Reilly, I think that my position would be that at the present time we leave that as it is.

However, I appreciate that there are others who have different views and who probably have very sound reasons for them. However, it seems to me that possibly there is an additional reason, one in addition to the reason stated by Mr. Reilly, why that is perhaps academic now, that is, that it is academic for us to decide now whether they shall or they shall not be required to come into the Federal Reserve System in order to get into the insurance fund, and that is that if the Congress should decide that that requirement applies, that they should come in, there is pretty good reason, is there not, why that should be in the law at the present time? In other words, that gives them 2 years' notice or more, and by "them" I refer to the nonmember banks.

Now, I want to ask either Mr. Crowley or Judge Birdzell a question with reference to the provision regarding the limiting of insurance on a single deposit of a trust fund, which I believe appears in subsection (h) of paragraph 5. You fix that limit at $5,000. Is that because of your assumption that the limit of insurance on a single trust-fund deposit is in the permanent writing of this law to be $5,000?

Mr. Birdzell. Yes.

Mr. SISSON. I was wondering if there was any confusion in your answers. When you answered Mr. Williams in regard to the qualification of banks to go into the permanent fund, were you assuming that the permanent fund would contain that limitation of $5,000?

Mr. BIRDZELL. Yes.

Mr. SISSON. Of course, under the present law, if we do not change it, there will be a $10,000 limit up to 100 percent, and then——

Mr. BIRDZELL. Up to $50,000 it is 75 percent, and beyond $50,000 it is 50 percent insured.

Mr. SISSON. Now, regarding another question that was raised yesterday, about the examinations and whether they were irritating and irksome, do you have a practice at the present time of combining in certain circumstances your examination with the examination made by the Comptroller of the Currency?

Mr. BIRDZELL. Not with the Comptroller, but we do with some of the States.

Mr. CROWLEY. You understand, we make no examinations of national banks.

Mr. SISSON. I just want to make this further comment with regard to some questions raised yesterday by Mr. Gifford about the examination of banks and the suggestion—and this is not a question addressed to you; I presume it is not in your province—that the exactions of the Comptroller of the Currency are so great as made through his examiners with respect to liquidity that it is slowing up and retarding our credit.

I presume, Mr. Chairman, that Mr. O'Connor is going to be here before the committee some time.

I would like to call the attention of the committee to this, that perhaps 2 or 3 months ago the Comptroller of the Currency made a speech at an association of bankers, I think in Nebraska, in which he, in my opinion, gave facts which pretty conclusively disproved the statement or the suggestion made by Mr. Gifford, and he gave the figures which were secured by his examinations and a classification of loans, as to whether they are in the slow column, or doubtful, and so forth, and that address of the Comptroller is incorporated in an appendix to the Record some time in January, I believe. If it is not, I make the suggestion, Mr. Chairman, or perhaps the request, with the approval of Mr. O'Conner, of course, that that be incorporated in these hearings. I think it pretty conclusively establishes—at least it does to my mind—that the oft-repeated statement that the Comptroller's examination of banks is the reason why the banks are not lending money as they ought to is merely an alibi on the part of the banks.

The CHAIRMAN. I am sure that the statement of the Comptroller would be valuable in connection with these hearings; I will be glad to have that incorporated in the hearings.

Mr. SISSON. I have one further suggestion, and then I am through. I think that everything else has been covered in which I am interested.

Now, I assume that there will not be any foreclosure on the question as to whether the amount of deposit insurance is going to remain permanently at $5,000, or whether it will be increased to $10,000, and I want to say that the statement of the chairman as to the history of this legislation, on whether State banks should be required to come into the Federal Reserve System in order to participate in this fund, to my recollection is an absolutely correct and accurate statement of it.

But going back to this other question for just a moment, the chairman and those of us who were on the committee when the Banking Act of 1933 was passed containing the provision for deposit insurance will recall that many of the big banks took a very decided and positive position against deposit insurance in general and deposit insurance in any amount, and, in fact, the American Bankers Association—and, of course, the chairman is more familiar with this than, I think, anybody else, because he probably had more to do with deposit insurance than any of the rest of us—met in convention very shortly after the adjournment of Congress, and very solemnly passed a resolution calling upon the President not to put this act into effect.

The CHAIRMAN. That is quite true, and they predicted dire consequences to the economic structure of the country, and then last year they were insisting that the amount of insurance on individual deposits should remain at $2,500 in the permanent law. This year I am not sure, but I think they are now insisting that we make it $5,000 in the permanent law.

In that connection, and not to be critical, but merely because we are dealing with a little history, the American Bankers' Association met here last fall, and that was 1 year from the date of the Chicago meeting to which Mr. Sisson referred, in which they passed a resolution condemning the bank-deposit-insurance law as dangerous to banking institutions and to the general condition of the country; and the first meeting after that was held here last fall.

The first 6 months of operation under the temporary-insurance fund had shown not a single bank failure among the banks that were participating in the fund, and down to the time of the meeting last fall, I think six or seven banks represented the total number of failures, and it showed that the Federal Deposit Insurance Corporation, instead of having encountered an insurmountable loss, was operating at a profit, and the country for the first time in the history of any man at that meeting had had a year of experience practically free from bank failures.

But no mention whatever was made of those developments by any man at the meeting of the American Bankers' Association last fall. They forgot it.

Mr. MEEKS. I want to ask Mr. Sisson this question: The address of the Comptroller of the Currency to which he made reference was delivered in Iowa, was it not?

Mr. SISSON. I think it was in Nebraska.

Mr. MEEKS. There was one delivered in Iowa, and he sent copies of the address to the Members of Congress and invited comment. That is the address that I have reference to. Was that delivered in Iowa?

Mr. BIRDZELL. In Nebraska.

Mr. MEEKS. Thank you; I just wanted to get clear on that.

Mr. FORD. Now, in connection with these examinations, there have been repeated charges made that there were three classes of examinations made of banks. First they said that the F. D. I. C. made them, and then that the Comptroller made them, and then that the R. F. C. made them, and that each one of the examinations called for a different standard as to the classification of assets, and that they never knew where they were.

I would just like to ask, is there any basis for that charge?

Mr. CROWLEY. Let me say to you that we have never examined a national bank and have no authority to do so. The law specifically says that we shall accept the Comptroller's examination.

I believe that we have attempted, in the entire Federal Service, to try to classify assets as nearly uniformly as possible. The R. F. C., on the matter of State banks, has always taken the examination of the Federal Deposit Insurance Corporation. The only time that they have ever sent a man in was where there had been some difficulty arising, where perhaps they already had an investment, or where, when we made our examination and found that perhaps the bank needed additional aid, or something like that, they have gone in with us and tried to work out that situation. There has been no harassing by duplicate examinations of the Federal Deposit Insurance Corporation and the R. F. C. The R. F. C., except in those unusual cases, has taken the examination of the Federal Deposit Insurance Corporation.

Mr. FORD. I was very certain that that was the case, but I wanted to get that in the record.

Mr. BIRDZELL. May I just add to that one thing that is just an impression with me, but I am quite certain that I am correct in asserting it.

I think that about 2 months ago the Reconstruction Finance Corporation announced that it would no longer examine banks, but would take the examinations of our Corporation, of the Federal Reserve Board, and of the Comptroller.

Is not that true?

Mr. CROWLEY. They have been doing it.

Mr. BIRDZELL. I think that they made a formal announcement of that. That is an impression that I have, and we can all check it.

Mr. CROWLEY. Except this, that they do reserve the right to protect their investments.

Mr. SISSON. You mean that they have taken the Comptroller's examination?

Mr. BIRDZELL. If they go into a national bank, they take the Comptroller's examination, and if they go into a State bank that we are interested in, they take ours. They did that with the idea that it would remove the criticism with respect to examinations so far as they were concerned.

Mr. WILLIAMS. Has that been the policy all the time?

Mr. BIRDZELL. It has been the policy quite largely.

Mr. WILLIAMS. I mean, in a case where the R. F. C. was advancing money for capital structure purposes, have they not gone in and made an examination of the bank to determine whether or not they would make that advance?

Mr. CROWLEY. No; except perhaps where there was a condition there where they did not agree with our examinations, or in connection with something that they wanted particularly to verify. In the capital rebuilding program, in better than 90 percent of the cases, they have always taken our examination.

Mr. BIRDZELL. A year and a half ago, they were then engaged in the work of capital rehabilitation, and they might have had to consider banks before we had gotten around to examining them at all, and in that case they would have had to make examinations on their own account.

Mr. WILLIAMS. I have heard that complaint.

Mr. BIRDZELL. A great deal is being done to eliminate the basis for it.

The CHAIRMAN. I am not complaining, exactly, but we should remember in this connection that the R. F. C. act as originally passed contained a provision for loans to banks, and also for loans upon the assets of closed banks, and at that time the F. D. I. C. was not even in existence.

Mr. BIRDZELL. That is correct.

The CHAIRMAN. And the country was in an unprecedented economic upheaval.

Mr. BIRDZELL. That is right.

The CHAIRMAN. And the R. F. C. was acting under a law that required them to take full and adequate security, so that when they began their operations they, of course, were more particular in looking over the assets of banks upon which they were to make loans than they were later on, in the light of later developments.

Mr. CROWLEY. There has been a lot of criticism of the examination of banks. A great deal of that criticism is very unwarranted. You understand that bankers have been under a great strain. They have seen the sloughing away of a lot of values. They have seen a lot of men who under normal times could take care of their obligations promptly unable any longer to do so.

Now, you go in and try to determine the position of a bank, in order that you may try to rebuild its capital position and put it on a sound basis. By the very nature of the trials and tribulations that they have had, if they have not sufficient reserves to absorb their losses and have to write down their capital, naturally there is a feeling of resentment.

But, after the job is all done, it is like the person who has an operation; they feel very good about it.

I know that there are a great many banks that take the examination of the Comptroller's office and of our office and use them as a sort of a club for collections, which is a very unfair thing. They take out the report and say to the borrower. "Don't you see, we have to call this, because the examiner classified it as slow."

Now, there is no criticism on the part of the examining body of a slow asset. The classification of a slow asset only means that the asset is good, but that it cannot be paid at maturity, that it must be spread over a period of time to give the borrower an opportunity to pay it gradually. As long as your banks are sufficiently liquid, it does not particularly mean that they are in hazardous position if a percentage of their loans is in a slow classification; but, as you went into the depression, with your depositors demanding money day by day, it was necessary that the banks, to protect themselves, force this liquidation, and that is the reason why you got your criticism of your slow loans. The depositors were demanding their money more rapidly than the banks could liquidate the loans to furnish it to them. When we have completed our capital rebuilding program, the recovery from the assets that perhaps have been charged off as doubtful and loss may mean considerable in the taking of losses that we have not yet found in our institutions. As we come out of this depression, our banks are again going to have some losses that they will have to face which do not show up on the surface today. A great many borrowers who are struggling today, hoping against hope that they may be able to pay their debts and maintain their businesses, will become discouraged and have to throw it up.

I think that a lot of this criticism is unfair. We will all grant that certain examiners become too officious, and when they get an assignment, they become autocratic; but, as a whole, I think that the examiners have tried to be sympathetic in taking into consideration the mental state of a great many of these bankers.

The CHAIRMAN. Now, if there is anybody else who desires to propound further inquiries to these gentlemen, I will be glad for you to proceed.

Mr. CROWLEY. Before we close, I would like to express our thanks for your kind consideration. Your questions have been most constructive, and if there is any additional information that we may furnish, we shall be very happy to do so.

The CHAIRMAN. If no one else has any more inquiries to make, I will say that we have finished with Mr. Crowley and Mr. Birdzell, and we will meet again tomorrow morning at 10:30, and I will try to advise the members of the committee this afternoon just what the program will be tomorrow. Before doing that, I want to talk to the comptroller, to Mr. Eccles, and to the members of the committee.

(Ordered inserted in hearing)

SPECIAL REPORT OF PUBLIC OPINION AS GATHERED BY THE NATIONAL EMERGENCY COUNCIL ON THE ACTIVITIES OF THE FEDERAL DEPOSIT INSURANCE CORPORATION

ALABAMA

March 26, 1935.—Never any criticism of this activity.

April 9, 1935.—Stands highest in public opinion of all emergency measures; has restored confidence in banks and resulted in greatly increased deposits.

ARIZONA

April 9, 1935.—Apparently public very favorable to Federal Deposit Insurance Corporation. This agency has restored confidence in all banks and undoubtedly exerted considerable influence in abolishing hoarding on the part of the people who had previously felt that banks were unsafe and that they should keep their money in cash at home. Every bank in this State except one is a member. Information at hand indicates that the citizens of the district where this bank is located are very dissatisfied and are not depositing their funds in this bank due to the fact that it does not have deposit insurance. Considerable interest expressed by public in the announcement that deposits in building and loan associations might be insured. General summary would be that the public is very much interested in continuation of deposit insurance and that it is a very determining factor in restoring and maintaining confidence in the banking institutions.

ARKANSAS

April 9, 1935.—Representative bankers advise that public reaction to Federal Deposit Insurance Corporation is 100 percent favorable. Great majority of bankers also favorable, but believe present limit might wisely be reduced to $2,500. Two bankers state they are strongly opposed to plan in principle. None interviewed has ever heard criticism of insured deposits by customers.

CALIFORNIA

April 9, 1935.—Public opinion strongly back of Federal Deposit Insurance Corporation, despite objections of some larger banks to paying premiums.

COLORADO

April 9, 1935.—Public opinion here practically unanimous in favor of Federal Deposit Insurance Corporation.

CONNECTICUT

April 9, 1935.—Public seems entirely indifferent to present Federal Deposit Insurance law. Some 12 or 13 banks in Connecticut have not subscribed to plan and their deposits have not been affected. Some depositors inquired of their banks about this insurance when it became effective, but none has mentioned it to the Hartford banks in months. There is no demand here for increasing amount of insurance above $5,000, as 95 percent of all accounts are fully protected under present law. No Connecticut savings banks subscribed to plan because of adverse opinion of State attorney general. I can find no objection by savings bank depositors. State director personally feels that the present $5,000 limit is sufficient in Connecticut. This State has been particularly fortunate in having very few bank failures.

DELAWARE

April 9, 1935.—Due to fact that no bank failures occurred in Delaware, the public has shown little interest in Federal Deposit Insurance Corporation. Contacts made are all favorable.

FLORIDA

April 9, 1935.—Have contacted 20 various business houses. Everyone heartily endorses the Federal Deposit Insurance Corporation. Believe this sentiment universal in Florida.

GEORGIA

April 9, 1935.—Federal Deposit Insurance Corporation was welcomed by great mass of people. Has been important factor in restoring confidence in banks, particularly smaller institutions. Regarded by many as one of the most constructive steps in present national administration. Increased savings deposits in many banks believed traceable to insurance plan. While activities not subject to general discussion now, individuals and business, especially smaller business, finding satisfaction in safety provided by its operation.

IDAHO

February 19, 1935.—Deposit insurance remains the cornerstone of public confidence in our banks.

March 26, 1935.—Remains cornerstone of public confidence in banks. Bankers admit Federal Deposit Insurance Corporation has produced solid public confidence in banks.

April 9, 1935.—Public opinion overwhelmingly favorable and confidence in banks remains solid with deposits increasing.

INDIANA

April 9, 1935.—Has restored confidence in banks, but has not resulted—for some reason—in a relaxation of bank credit.

IOWA

April 9, 1935.—Public reaction to Federal Deposit Insurance Corporation on bank deposits definitely favorable. Small depositor, which includes savings depositor, is very favorable to insurance of deposits. Best evidence of this is literally hundreds of cases reported to us of money taken from Postal Savings, from hoardings, and from larger banks in border States and deposited in Iowa banks after inception of Federal Deposit Insurance Corporation. There is some disposition to the belief that insurance is so satisfactory to the depositor that he does not seek other investments. Large commercial accounts do not emphasize insurance on their deposits, except as it tends to restore confidence in the bank and thereby stabilizes banking conditions and satisfies small depositor, who as a rule is a cause of runs on banks. Public is grateful and happy for benefits of Federal Deposit Insurance Corporation.

KANSAS

March 5, 1935.—Banks now beginning to fully appreciate the value of this activity with the result that an increasing number are subscribing, however, many banks still remain without insurance.

April 9, 1935.—Although many banks remain without insurance, it has greatly increased confidence in financial institutions.

KENTUCKY

April 9, 1935.—Much appreciated by public generally. Resulted in growing increase of deposits in all banks. Smaller banks quite enthusiastic. Some larger institutions feel their independence, objecting to expense of operation. Some suggest annual assessments of service; others suggest limitation of amount of insurance to $5,000. These objections made some months ago but little protest at present time. Unquestionable demand for retention of act.

MAINE

April 9, 1935.—Public sentiment favorable to Federal Deposit Insurance Corporation. Maine commercial banks favor this. State savings banks have centrally managed liquidity fund.

MARYLAND

March 26, 1935.—Activities progressing quietly.

MICHIGAN

April 9, 1935.—From every source I get only favorable public reaction to Federal Deposit Insurance Corporation. Belief quite general that this agency is reestablishing faith in banks. Increased deposits in Michigan banks best proof of renewed confidence.

MINNESOTA

March 5, 1935.—Agency has done outstanding work and 95 percent of banks in this State are insured. Public well informed and very favorable toward this activity.

March 26, 1935.—Agency 100 percent efficient and popular with both public and banks.

April 9, 1935.—Exceedingly popular and has produced great public confidence in banks.

MISSISSIPPI

April 9, 1935.—Public opinion appears entirely favorable because of Federal protection.

MISSOURI

April 9, 1935.—Reaction of public and State banking department to Federal Deposit Insurance Corporation is universally favorable. Deposits substantially increased. More than 500 State banks have voluntarily come under Federal Deposit Insurance Corporation and only 40 have not. Most of these 40 are small or family banks and expense is deterring factor. The favorable public reaction is general over entire State and also the four-State area. It is recognized as an essential part of the banking system.

MONTANA

March 26, 1935.—Has greatly restored confidence and receives almost unanimous acclaim.

NEBRASKA

February 19, 1935.—Agency has made a fine record in this State with a high percentage of deposits now insured.

NEVADA

April 9, 1935.—After experience of last 3 years when banks were blowing up like firecrackers in Nevada, depositors unequivocally approve deposit-insurance plan. They are not interested in howl of big banks, who may have to carry premiums for some of their weaker brethren. They feel this latter will be an incentive to insist on good banking practices and will insure national supervision and inspection.

NEW HAMPSHIRE

April 9, 1935.—About 1 out of 50 know anything about it. New Hampshire Bankers Association report public neither informed nor interested. Reaction nil.

NEW JERSEY

March 5, 1935.—There is little comment concerning this agency, but it is believed that this activity has full public support.

March 26, 1935.—There is little said about this agency, its activities being accepted as a matter of course.

NEW MEXICO

April 9, 1935.—Have heard of no comments either pro or con in New Mexico.

NEW YORK

April 9, 1935.—Public reaction to Federal Deposit Insurance Corporation not wide-spread, but generally favorable. Larger banks in Manhattan protest method of assessment, claiming only insurable amounts of deposits should be taxed. Otherwise not opposed, although unenthusiastic.

NORTH CAROLINA

April 9, 1935.—General public reaction most favorable. Find in contacting number of bankers, who will eventually help mold public opinion, in vast majority think $5,000 coverage sufficient and favor definite premium sufficient to cover, but to be lowered if justified later. Majority same parties favor premium on insured deposits only. Five thousand limit covers 95 percent depositors banks this State.

NORTH DAKOTA

February 19, 1935.—Public attitude and editorial comment uniformly favorable.

March 26, 1935.—Has restored public confidence in banks and is now accepted as a matter of course.

April 9, 1935.—Agency has restored confidence in banks and public opinion remains wholly favorable.

OHIO

March 26, 1935.—Program has been exceptionally beneficial and remains least criticized of all emergency activities.

April 9, 1935.—Is least criticized of all emergency agencies.

OKLAHOMA

April 9, 1935.—Public reaction reveals this is one Government program with which general public will go all the way. No derogatory comment to Federal Deposit Insurance Corporation was made in interviews with large number of Oklahoma business men and individual depositors. Editors and newspaper clipping bureaus report Statewide approval of program as reflected in press.

Increased deposits indicative of restored confidence. Group 4 of Oklahoma bankers' association in convention at Ardmore yesterday passed resolution recommending titles 1 and 3 of Congressional Banking Act of 1935 and commending work of Federal Deposit Insurance Corporation. Group 5 in Tulsa today expected to pass similar resolution according to secretary of association. These group meetings represent approximately 450 eastern Oklahoma bankers. State banking commission reports only two failures in State banks since inception of Federal Deposit Insurance Corporation. Continuance of Federal Deposit Insurance Corporation under competent management felt essential to continued faith in banking system.

OREGON

February 19, 1935.—Has produced desirable feeling of security of average citizen in his bank account.

PENNSYLVANIA

March 26, 1935.—Has functioned very successfully and restored confidence.

April 9, 1935.—Has greatly strengthened banking system, although many small banks, due to limited capital, criticize the provision compelling them to join the Federal Reserve System by July 1, 1937, in order to maintain their insured status.

RHODE ISLAND

April 8, 1935.—Banking situation here unusually strong, therefore, except for added confidence due to Federal Deposit Insurance Corporation, difficult to determine public reaction.

SOUTH CAROLINA

February 19, 1935.—Has restored confidence in banks. Comment is frequently expressed that this program is one of the most important in "new deal."

March 26, 1935.—Public has great faith in this activity.

April 9, 1935.—Most beneficial.

SOUTH DAKOTA

February 19, 1935.—Comment wholly favorable, with the exception of a very few bankers who are opposed to the principle of this activity.

March 5, 1935.—There is little comment concerning this agency, but it is believed that this activity has full public support.

TENNESSEE

March 5, 1935.—It is suggested that means be provided to inform the public of a bank's insured status by means other than the notices on tellers' windows.

March. 26, 1935.—Has restored public confidence in banks.

TEXAS

March 26, 1935.—Well-staffed and functioning effectively.

April 9, 1935.—Continues to function effectively.

UTAH

February 19, 1935.—Public opinion generally favorable.

March 26, 1935.—Public unanimously for Federal Deposit Insurance Corporation, although some bankers and financial interests remain skeptical.

VERMONT

April 9, 1935.—Public reaction to Federal Deposit Insurance Corporation quiet but favorable. About half the banks use their participation in their advertising. Bank public apparently take it as an accomplished fact and rely upon it, although not particularly outspoken in their comment.

WASHINGTON

March 26, 1935.—Has resulted in vastly improved banking conditions and a general increase in deposits.

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April 8, 1935.—Has resulted in improved banking conditions, although need is seen for means to enforce provisions of Federal Deposit Insurance Corporation.

WEST VIRGINIA

April 9, 1935.—Public reaction to Federal Deposit Insurance Corporation quite sympathetic and guaranteeing of deposits has stimulated confidence in banking institutions. Deposits have materially increased. Bankers, however, are opposed to proposed amendments to existing law now pending in Congress.

WISCONSIN

April 9, 1935.—Don't hear about it. Deposits on increase. Only through restatement of fact that money is in circulation, do we know about its works. Banks favorable.

WYOMING

April 9, 1935.—Banks noncooperative toward this activity.

(Thereupon, at 12:45 p. m., an adjournment was taken until Friday morning, Mar. 1, 1935, at 10:30 o'clock.)

BANKING ACT OF 1935

FRIDAY, MARCH 1, 1935

House of Representatives,
Committee on Banking and Currency,
Washington, D. C.

The committee met at 10:30 a. m., Hon. Henry B. Steagall, chairman, presiding.

The Chairman. All right, gentlemen, we have with us this morning Mr. O'Connor, Comptroller of the Currency, and he will discuss the bill. I am going to suggest that Mr. O'Connor be permitted to proceed in his own way, without interruption, until he shall have finished his preliminary statement, if that is agreeable with the committee.

We will be glad to have you proceed without interruption, until such time as you desire to be interrogated, Mr. O'Connor.

STATEMENT OF J. F. T. O'CONNOR, COMPTROLLER OF THE CURRENCY

Mr. O'Connor. Mr. Chairman and gentlemen, I assume that, from the inquires I have received from the members of this committee and others in Congress, that they have a very especial interest in the national-banking situation, inasmuch as Congress is more directly and largely responsible for the national banks, and I, of course, have most to do with that possibly as Comptroller, and also as a member of the board of the Federal Deposit Insurance Corporation, and I would like to discuss the general situation as well as the bill.

The Chairman. Mr. O'Connor, if you permit me, I am going to suggest that you address yourself, first, to title I of the bill, as we have had that solely under discussion down to this time. After you shall have finished with that, we will then decide as to when we will take up the other parts of the bill, if that is agreeable to you.

Mr. O'Connor. Yes; thank you. Unless the committee desires it, or unless they do not desire it, I would like to bring you up to date with a brief picture of the national banking situation as it is today, from the office of the Comptroller, with reference to these closed banks and unlicensed banks that we started with after the termination of the banking holiday of 1933.

At the close of the banking holiday in March, we had 1,417 national unlicensed banks, and these banks had in deposits $1,971,960,000. The question naturally arises before us this morning as to what has been done with those banks and those deposits, and I am giving you the figures of my office up to the first of February, as we release a monthly report at the end of every month.

We have reorganized 1,091 of these banks with deposits of $1,805,622,000. Thirty-one of these banks decided to go out of business, and they paid their depositors in full, $11,513,000.

There was placed in receivership 292, with deposits of $151,540,000.

Now, that accounts for 1,414, leaving 3 unlicensed national banks at the beginning of the present month, or the beginning of February, rather, and those 3 had $3,280,000 in deposits.

Let us now take up the problem of these banks in receivership. We have paid to depositors in those particular banks, $51,084,265; and we have plans approved for reopening four of these receivership banks, which will release an additional sum of $1,427,000.

That is the complete picture, gentlemen, from March 1933 to the first of February of the present year, and you will notice that all that remains of approximately $2,000,000,000 in the receivership banks is approximately 5 percent of that amount.

That is, briefly, the story of the unlicensed national banks after the holiday.

During the same period, from March 16, 1933, there has been distributed to depositors in all banks, those closed before the bank holiday and since the holiday, $621,920,917; and, roughly, I believe that represents, gentlemen, about 54 percent of the total in the national banks; and please bear in mind that I am only referring to the national banks in this statement.

The total number of receiverships accumulated over the years up to the present time, including those that I mentioned of unlicensed banks, was 1,547, and they had deposits, at the time of the closing, of $1,880,710,184, and there has been paid to depositors to date of February 1, 1935, $1,016,836,666.

In addition to that work, the Comptroller's office has been very much interested in the sale of preferred stock in the national banks, to do two things: First, to strengthen the capital of the national banks; and, secondly, to make more money available for credit, and also to relieve the banks from compelling debtors to pay who are not able to pay at present, but had good, going businesses, and if permitted to go along, could, in time, pay. That was the object of purchasing preferred stock in national banks.

I have received this morning from the Reconstruction Finance Corporation the purchases of preferred stock and capital notes and debentured outstanding, and also loans on preferred stock outstanding, divided, first, national banks and, secondly, State member banks, and third, nonmember banks.

In national banks the loans on preferred stock outstanding were $9,624,716.30; purchases of preferred stock $437,577,064.65, a total of $448,444,001.09.

In State member banks the loans on preferred stock outstanding—and that probably would be also debentures or notes where they were not permitted by State law to issue preferred stock—$1,064,618.44; and purchases of preferred stock, capital notes, and debentures outstanding, $174,943,610.25, or a total of $176,008,228.69.

With reference to nonmember banks and other State banks that are not members of the Federal Reserve System, loans on preferred stock outstanding, $8,797,658.20; purchases of preferred stock, capital notes, and debentures outstanding, $242,213,311, or a total of $249,768,749.06.

Now, that makes a total of the loans by the Reconstruction Finance Corporation on these three classes of banks of $19,486,992.94; and purchases in the capital structure of $854,733,985.90, and a grand total of $874,220,978.84.

I think you will be interested in knowing that there was purchased. locally, of the preferred stock in national banks, $73,366,655.

I think you will be interested in having pointed out, so we will have the record clear, what we mean by loans on preferred stock or capital debentures by the Reconstruction Finance Corporation and the figure I have just given you, the figures with reference to purchases locally; it is the policy of the Reconstruction Finance Corporation that when a bank, whether State or national, needs capital strengthening, first an effort is made to get the people in that community to buy the stock. That seems to be the agreed and very sound policy, that we all feel that we would much rather have the people in the community own these banks, of course, than the Government; the Government, as I take it, being only a temporary expedient in the emergency, and that the stock should be purchased by stockholders and others locally.

Now, another plan that has been worked out, which is also sound, is that when local interests are willing to make purchases of the capital stock to strengthen the bank, preferred stock or debentures of capital notes, who are not able to pay for them in cash, which, of course, must be done, the Reconstruction Finance Corporation will take that stock and other collateral and lend against it, so that it gives the purchasing party an opportunity to finally buy his stock and own the bank.

Just for the record, because you gentlemen, of course, thoroughly understand it, but so someone else reading the record will have it clear, when we speak in the same breath about preferred stock and capital notes and debentures, the reason for that is that Congress permitted national banks to sell preferred stock, Congress having exclusive jurisdiction over the national banks.

Most of the State laws, however, do not permit the sale of preferred stock in State banks; and, therefore, Congress worked out the problem for them of permitting them to sell debentures, or sell capital notes; and the interpretation of all of the banking departments of the Government is, that those notes and debentures are considered the same as preferred stock in the capital structure of the banks, some States permitting notes and some permitting debentures to be sold. I thought that ought to be cleared up, but it does not need to be cleared up for you gentlemen, but someone else who might read it.

I would like, with your permission, Mr. Chairman, to read my recommendations with reference to title I, which is the bill under consideration, which is found on pages 14 and 15 of the annual report of the Comptroller of the Currency, for the year ending October 31, 1934:

Consideration should be given to strengthening the provisions of the law governing the Federal Deposit Insurance Corporation. In view of the protection afforded depositors, no doubt many of the States will follow the precedent established by Congress in eliminating the double liabilities on shares of stock.

Relieving shares of stock from the double liability, and the insurance of bank deposits offer added encouragement to the establishment of new banks. Great caution should be exercised in the future in the establishment of either State or national banks, or branches of either, in order to prevent a repetition of the failures of a few years ago. Under the present law, if a bank's assets are sufficient to pay its liabilities, the Federal Deposit Insurance Corporation must accept it as a member, although it may have no capital structure.

The Comptroller's Office, under existing law, is in a position to require national banks to maintain adequate sound capital, and also to prevent the organization of a new national bank unless it has adequate, sound capital, and unless there is need for additional banking facilities in the location chosen, and a reasonable prospect that the bank will operate successfully. The Comptroller's Office is thus able to protect the interests of the Federal Deposit Insurance Corporation in those respects with reference to national banks, particularly since the Comptroller is a member of the board of the Corporation. There is, however, no such safeguard as to State banks and it is believed that the law governing the Federal Deposit Insurance Corporation should be amended to make a State bank's admission to the fund conditional upon the approval of its capital structure by the Corporation; and in the case of a new State bank, the board should be required to pass upon the need for additional banking facilities in the place selected and upon the reasonable prospect of the bank's successful operation.

It would be well to consider whether the law should not be further amended to permit the Corporation, under proper limitations, to purchase assets of an insured bank for the purpose of assisting in merging such a bank with another, or of reorganizing when it becomes apparent that a loss to the Corporation is impending. In this manner, losses may be limited or minimized. Under the present law, the Corporation may do nothing until a bank is closed and after that its recovery is dependent upon liquidation. Recoveries through liquidation are certain to be less than the values which may be placed upon the same assets by a going institution.

The law should be amended to provide for examination by the Corporation of State nonmember banks which become members of the fund. An express provision should be made for reports of condition by all insured banks not now reporting to a Federal agency at intervals of not oftener than twice a year, such report to be as of the same date as a call report made by national banks to the Comptroller of the Currency.

The Banking Act of 1933 in section 11, subsection (d) makes specific provision that security for deposits of postal savings funds in banks shall not be required to the extent that such deposits are insured. A general statutory provision should be enacted so that no security shall be required under Federal statutes for any deposits in banks to the extent that deposits referred to in such statutes are insured under section 12 (b) of the Federal Reserve Act, as amended.

It is believed that Congress might well consider the advisability of levying an annual assessment under the permanent plan in lieu of an assessment merely to repair insurance losses, and that it might make provision for carrying a portion of the assessment in a reserve which could ultimately operate to decrease such annual assessment. In banking, as in other businesses, it is desirable when practicable to anticipate the fixed charges, and so far as possible, the cost of insurance should be made a fixed charge subject to reduction through economical and efficient operation.

Miscellaneous incidental matters affecting the Federal Deposit Insurance Corporation should be provided for as follows:

Extend criminal provisions applicable to officers of member banks to officers of all insured banks. Eliminate reference to par value of Federal Deposit Insurance Corporation stock in subsection E of section 13 (b) of the Federal Reserve Act by substituting therefor the amount paid for said stock; extend the prohibition in the present law against gratuities to Federal examiners to examiners of all insured banks and their officers and likewise extend to same the prohibition against disclosure of confidential information; give the Federal courts jurisdiction of actions against the Corporation; extend to the Corporation the protection now given to other Federal institutions against misleading use of their names; and extend to all insured banks the present law making robbery of member banks a Federal offense.

Mr. Chairman, I am ready now for questions.

The CHAIRMAN. I am going to suggest that we begin with Mr. Reilly.

Mr. REILLY. I have received quite a few letters recently, Mr. O'Connor, from old national banks, inquiring as to the possibility of relief from that double liability of assessment through an act of Congress, or some other method. What is your view as to the advisability or necessity or wisdom of any act by Congress at this time?

Mr. O'CONNOR. I covered that in my annual report, and if you will permit me, I will give you that. On page 12 of the annual report of the Comptroller of the Currency for 1934, in answer to Mr. Reilly's question, I make this statement:

> Section 22 of the Banking Act of 1933 relieves shareholders of national banks from the additional liability imposed by Revised Statutes 5151, as amended, and section 23 of the Federal Reserve Act, as amended, with respect to shares issued after the date of enactment of the act. Bills were presented in the last session of Congress to extend this relief to all outstanding shares of stock of national banking associations, regardless of date of issue.
>
> In the event it is determined to completely eliminate this assessment liability of shareholders, it is suggested that serious consideration be given to providing for increasing the surplus of national banking associations until same equals the amount of its common capital stock, thereby restoring to the bank's creditors the protection now given by the potential assessment liability of the shareholders and maintaining a sound banking structure.

Let me say, in that connection, that is a matter that our office, Mr. Congressman, has given very serious consideration to. We must at once appreciate the fact that, by eliminating the double liability on all national banks, we have tremendously weakened the banking structure of the nation. That must be clearly kept in mind. Therefore, I have suggested that, if the Congress decides to eliminate the double liability on all old national banks, the banks should be required to build up, out of their profits, some substantial amounts which shall go into a surplus fund of the banks.

Thereby, you will have in a bank and behind the capital structure, really, in time, the double liability and then relieve the stockholders of it. I appreciate that many people object to relieving the stockholders of this double liability in banks, but those, I think, ought to consider this: First, that banking investments are greatly discriminated against, because of that double liability, investors not wishing to put their money into a corporation upon which they may be called upon later to pay double the amount, or the same amount they have already contributed; and particularly those who make investments feeling that, not during their lifetime, but it might happen that, at their deaths, they have unloaded onto their widows and children liabilities that might wipe out the whole assets and whole savings of that man during his lifetime, which has happened in some instances, unfortunately.

And, again, I think it ought to be pointed out to those who criticize Congress for doing this, that you levy the assessment at the very time when either the holder of the stock or his family is less able to pay it, because in good times you do not need it, and it is only when we get into a period such as we have been going through that we put this extra burden and hazard upon people who are less able to bear it.

It has been the policy of our office to look into every case individually, because we have the duty imposed upon us by Congress to collect these assessments, and when people are perfectly able to pay we require them to pay; we have no option, we cannot give away money.

When people who have property and are not attempting to transfer it to defeat this assessment, or to sell it, come to us and tell us that they are attempting to secure it, but they need time, in every instance we have worked out a satisfactory arrangement with people in those circumstances, and we have not had any particular complaint that we have been unduly harsh in that respect.

Now, directly to the Congressmen, I have given you my view of that, and have tried to answer the criticism.

Mr. REILLY. Your view would be that any legislation by Congress waiving the double liability in the old national banks should be limited to those institutions that have built up a reserve equal to their capital stock?

Mr. O'CONNOR. That is not quite correct. I would abolish the double liability on all banks and provide for the building of the surplus to 100 percent of capital in the future.

Mr. REILLY. I wonder whether any of that kind of legislation would be constitutional. Has Congress any right to declare, by law, that the depositors in a bank, say of $500,000 capital stock, shall be denied the right to levy to the extent of that capital stock, in case the bank should go into insolvency?

Mr. O'CONNOR. Mr. Congressman, you have raised a very important question, and if I have retained any law since I got into the banking business, I do not believe that Congress could pass a law effectively today that would relieve the shareholders from double liability as to depositors and creditors who have entered into a contract with the bank at that time, when their rights were fixed; and their rights are fixed and their contractual relationship with the bank does exist, and I do not think Congress can destroy it.

The only thing Congress can do would be to throw the operating period into the future a sufficient length of time, so that the existing creditors would not be affected, and that would be a contract—because every depositor has a contract between the depositor and the bank—they would then come under the terms of the new law.

I think you have raised a ver yimportant question.

Mr. REILLY. Or give them time to take their money out of the bank and put into some other bank?

Mr. O'CONNOR. Yes.

Mr. REILLY. Right on that point, on that question, what difficulties do the banks encounter when they attempt to reorganize and come under a new law? Suppose you had a national bank of $500,000 capital stock and it wants to get away from its double liability, is there any difficulty in reorganizing and getting a new charter by changing some word in its title?

Mr. O'CONNOR. No; it can do that. Any corporation has that right, but there is a great many procedural difficulties in it.

In the first place, they have got to get the consent of all of their stockholders and explain to them why they are doing it, and bankers rather hesitate to take all of these issues and explain them and get consent from several hundreds or thousands of stockholders and, frankly, since the law has been in effect, we have not had that question presented. There are probably one or two cases that I am not familiar with, in no number that would affect the attention of anybody.

That is my best answer, and I believe bankers have the feeling that it is difficult to do it.

Now, under the present law, Mr. Congressman, you have this: We have in national banks some stock that is subject to double liability, and in the same bank we have stock that is not subject to the double liability.

Mr. REILLY. How does that happen?

Mr. O'CONNOR. Because all the new issued stock is not subject, as you provided in the act, to the double liability.

The CHAIRMAN. Right there, let me trace the history of this legislation. I might say I am responsible for the amendment to the law, the purpose of which was to remove the double liability of the stockholders. The bill as it passed the house, applied to the need to something constantly requiring—I mean the bill as reported by the committee to the House had that language, and the bill was amended in the House in language that I cannot just at the moment recall. I asked Mr. Awalt, a moment ago, if he remembered, but he does not recall the exact language, but in conference the provision was rewritten, and I suggested to Senator Bulkley—the fact was that the Senators in Congress were hesitant about agreeing to it and I suggested to Senator Bulkley, who is an able lawyer, that he rewrite the language so as to make sure of the accomplishment of the purpose in mind.

It was my thought that the language employed by the House in the passage of the bill was not adequate to accomplish the purpose, and Senator Bulkley suggested a new idea which made it apply to stock thereafter issued.

I, at least, and I cannot speak for the other members of the conference committee, but for myself, I proceeded upon the idea that all stock repurchased or resold had to be reissued and that, therefore, the language making the relief applicable to stock thereafter issued would cover all old stock, if transferred.

So that the Comptroller's office—and I am not questioning the soundness of the decision—conclude the act to apply to stock thereafter authorized to be issued; or in other words, applicable only to new issues of stock. The construction was not in line with my own idea. However, that is not important now.

I understood you to say that, in order to make such a provision applicable to the existing stock, or to old stock, it would be necessary to make the effective date at some future time as would remove all question of the contractural relationship between the stockholder and the depositor, or any other creditor of the bank.

I am wondering if you are not slightly in error about that, for this reason: That under the original law, any stockholder of capital in a national bank might transfer his stock and relieve himself of all further liability by meeting the requirements of the existing law, which fixes a definite time within which the statute of limitations would operate against a stockholder who had transferred his stock in good faith, and the period, as I remember it, was 60 days, as I remember, Mr. Awalt.

Mr. AWALT. That is correct.

The CHAIRMAN. So that, in any event, any stockholder could have relieved himself, under the original law, completely from any liability to assessment, if he transferred his stock in good faith 60 days before the failure of the bank, or the period of liquidation; is that true?

Mr. O'CONNOR. Then, Mr. Chairman, the man to whom he transferred it would be liable.

The CHAIRMAN. What was that?

Mr. O'CONNOR. The stock is still liable. The man to whom he transferred it would then be liable.

The CHAIRMAN. Yes, that is quite true.

Mr. O'CONNOR. You have not, you see, eliminated——

The CHAIRMAN. I am speaking now of the contractual relationship of the man in the first place. That man could relieve himself of the contractual relationship after a period of 60 days, if he transferred his stock in good faith?

Mr. O'CONNOR. To make it clear, we had better talk about the liability attached to the share of stock, rather than to the individual, and that you cannot abrogate by act of Congress.

The CHAIRMAN. Let me ask you this question: Do you know how many States have laws providing double liability on the capital of banks—State banks?

Mr. O'CONNOR. My recollection is, nearly all of them.

The CHAIRMAN. Nearly all of them?

Mr. O'CONNOR. Nearly all of them. That is my recollection.

The CHAIRMAN. I am a little surprised to hear that. Although I have never seen the figures.

Mr. O'CONNOR. I think we can get a very clear picture if we ask each member of the committee what his State holds, and you can then get a cross section of the whole country.

The CHAIRMAN. It was my impression that only a few States provided for the double liability.

Mr. O'CONNOR. The members of the committee could tell us quickly what State has not got it.

The CHAIRMAN. Let me ask you this question, in that connection: What would you think of a provision that would go the whole way in the limitation of contractual obligations and existing difficulties in relieving stockholders in national banks, in all States where no double liability attaches to the stockholder, or to stock issued by a State bank?

Mr. O'CONNOR. I can say, Mr. Chairman, and I am just giving my opinion from my experience as a lawyer, my answer would be that it would not avoid the constitutional objection that Congressman Reilly has mentioned.

The CHAIRMAN. I don't think you quite got my question. I mean aside from those difficulties, insofar as you might do so—I am speaking now of the policy of duplicating the same law as to the liability of stockholders.

Mr. O'CONNOR. That is a matter of policy entirely within the discretion of Congress, with the limitation that I previously stated to the committee with reference to the constitutional objection. It was placed, as I believe, in the future a sufficient length of time——

The CHAIRMAN. My question contemplated the removal of those difficulties.

Mr. O'CONNOR. Oh, I see.

Mr. CROSS. Let me ask a question right there, Mr. Chairman.

The CHAIRMAN. Certainly, Mr. Cross.

Mr. CROSS. See if this would not eliminate the situation: I understand, of course, about making a deposit in a bank, and that at the time I do it the stockholders are subject to double liability. I assume, of course, that I have a contract with them, or when I put it in the bank, they are liable, and that gives me better security to get my money back. But suppose you were to put a clause in the law that all deposits hereafter, the new deposits that go in a bank, shall not have the double liability, so that when I put in money in it, in that bank, after that—any money that I put in there before that, I can take it out, all right, but that money that I put in after that is no longer put in there under a contract that I can reap the double liability on the stockholders, so why not put in a clause like that relieving those stockholders of that double liability only in reference to all new deposits?

Mr. O'CONNOR. Mr. Congressman, I think you are absolutely correct, because whenever you do that, you establish a new contractual relationship. Could I suggest probably that some difficulty would be that of administration, of segregation of the amounts, the determination of the dates of the deposits, and then waive the assessment for depositors who are under the double liability and segregated from those that are not?

Mr. CROSS. Suppose I had $10,000 in a bank today in my checking account—of course, I am putting money in the bank and drawing money out, and my checking account will add up to $10,000. Now, when my checking account adds up to that, then the stockholders are not liable for the penalty, for the double liability?

Mr. O'CONNOR. You are absolutely correct. Mr. Congressman, may I call your attention to page 53 of H. R. 5357, section 304, which reads:

> Section 22 of the Banking Act of 1933, as amended, is amended by adding at the end thereof the following sentence: "Such additional liability shall be on July 1, 1937, with respect to shares issued prior to June 17, 1933, by any association which shall be transacting the business of banking on July 1, 1937."

I just call your attention to that because that is the section that you would operate on, if I might use that word, if you decide on what you are discussing.

Mr. HOLLISTER. Mr. O'Connor, your idea is that, even with respect to the deposits which have been incurred, or which have been made obligations of the bank, incurred prior to the enactment of this act, if enacted—if a certain length of time, 2 years or something more is given, that notwithstanding the obligation that exists at the time the deposit was made, which would give them ample opportunity and they would be charged with knowledge of the change in the act, no depositor could claim it after that time?

Mr. O'CONNOR. Now, you are probably a better lawyer than I am——

Mr. HOLLISTER. I doubt it.

Mr. O'CONNOR. This is very important, Mr. Congressman. Of course, as lawyers, we both agree that any individual charged with notice of the law, that he is bound by it, so far as it affects his rights.

You have raised the question that, if he continues during that period with the same contractual relation that he had with the bank as to those amounts, it is doubtful if the bank could abrogate that contract. There is no doubt about a new contract, as the Congressman has suggested. In view of the law, there would be no question about relieving them.

Mr. HOLLISTER. Would it not be a very simple matter with respect to that, because the bank coud really notify all of its depostors to that effect, or to the effect that, on such and such a date, the law would come into effect, and that any depositor will have a right to withdraw his deposit? It will be assumed that, if a depositor does not withdraw his deposits, that he will consent to making that new deposit on that date, and thus change the contractual reationship between the depositor and the bank.

Mr. O'CONNOR. I think, Mr. Hollister, you are absoutely correct.

Mr. HOLLISTER. It seems to me that woud be a perfectly easy way of obviating constitutional questions which might otherwise arise.

Mr. O'CONNOR. In other words, this contractual relationship you talk about can be terminated by either party, because the bank has the right to say to a depositor, "We don't want your money."

Mr. HOLLISTER. A depositor has no vested right in making a deposit, and if a bank cares to notify a depositor that, at a certain date, the relationship between them will be changed, giving him plenty of time to withdraw, it seems to me you are more than liberal in 2 years. You can make it 6 months, and if a bank wanted to notify all of its depositors and give them plenty of time to withdraw their savings as well as demand deposits, that constitutional difficulty will be obviated.

Mr. O'CONNOR. I am inclined to agree with you.

The CHAIRMAN. I was going to propound that very inquiry.

Mr. O'CONNOR. You are too late.

The CHAIRMAN. That is just what I was going to ask.

Mr. O'CONNOR. You are too late.

The CHAIRMAN. What would be the difference between terminating your liability at the end of 60 days, or at the end of 2 years or more? The principle would be the same, of course. Under the amendment, you are going to terminate those obligations arbitrarily, or by one party to the transaction, and if you are, you could do it just as well at the end of 60 days, if you met the same requirements.

Mr. O'CONNOR. Mr. Congressman, may I make this rather broad and rather challenging comment on why this should not be done at the present time, in my judgment? You may not follow it, at all, but looking at the picture now and not from a local angle but from a national angle, I have given to this committee the work of the Government in strengthening the capital structure of these banks. We have gotten them all in very good condition today. I am inclined to believe that we were able to do this job a good deal because of the double liability that was on the shareholders.

Now, let me make that very particular: Here is a bank that has an impairment of its capital, and the Comptroller says, "You have got to repair that capital and put up $100,000, or $1,000,000", and if there is no double liability, those directors and shareholders are not as interested in repairing that capital and working out the problems of that bank as if there was no double liability, because they are just apt to say, "Take it; it is yours", and walk out of the picture.

Now, while we are working out this problem, it is their problem as well as ours, and the Government has gone a long way with these banks in strengthening the capital structure of them, in getting local contributions, so that ultimately they will be owned in the communities; and when they realize the fact that, if we close them, they will pay one hundred cents on the dollar of the liabilities, they are going to hesitate a long time before they will permit that to be done.

Therefore, I believe that, until we get it worked out further, that that is the controlling influence in saving a great deal of the banking situation of this country, and that is why I would not like to see it interfered with.

The CHAIRMAN. Mr. Comptroller, there is a great deal of force in what you say, and I think I can appreciate it. The fact is, if I may take time to say so, that I am not so enthusiastic about the change in the law as I was at one time, because my attitude grew out of the deep sympathy that I felt for so many innocent stockholders, many of them citizens who, out of public spirit and for the promotion of the community, had purchased stock in banks that were under the control of others, with no part in the management, themselves, and who had suffered finally by the imposition of the double liability; and as you suggested a little while ago, many instances have occurred of widows and children who found themselves in the attitude of having inherited a serious liability, rather than an asset. Those conditions were accentuated a year or two ago.

But let me ask you this, in connection with your statement a few moments ago: Is is not true that great difficulty was encountered, in many instances, in reorganizing banks that had been temporarily closed, because of the dread of the investors putting their money in institutions where they incurred liability of reassessment equal to their original investment? Would that not, in many instances, interfere with the reorganization of banks?

Mr. O'CONNOR. No; because that was the reason for passing the law limiting double liability in new banks.

The CHAIRMAN. I am not talking about that; I am talking about old institutions, who had a chance to replenish their capital and go forward under the same ownership or organization and——

Mr. REILLY. The new stock issued has no double liability?

The CHAIRMAN. That is true.

Mr. O'CONNOR. It was all new stock, because it wiped out the other stock.

The CHAIRMAN. You had many cases of this kind, where stockholders would come to the rescue of a weakening institution, by putting in new investments, and all that sort of thing, did you not?

Mr. O'CONNOR. They took new stock, which was not subject to the liability.

The CHAIRMAN. They could take the existing stock, as well as the new stock——

Mr. O'CONNOR. You mean to issue new stock?

The CHAIRMAN. No; strengthen the existing stock was what I referred to.

Mr. O'CONNOR. Yes; they have done that, Mr. Chairman, but not in a great many cases.

The CHAIRMAN. Let me ask you one other question: I believe you suggested that stock in an existing institution is to be relieved of double liability—that when it is to be relieved of double liability, it shall be a requirement that a surplus should be built up equal to the amount of capital. Would you apply that to a newly organized institution?

Mr. O'CONNOR. Absolutely. There is no reason why they should be exempted from it. We would, under the terms of the bill, require 20 percent to start and gradually build up to 100 percent.

The CHAIRMAN. I was wondering, if they did not, why not. They would be, of course, better protected, and it may be better business—I would not say it would not—than the old plan of putting up one-half and being liable for the other.

Mr. O'CONNOR. That is better. Mr. Congressman, can I make one more comment?

The CHAIRMAN. Certainly, go ahead.

Mr. O'CONNOR. Do you not see how much it is going to also assist the Federal Deposit Insurance Corporation, of course, if we can keep that system strengthened and——

The CHAIRMAN. It would, of course, make for a sounder system. I think anybody can appreciate the contention that a bank should not be permitted to pay out dividends to the point of weakening its position.

Mr. REILLY. Mr. O'Connor, with the exception of the interest that the Federal Deposit Insurance Corporation would have in the subject, and the interest of the depositors above the insurance liability, is not that academic, as far as the great mass of depositors are concerned—that you are going to get this money, whether you get it from the stockholders or from the insurance corporation? So, relatively speaking, they are only a small fraction of the depositors in our banks today, and only about 2 or 3 percent of them having any financial interest in the question of whether or not that double liability will be wiped out or left in, they are going to be paid just the same, are they not?

Mr. O'CONNOR. You are absolutely right, Mr. Congressman, keeping in mind the distinction between depositors and deposits in a national bank, and that 42 percent of the deposits are insured under $5,000.

Mr. REILLY. The great majority?

Mr. O'CONNOR. Yes.

Mr. REILLY. You would really think that the Insurance Deposit Corporation—if all of the depositors in a bank which was above the insured limitation, would sign a request that the liability be wiped out, there would be no reason why it should not and could not be wiped out or eliminated?

Mr. FORD. Might I make a suggestion?

The CHAIRMAN. Yes.

Mr. FORD. Would it not be wise to have it printed on the bank pass book, that on and after such and such a date there was no double liability on the part of the stockholders, and give every depositor ample notice, and print it in the part of the rules in that pass book? Why not, in a commercial bank, have it brought to the attention of the depositor, by being printed on his pass book?

Mr. O'CONNOR. I think, Mr. Congressman, that is a very sound suggestion. Mr. Hollister has the same suggestion, without being specific. Mr. Hollister suggested that that would eliminate the constitutional objection, by notification to the depositor, and you suggest a specific method, and that method by you brings the direct knowledge to the depositor, and he would not be injured, because I think we have all agreed that it is a contractual relationship that can be terminated and there is no injury done, because that depositor can do as he likes.

The CHAIRMAN. I am not sure—I do not mean to put my judgment in the matter against that of lawyers competent to pass on it; but I am not sure that any party to a contract can abrogate it merely by notifying the other party that he is not going to live up to it.

Mr. O'CONNOR. Can I answer that, Mr. Congressman?

The CHAIRMAN. Yes.

Mr. O'CONNOR. You can, if it is a contract that can be terminated by either party on notice, and that is what this kind of contract is.

The CHAIRMAN. All right, Mr. Cross.

Mr. CROSS. I want to make this suggestion, or ask him a question: Two methods have been suggested by which that could be done, that contractual relationship could be terminated, but if you notified all of the stockholders—I am speaking now from the psychological standpoint and expediency—that, at a certain date, the double liability of the stockholders will end, or if you put in the pass book that notice, would not that have a tendency to frighten the average citizen, because he does not know anything about that? He would say that the bank is in bad shape, or it is weakening. But you could put that in the law and nobody would know anything about it, and that would settle the whole thing, and it would go along smoothly, without any difficulty at all.

Mr. O'CONNOR. Mr. Congressman, I do not think it is possible to frighten depositors today, with Federal Deposit Insurance Corporation.

Mr. CROSS. Well, some of them have more than $5,000 in the bank.

Mr. O'CONNOR. Well, we just covered the point of the amount which is involved. In the national banks, we have got 98 percent of the number, so that the people that have the large deposits—I think they probably are in a better position to know.

Mr. CROSS. A little more intelligent than the other fellow would be?

Mr. SISSON. Mr. O'Connor, I would like to get this information, if you have it at hand.

Mr. O'CONNOR. Yes, Mr. Sisson.

Mr. SISSON. When you proceed to collect double liability, and in case that you have to go to court, what is the percentage that you collect, what do you get out of it, after it is all done?

Mr. O'CONNOR. I can give you that very accurately, as it is in the annual report. It is 49.78, and that is for a period of 70 years, Mr. Congressman.

Mr. SISSON. There is one other thing about this: I suppose your department had no other resource but to proceed to collect?

Mr. O'CONNOR. No.

Mr. SISSON. But it is a terrible thing to happen to a community, to have to do that. It is just too bad that a situation of that kind has to come up, where the whole community interest may be destroyed. You are very familiar with what I have in mind. I am thinking of a city in my own district right now.

Now, what I am particulary interested in is this: If this H. R. 5357 becomes the law, what is it going to do with the State banking system?

Mr. O'CONNOR. If what, Mr. Congressman?

Mr. SISSON. If this bill which we have under consideration right now, H. R. 5357, becomes law, what is going to happen to the State banking situation?

Mr. O'CONNOR. You are asking a question on this title?

Mr. SISSON. We practically forced the State banks into the Federal Reserve System, or do it in the next 2 years, and I want to know what we are going to do for those State banks, to make it easy for them to get in; or how many of these banks are we going to put out of business?

Mr. O'CONNOR. I can only answer that in a general way: I have taken this position, and it is also one of the recommendations in my annual report, that we ask the Congress to liberalize the assets that are in these State banks, what we call under here "nonconforming assets", so as to permit State banks to more easily become members of the Federal Reserve System. In other words, if we are going to compel the State banks to do something, we have got to be careful that we do not do an injustice to those institutions; and if a certain institution has got sound assets that are not conforming, I feel that the Congress should give the Comptroller permission to permit those banks to qualify, or permit them to come into the Federal Reserve System, and permit the Federal Reserve System to accept them, which it could not do today under the existing laws, because of the assets being as we say, "nonconforming." I believe with you, Mr. Congressman, if we compel then—if we compel that to be done, we have got to be exceedingly liberal in permitting State banks—nobody wants a bank that is not sound, but we have got to be liberal in permitting them to join. When you, by an act, compel them to do that, you have got to be careful that you do not do them a great injustice.

Mr. SISSON. Do you think that could be written into the law, do you think that would be possible?

Mr. O'CONNOR. You have got to write—you would have to change the law, because you have fixed certain standards of membership, and they must have what we call "conforming" assets. You would have to change that, and we will be very glad, at the proper time, to go in and analyze that section with you, and check up on it.

Mr. WOLCOTT. May I suggest that the Federal Reserve System waive, in whole or in part, the capital requirements of nonmember banks, as an inducement to get them in; and if that were true, I assume the Board would be liberal in its interpretation of the law and liberal in its requirements.

The CHAIRMAN. Mr. O'Connor, have you any further matter that you would like to discuss relating to title I? If you have, I would suggest that you do so, because we will be glad to hear you, and then will resume our questions.

Mr. O'CONNOR. Well, I have given my general approval, Mr. Chairman, to this bill. I feel that it has been very carefully worked out, and I think that the fundamental parts of it are very important in looking forward to the successful operations of the Federal Deposit Insurance Corporation.

This bill has been passed by the Banking Committee of the Treasury, and I want to say that I think it is in very excellent shape. I did tell the committee that one provision of it I thought was not just in harmony with my ideas, but the committee thought otherwise. That is with reference to receiverships.

I feel that the present system should be continued. The Comptroller should appoint the receivers of all national banks, particularly based on the record of the office of 70 years, without any reference to myself, because I think we have done a good job in years past, and I hope in the present, when we have returned, out of every dollar collected, 93 cents to the depositors, and we have only taken 7 cents out of any dollar for expenses of salaries of the receivers, and attorneys' fees and rent, and every other item that you can possibly conceive of, which has been included in the 7 cents, and we have returned 93 cents to the depositors.

I doubt the wisdom of setting up two insolvent divisions in Washington. The Comptroller's Office has handled nearly fifteen hundred and I believe that, particularly in view of the fact that only 42 percent of the deposits in national banks are protected by the Insurance Corporation—still, the Comptroller is responsible for the administration properly of the balance of nearly 60 percent and——

Mr. HOLLISTER. Fourteen hundred since the office was established?

Mr. O'CONNOR. Yes. It would probably be just as well for it to continue without duplication. I am very much opposed to the use of duplication in Government or private business.

I wanted to make that clear, and then say that the bill before you has the endorsement of the committee and I have their comments on it.

There is one other section of the bill that I, frankly, have not discussed with anybody, because I just ran across it yesterday, but I believe——

The CHAIRMAN. Before you leave that, Mr. Comptroller, it might be well to call attention to the fact that, under the existing law and under the original Deposit Insurance Corporation law, the Deposit Insurance Corporation could take over any national bank that was closed and operate it as a clearing house for a period of 2 years; meanwhile giving an opportunity for the reorganizing, or for the organizing of a national bank.

The thought back of that was not so much to secure the wise administration of the assets of the closed banks, but to permit the corporation to continue to operate the bank, and to avoid paying the actual cash to the depositors, by being authorized to issue new deposit receipts by the new institution operated by the Deposit Insurance Corporation.

Mr. O'CONNOR. When banks fail because of lack of business, I think it is unwise to attempt to establish another bank on the ashes of the old.

Only one national bank went into receivership in 1934, and it was in Montana, with a deposit liability of approximately $30,000. For several years there were no rains and the surrounding country, the country surrounding it practically dried up, as illustrated by the fact that it only had $30,000 in deposits. The community just could not sustain another bank.

The CHAIRMAN. Then you think it would be uneconomical and unwise to require the Deposit Insurance Corporation to continue to operate a bank, even in a limited way, in that community?

Mr. O'CONNOR. Absolutely.

The CHAIRMAN. But any such institution should at once be placed in liquidation?

Mr. O'CONNOR. Yes. Now, we have a right whereby we may, under this law, establish a national bank, but we do not do it, because I am so anxious to avoid establishing banks which will only result in distress to investors and depositors in the community.

Now, so far this year, we have had only one and——

The CHAIRMAN. In the instance to which you have referred, or to the particular case to which you have referred, that was not a case where there would have been a national bank organized, or would have been required to operate the bank for 2 years, but there would have been no likelihood of reorganizing it?

Mr. O'CONNOR. That is correct. Now, Mr. Chairman, following that out, we only had one national bank fail this year, and they did not fail because of the lack of business or of the lack of necessity for a bank in the community. I would rather not give the State, because that is not necessary, but it was due, unfortunately, to the fact that one of the officers had embezzled some $70,000, and who later confessed the embezzlement. That is something that cannot be avoided. There is need for a bank there and we have set up a bank and made excellent progress, or are making excellent progress in the sale of the old bank to the new bank and the sale of the stock to the people of that community, because they must have banking facilities there, and that gives them the option to do it.

Those are the only two, Mr. Chairman, in the national banking system last year and this year that failed.

The CHAIRMAN. So that, as a matter of fact, you have had, last year and this year, only two national bank failures?

Mr. O'CONNOR. That is right.

The CHAIRMAN. The insurance of deposits under the temporary plan of $2,500, and under the $5,000 limitation provided in the act last year, was not very harmful to the national banking system in this country, was it?

Mr. O'CONNOR. I think it is one of the things that has reestablished confidence all over the country, Mr. Chairman, and I think it is one of the justifications for the contribution on the part of the large banks to sustain the banking system of the country, because when the banks started to crack up, outside of New York, they immediately drew out the reserves from the large centers, and the large banks immediately drew upon the market stocks, in order to meet the cash withdrawals, and we thereby started a vicious cycle of depression; and if we can secure or reestablish the confidence of the depositors of the country, so that will not happen, we have saved the banking situation. The big banks that suffered by that did not close, but they suffered in those trades, and they should be willing to go a long way to prevent that again.

The CHAIRMAN. The fact is that a good many big banks actually closed before the holiday?

Mr. O'CONNOR. I am talking about the big centers, where the big cash reserves are kept, like New York and the other centers; but some very large ones did close, Mr. Chairman, which started the withdrawals from these centers, which, in turn, shut the banks. I am talking about the effects on the good banks, how they suffered, even though they said, "You can't close it"; but they suffered just the same, and the whole country suffered by the throwing of hundreds of millions of dollars worth of securities on the market, in order to realize cash to take care of their customers in the country.

Mr. GIFFORD. Mr. O'Connor, I want to ask a question. I think you have made a very good report here relating to the examination of your banks, but as I recall, even the White House, itself, issued a warning last fall that the bank examiners were still rather too strict, and that they could not expect money to be loaned as long as the banks were worried about collecting their slow loans and liquidating their loans.

I remember your speeches over the country, and I think perhaps you may recall that I may have written you a letter regarding your own viewpoint, and you seem to agree, in those addresses, that the banks should loosen up.

But in my section, whenever I visited the banks, and I visited a great many, there existed a fear of your examiners, especially relating to slow loans. Now, you are claiming in your report that you gave your examiners no instructions relating to the demanding payment of the slow loans, but simply marked them "slow." That, naturally, was effective on the banks and the people who owned that money, by marking them "slow loans." As I think the White House expressed it, there were two branches of the Government, the Reconstruction Finance Corporation and yourself arguing with the banks that they should loosen up, and another branch, which is the examination branch, frightening the banks so they did not dare make loans.

If I may pursue that, I realize that most of the banks—the chief thing they had in mind was to reduce the slow loans, and they did not want to get into any more trouble. You acknowledge in your report, if you are not quite ready to answer——

Mr. O'CONNOR. Yes, I am.

Mr. GIFFORD. You say here that there has been considerable controversy and misunderstanding with reference to the examination of banks; that they may have been harassed by the Reconstruction Finance Corporation's examinations, by the Federal Deposit Insurance examinations, though you examine but twice a year, but, while they were only supervisory examinations, they probably did intimidate and perhaps harass some banks by so many of these examinations.

Mr. O'CONNOR. First, Mr. Gifford——

Mr. GIFFORD. Comment on that, please, on the slow loans.

Mr. O'CONNOR. There is no harassment of banks by several examinations. No national-bank officer in the United States, at no time and at no place, has made criticism of a duplication of examinations, because no such thing exists. The only man who has authority to step into a national bank to examine it is an examiner from the Comptroller's office, and you have provided by law that we must make at least two examinations a year. No other examiner from the Federal Government ever goes into a national bank, with one exception: When a national bank asks the Reconstruction Finance Corporation to become a partner—because that is what they are when they buy preferred stock in a bank—when they ask the R. F. C. to become a partner, the banker and the Reconstruction Finance Corporation sit down and agree on how the deal shall be made, and in that deal the R. F. C. and the bank may agree that a R. F. C. man may come in at a certain time and look over their assets or check up certain matters, which is a matter entirely between the bank and the R. F. C. The bank does not have to do that, or the bank may yield to it, just in the deal between themselves.

The bank has a right to ask that an independent auditing firm make audits—and many of them do that—aside from our examinations. Many of the larger and better banks have independent audits made by some of the large auditing firms to be sure that they have completely checked up on that bank. That disposes of the point of harassment of different examinations.

Now, I want to direct myself to the instructions that were sent out in October 1933 to the national-bank examiners, and then I want to show you the results that followed those instructions.

Mr. SISSON. May I suggest, Mr. O'Connor, that you give Mr. Gifford the figures as to the way you have classified the loans which were placed in the loss column and the loans which were placed in the doubtful column?

Mr. GIFFORD. I have read that, Mr. Sisson. There are very few in the loss column. That is why I limited my question to the slow loans.

Mr. O'CONNOR. I was coming to it, Mr. Gifford, but I have to lay the foundation to get the figures, if I might be permitted to do that.

Mr. GIFFORD. Yes; but I wanted to tell Mr. Sisson that I understand those figures, but I limited it to the slow loans.

Mr. HOLLISTER. Might I ask a question, Mr. Chairman?

The CHAIRMAN. Yes.

Mr. HOLLISTER. Mr. O'Connor, to go back, temporarily, to that question of the taking of debentures in place of preferred stock, is it not true that, in a great many cases, debentures were taken by the Reconstruction Finance Corporation rather than preferred stock in some States, because the laws of the State did not permit the issuing of preferred stock, but also because, in some States where the preferred stock might have been issued, it would have covered double liability and the Reconstruction Finance Corporation did not want to take stock that carried double liability?

Mr. O'CONNOR. Yes; I think that is true.

Mr. HOLLISTER. To show you what I am leading to, whether you take preferred stock or notes or debentures of banks, it is exactly the same, and it was merely to get additional capital?

Mr. O'CONNOR. Yes.

Mr. HOLLISTER. That brings me to the question I am going to ask you, not that it has anything particularly to do with this bill, but I believe it ought to be brought out, and this is a good opportunity: Is it not true that, at the present time, for income-tax purposes, a bank which has notes and debentures outstanding, may deduct the obligation of paying interest on those notes or debentures from its income, and thereby pay less income tax; whereas a bank that has preferred stock outstanding is not so permitted to deduct it, but the amount which is ultimately paid out upon preferred stock must be paid by the bank for income tax purposes; is that not the case?

Mr. O'CONNOR. You are absolutely correct, Mr. Congressman.

Mr. HOLLISTER. So, would it not be proper to have—I realize you have come from the Ways and Means Committee—would it not be proper to have some sort of legislation passed, which would permit the deduction by the bank of what it has to pay out, the same way that the other banks that have debentures outstanding may deduct the interest on those debentures?

Mr. O'CONNOR. On page 7 of my report to Congress, I make this statement:

> Section 23 of the Revenue Act of 1934, paragraph (b), provides for certain deductions from gross income. It is understood that State banks which have sold capital notes or debentures to the Reconstruction Finance Corporation may under this paragraph deduct interest paid thereon in computing their net income for taxable purposes.
>
> National banks in strengthening their capital structure have issued preferred stock to the Reconstruction Finance Corporation, paying dividends thereon, which payment of dividends is substantially equivalent to the payment of interest made by State banks on capital notes sold by them to the Reconstruction Finance Corporation.

You used my language.

Mr. HOLLISTER. I knew that was in the report, but I thought it well to bring it out. Can you tell the committee whether your office is suggesting to the Ways and Means Committee that they take up that matter?

Mr. O'CONNOR. Yes, we have submitted it.

The CHAIRMAN. Mr. O'Connor, let me suggest that you conclude your discussion of the matter of examinations.

Mr. O'CONNOR. Oh, yes; thank you.

The CHAIRMAN. As I understand, you had not finished.

Mr. SISSON. Mr. Chairman, may I interrupt?

The CHAIRMAN. Yes.

Mr. SISSON. Mr. O'Connor, you spoke, a short time ago, about the fact that—or you mentioned the fact that 97.5 percent, I believe, of the total number of deposits were—I assume you were referring then to the member banks, or just to the national banks?

Mr. O'CONNOR. National banks.

Mr. SISSON. Were covered by deposit insurance. I am not sure whether Mr. Crowley testified—he testified yesterday quite fully on that, but I am not sure whether he gave the aggregate amount, in dollars, of the deposits that were covered. If you have that conveniently, I think it might be well to have that in the record at this point.

Mr. O'CONNOR. National banks, 5,450, insured deposits, $8,488,-554,000, uninsured deposits, $11,583,949,000, and total deposits, at this time, or on October 1, were $20,072,503,000, which shows that 42.29 percent of the deposits are insured by the Federal Deposit Insurance Corporation, insuring $25,972,035,000 deposits, and 405,811 deposits are partly insured, which makes a total of 26,377,846 depositors, and 98.46 percent of the depositors are insured; and in State banks, which are members of the Federal Reserve, we have 969 banks, with insured deposits of $3,582,449,000, and uninsured $7,382,986,000, making a total of $10,965,435,000, which shows that 32.67 percent of the total deposits are insured, with 9,361,278 depositors, and 119,082 partly insured, with a total number of depositors of 9,560,360, and the percentage of depositors insured is 97.92 percent; and State banks, which are not members of the Federal Reserve, exclusive of the mutual savings banks, number 7,638, with insured deposits of $3,580,803,000; uninsured deposits of $1,363,262,000, and total deposits of $4,944,-065,000; and the ratio of insured to the total deposits is 72.43 percent; and the depositors fully insured are 13,687,403; and depositors partly insured, 142,947, making a total number of depositors of 13,812,350, or 99.10 percent of the number of depositors in State banks are insured.

The CHAIRMAN. As State nonmember banks?

Mr. O'CONNOR. Yes; that gives us a total there which is rather interesting in these three divisions: 14,057 banks with insured deposits of $15,651,806,000; uninsured, $20,330,197,000, with total deposits of $35,982,003,000, with the ratio of insured to total deposits of 43.50 percent; and depositors fully insured, 49,020,716; depositors partly insured, 729,840; and total number of depositors, 49,750,556; and the total number of depositors insured in the three classes, under the $5,000, is 98.53 percent.

Mr. SISSON. That gives the complete picture there.

Now, may I say, in a preliminary way to one question that I want to ask, and I am not indicating any opinion that I have, because I do not know whether I have any positive conviction about the advisability of increasing the maximum of insurance deposits, but I just wanted to ask you, before you pass from it, if you are going to discuss it at some later date before the committee, that is, as to your opinion of the advisability of increasing the maximum limit of deposits, insured deposits? If you do, I do not care to ask you to go into it now, because that is perhaps breaking up the continuity of your statement.

Mr. O'CONNOR. Well, Mr. Sisson, I feel that we have presented all of the statistics and figures, and the amount is a matter that ought to be a matter of policy of this committee.

Mr. SISSON. Yes, sir; but guiding the committee, unless the majority of the committee have decided already that there will be no increase, the committee probably before voting upon or deciding upon it, would like your opinion.

Mr. O'CONNOR. Then, may I put it this way?

Mr. SISSON. I am not asking you to give it now.

Mr. O'CONNOR. If the committee agrees to it, or gets to that point, I will be very glad to give you my opinion.

The CHAIRMAN. Mr. O'Connor, have you given any thought in that connection? I am asking this question: Have you given any thought to the difficulties that the banks will find themselves in, in relation to their obligations to other banks, when they fail;

what that picture would disclose, if we should have any considerable number of bank failures in the country?

Mr. O'CONNOR. Yes, we have thought a good deal about that, and it is pretty complicated.

The CHAIRMAN. I am wondering how much noise we will hear around here about the amount of deposit insurance after the banks gather some experience and they find they are not insured against one another. That thought is reconciling me somewhat to the idea of limiting this insurance, for the time being. I have the idea that the banks will take care of the matter of increases, as soon as they gather some experience, in case we have a large bank failure. I would like to be here when that happens.

Mr. GIFFORD. Mr. Chairman, do you want me to continue on the examination?

The CHAIRMAN. Gentlemen, if nobody objects, let me suggest that Mr. O'Connor conclude his discussion of this matter of examinations, if he desires to say anything further.

Mr. O'CONNOR. I started, several times, and there is just two pages, and as a foundation, I would like very much to put this in the record and be subject to any questions.

The CHAIRMAN. There will be no objection to your incorporating that in the record. You may do so right now, and if you desire to say anything further, we will be glad to hear you.

(Here followed discussion off the record.)

Mr. O'CONNOR. Mr. Chairman, I would rather that speech would stand, because it is so knit together.

The CHAIRMAN. We will be glad to have it.

Mr. O'CONNOR. But at this time I would like very much to call the committee's attention, for the purpose of laying the foundation for future questions on a very important matter that the country has been greatly interested in, and which has been considerably misrepresented until this was given to the country, and I would be glad to give some reactions that I got after this speech was made by depositors as well as bankers and others.

The Comptroller of the Currency sent, on October 26, 1933, to each of the 12 chief national-bank examiners in the United States instructions to this effect:

"After the 'Bank Holiday', national-bank examiners were largely engaged in the examination of banks which did not receive a license for the purpose of reorganization. It appears that some examiners in making examinations of licensed national banks have become what might be termed 'Reorganization Minded' and have lost sight of the President's recovery program and its relation to licensed banks. It is the administration's desire that credit channels be opened through licensed banks, and this policy cannot be accomplished if examiners follow a deflation policy in examinations. We are all concerned in having solvent banks, but there is a wide distinction between the potential and intrinsic value of assets of a going institution, and liquidating values. Examiners in appraising and classifying assets of licensed banks will not apply liquidating values but will appraise on the basis of fair values on a recovery basis.

"As an example—in dealing with bank buildings, the examiner must realize that a bank building of a going bank has an intrinsic value, as distinguished from present depressed values, which, combined with the element of recovery, may fully substantiate the carrying value given to it by the bank. The same is true of mortgages, and in this connection the examiners should familiarize themselves with the instructions given with respect to real-estate mortgages by the Federal Deposit Insurance Corporation to its examiners.

"You will advise examiners who are examining licensed banks of this policy and see that it is carried out. Any examination now in process, or any future examination, will be governed by these instructions and where an examination has been completed, the examiner making the report will review the report on the above basis and rewrite such report if found necessary. If the examiner is not now available it may be necessary to make a new examination on the proper basis."

Again on March 13, 1934, the following instruction was sent to all chief national-bank examiners:

"Reports of examinations received by this office recently clearly indicate that some few of the examiners throughout the country have not fully grasped the meaning of instructions communicated to the chief examiners under date of October 26, 1933, and are making more drastic classification of assets of the banks examined by them than is necessary under the circumstances and more severe than is contemplated by the instructions contained in office letter referred to above.

"If there are in your Federal Reserve district any examiners who, in your opinion, are making unnecessarily drastic classifications of assets, please confer with them promptly, looking towards having their classifications as lenience as circustances in each case will permit and in order that they will be in accord with the policies of this office.

"While you are familiar with the character of examinations made by your examiners, it is suggested that in determining whether or not any of them are too severe in their classifications, you give particular attention to their appraisals of banking houses, furniture and fixtures, and loans secured by real estate."

No system is perfect because men are not perfect. Here and there isolated cases appear where examiners have been too harsh. These instances are sometimes called to the attention of the proper officials; but where examiners are too lenient, that fact seldom appears. The instructions which I have cited have never before been made public. However, I believe the time has come to clarify a criticism which is unfair. The question naturally arises—what were the results obtained under the instructions? Again, for the first time, I will give you a complete picture of the examinations made by the national bank examiners as shown by 1934 reports of examination. As is well known to bankers, examiners classify loans under three headings—slow, doubtful, and loss. There is little room for argument when assets are placed in the loss column and very little question arises in the doubtful column. The slow column attracts the most attention and controversy. An examination of the reports filed with the Office of the Comptroller of the Currency in each of 5,275 banks reveals the following interesting figures: The total amount of loans was $7,740,596,000. The examiners placed 2.88 percent of these loans in the loss column and 4.19 percent in the doubtful column and 27.05 percent in the slow column. The country has been advised of the definition of slow paper as follows:

"The examiners when classifying loans as slow should state briefly the reasons for such classifications, but should bear in mind that the responsibility for determining and taking such action as may be necessary to place such slow loans in proper bankable shape rests entirely with the bankers. The examiners therefore, should refrain from instructing the bankers as to what course they should pursue with their customers whose paper is classified as slow."

Now, I want to answer specifically, Mr. Congressman, the question you raised with reference to the reaction to the slow column or classification. My general experience is that bank directors, aside now from the operating officials of banks, are very anxious that we retain in our reports these slow columns. The purpose of that is to direct the attention of the directors to what our examiners find in the banks, so that a bank will not gradually find itself in a very frozen condition.

We merely point out certain paper to be slow; it is good, it is sound or it would not be in that column; and by specific directions, we say to our examiners, "You shall not tell that banker what he shall do with that paper." Now, we say, "You are to make comments to us." Everyone will agree that a bank should not have an undue amount of slow paper, and without giving places, which I trust you will not ask me for, because it is not necessary for the purpose of discussion, two most serious cases that arose in this country, and in one where the greatest distress was found because of the lack of dividends to depositors, was due to the fact that the bank became frozen with slow paper, which should not have happened.

Therefore, it seems to be the common opinion among directors, and in most instances now they are much more careful than they were before, and they asked to have read and in the directors' minutes, and our reports are read to them, and they are generally discussed, and if they find the amount of the slow paper the directors themselves can make inquiry of the officer as to that particular paper, what it is, and make some investigation of it; and we find, Mr. Congressman, notwithstanding the fact that there has been some discussion as to the elimination of the slow classification, my judgment is it would be a serious thing to do.

Mr. GIFFORD. Mr. O'Connor, I think you fully understand why I am asking the question. The public at large is interested, because they thought there were two branches of the Government, one working against the other; and when I got your report as to the slow loans, I thought you did not even imply that putting them into that column meant that they ought to be paid.

Our bankers say, "We run our banks. We must pay 6 percent to get this paper renewed." They have an abundance of property or assets, and we have to harrass them. But those slow loans—I got notice from the banks that the examiners had criticized their loans, and when they put them in that column it was implied criticism, although not an implied order that they must be collected.

Mr. O'CONNOR. The banker who said that was dishonest. The banker who made that statement was dishonest with the borrower, unless he accompanied it with the instructions that we sent to the banker and to the examiners.

Mr. GIFFORD. If the banker had told you it was put into the slow column and is must be made an active account, something must be paid on it, what would you thing about it? Of course, I could bring up specific instances now, but I just do not want to. I could give you several that I am sure you would agree to, I think, from your letters to me, which I believe show your viewpoint.

Mr. O'CONNOR. Yes, I know. I appreciate that very much.

Mr. GIFFORD. You acknowledge, yourself, your second letter to your examiners, that in matters of real estate, they have been too strict. Of course, there had been many cases where they were marked off as a complete loss, certain real estate loans, that might later prove of some value; and in many cases, the bank claimed the loss, so they had to go to the R. F. C.

All of my questioning is specifically founded upon the fact, in this article, or in this title I, you ask the banks to furnish burglar insurance, and a whole lot of things, and that they be subject to further examination. If the examinations have been an irritating factor to a sufficient degree, to have caused the banks, in the last 2 years to be unwilling to loan money, and that has been their chief——

Mr. O'CONNOR. Alibi?

Mr. GIFFORD. You agree with that?

Mr. O'CONNOR. An alibi?

Mr. GIFFORD. Yes; call it an alibi, if you wish.

Mr. O'CONNOR. Which is not true.

Mr. GIFFORD. I doubt if it is true, myself, but we have been faced with it by men who wanted to borrow money and——

Mr. SISSON. Mr. Chairman, if the committee will pardon a personal allusion, I used to manage a baseball team and I fully realize how an alibi can be used, because when a player, when he missed a ball, he said that the field was uneven and the ball did not bounce right. I think the most interesting alibi the bankers have had is, that they have laid the blame upon the Comptroller's examinations.

That is what I have been trying to bring out before this committee.

The CHAIRMAN. The truth is, that the Comptroller's Office, for several years, has been criticized because of its liberality, and it risked a great deal in going as far as it did in liberalizing the policy of examinations, to try to deal constructively with the difficulties we have had in the past years, and I commend you and your predecessors for what you have done, and I believe the people who understand it feel the same way.

Mr. GIFFORD. Mr. Chairman, I am trying to bring out the facts that the banks have not loaned money the last 2 years, call it alibi or anything else you like; they have not done it, and there has been no reason for it.

The CHAIRMAN. When you call it alibi, I agree with you.

Mr. GIFFORD. I am allowing that word to go in, but some definite reason has been back of it for 2 years.

The CHAIRMAN. They are scared to death.

Gentlemen, let me ask if there are any other questions from Mr. O'Connor; and if there are not, I am going to suggest we excuse him and conclude with his statement on title I, and the committee will not meet again until Monday.

Mr. WOLCOTT. Just a moment, please, let me ask you a question: The Federal Reserve System, I am given to understand, have about $2,400,000,000 of excess reserves. What is your opinion, Mr. O'Connor, as to why that money has not been loaned?

Mr. O'CONNOR. Well, Mr. Congressman, a rather careful analysis was made of that in Dr. Viner's report, which he made sometime ago, a few weeks ago, or probably a month ago, and he sent some very efficient men, I believe, and compared very carefully the reasons—now, I am just giving you what I think about it, not having anything to do with it, but I believe that he sent men to follow through the loans of the banks that were rejected and get an analysis of why the people were not borrowing and why the loans were rejected, and I believe the Doctor concluded that there was not such a demand for loans. He concluded that the demand was not there for legitimate loans that the people thought.

Now, I am just stating that, because I read the report very briefly and hurriedly, but the report is available and that was his conclusion, and I think that the report—I would rather refer to it and refresh my memory about it than to give you an offhand opinion, without any facts.

Mr. WOLCOTT. That would seem to be true, in view of the fact that the Reconstruction Finance Corporation, I understand, has had demands made upon them for only about $100,000,000 of the money we made available for loans to small industries, and have paid out actually less than $7,000,000.

Mr. O'CONNOR. That is right.

Mr. WOLCOTT. What I am getting at is an expression of my own personal feeling in that connection, that undoubtedly the lack of demand on the part of borrowers is due to the uncertainty of the economic future of the country; and possibly we might be able to overcome that by maintaining—by establishing and maintaining definite policies concerning our money and our attitude towards business. Do you not think that might help some?

Mr. O'CONNOR. As I say, that report, Mr. Congressman, is something new, and it is a particular question that I have not gone into, and I would have to refresh my memory; but he actually went into the field and made an investigation. The only way we can get at these things is by the actual facts, and whatever they are, let us have the facts. If it is a fact, let us look at it. Dr. Viner did send his men out, made a very careful analysis, and got reports back of a number of applications and why they were rejected and the amount of them, and he follows great detail in it and made his conclusion in that report; and I would like awfully well to refer you to that report.

Mr. WOLCOTT. Yes; I will read it with a great deal of interest. I assume, from your statement, that he came to the conclusion it is due to a lack of demand for the money?

Mr. O'CONNOR. I think that is one of his conclusions. Well, put it in another way, I think my impression from the report was, that there was not as great demand as some people believed.

Mr. WOLCOTT. Following that through, the panacea for all of this seems to be to create a condition of confidence, in which business will get started to borrowing money from the banks and demanding money from the banks for constructive purposes. I will not expect you to answer that, Mr. O'Connor.

Mr. O'CONNOR. I do not know. I am only referring you to the only authentic report that I know of.

Mr. FORD. Could you not send copies of the report to the members of the committee?

Mr. O'CONNOR. It is a very voluminous report.

Mr. WOLCOTT. What is it, a very long report?

Mr. O'CONNOR. Yes, sir.

Mr. HOLLISTER. You have only to read about two pages of it, which is a summary of the thing.

The CHAIRMAN. Do you desire to say anything further right now?

Mr. O'CONNOR. Yes, there was one other section that I thought we ought to give some discussion to, and I want to briefly state that, in our banking law—and as I said, I had not given it consideration until yesterday, but I feel we should not go along without at least one comment on it, and that will conclude my troubles. On page 34, section 18, the bill provides, in title I, the following:

The board of directors, from time to time, shall gather information and data and shall make investigations and reports upon the organization, operation, closing, reopening, reorganization, and consolidation of banks, banking practices and management, and the security of depositors and adequacy of service to borrowers. The board of directors, in any annual or special report to Congress, shall report its findings and make such recommendations and requests as it shall find necessary and appropriate for the purpose of carrying out the purposes of this section and fully provided for all of the obligations of the corporation.

I find some objection, Mr. Chairman, I am sorry to say, to this section, because the Comptroller of the Currency makes a report to Congress, the Federal Reserve Board makes a report to Congress, and this is mandatory upon the Board, and I do not think that we can justify an expense of as much as $50,000 or $100,000 to get that additional information, which is now available through the Federal Reserve and the Comptroller of the Currency, all of which is worked in connection with our board, and I do not believe that section is necessary and I think it would be a useless expenditure of money.

The CHAIRMAN. Mr. O'Connor, before you conclude, there is one matter I would like to draw your attention to for a brief discussion by you, and that is the provision respecting the payment of interest on deposits.

Mr. O'CONNOR. Have you special reference to the act which provides for the elimination of interest on demand deposits?

The CHAIRMAN. Yes.

Mr. O'CONNOR. Now, that is very important, Mr. Chairman, and I am glad you mentioned it. There has been a great deal of discussion about the assessment on banks for the purpose of the Federal Deposit Insurance Corporation. In the Glass-Steagall Act of 1933, you provided that no longer should banks pay interest on demand deposits. I believe that was one of the very serious matters in our banking structure, and I think was a wrong system of banking.

The little depositor never got anything, anyway, and it inured entirely to the benefit of the very large depositor, and it led to such competition between banks for the large banks in their rates of interest.

So you eliminated that by the act of 1933, and I called attention to what that sum amounted to in my address before the American Bankers in Chicago in September 1933, and discussed rather fully that and other provisions of the insurance corporation, and I would like to call attention to that particular point, Mr. Chairman, if you will permit me to put that address in the record.

The CHAIRMAN. We will be very glad to have you do so.

Mr. O'CONNOR. On page 6 of the printed address, I said:

The elimination of interest on demand deposits will save the banks many billions of dollars. The total amount paid during the past 5 years by member banks on demand deposits was $1,230,242,000, making an average of $246,-048,500 per annum.

And I believe out of the amount we collected from the banks upon the levies of assessments we made—we levied the assessment and they collected one-half of the levies—and I believe it was around $70,000, and here we have just the member banks, because we do not have available the figures on all banks, that the banks have paid out approximately $250,000,000 a year that you prevented them from paying out, is not considered by Congress as good banking. Now, I think that is rather a striking statement.

The CHAIRMAN. Well, if we were to leave the assessments against the member banks, which would amount to $250,000,000 annually to support the deposit insurance fund, we would not have added that burden upon the banks; is that a sound conclusion?

Mr. GIFFORD. What are you going to do with that amount of money?

Mr. HOLLISTER. That is the total?

The CHAIRMAN. Yes; that is the total.

Mr. REILLY. Mr. O'Connor, have you got any report upon any banks in recent years on the service charges that they did not charge some years ago?

Mr. O'CONNOR. No, sir; we have not.

Mr. REILLY. Can you get that report?

Mr. O'CONNOR. I am glad you asked that question, because we have had a great many letters, Mr. Congresman, asking about those matters, and we have no jurisdiction in the Comptroller's office to regulate or to fix in any way those charges. That is a matter entirely at the present with the banks themselves.

Mr. REILLY. Do they not report their income items?

Mr. O'CONNOR. Yes.

Mr. REILLY. Have you not got any idea what they collect for service charges?

Mr. O'CONNOR. Not a separate item, Mr. Congressman; no, not the separate items.

Mr. REILLY. Some of the banks are making some awful charges for handling accounts.

Mr. WOLCOTT. When they are prohibited from paying interest on demand deposits, that likewise carries with it the fact that those funds are more or less static and not being used by the banks for the purpose of making money, yet I do not find any restriction in the act which protects those depositors against their use for long-term investments. Do you not think that would be in keeping with the act, that they do not pay interest on them, but they collect a service charge for handling the accounts, that they maintain a little higher degree of liquidity with reference to demand deposits than they do with respect to time deposits and——

Mr. O'CONNOR. I think that is sound, Mr. Congressman.

Mr. WOLCOTT. In other words, it has been considered unsound banking to invest commercial funds in long-time paper, has it not?

Mr. FORD. Mr. Chairman——

The CHAIRMAN. Just a moment, until Mr. Wolcott gets through, please.

Mr. O'CONNOR. Would you read the Congressman's question?

(Thereupon the reporter read the pending question of Mr. Wolcott.)

Mr. WOLCOTT. Perhaps I should say it should be considered unsound banking to do that.

Mr. O'CONNOR. Yes, that is correct.

Mr. FORD. At the opening of this hearing, Mr. Crowley was in the chair, and I made this statement, and I think that this discussion verifies it, that as a matter of fact, the banks are not paying the insurance premium on the insuring of deposits, but the depositors were paying it, because they have been relieved of paying interest on time or demand deposits.

Mr. REILLY. Mr. Ford, those were the big depositors, not the great mass of depositors.

Mr. FORD. Well, big or little, that is the situation just the same.

Mr. SISSON. Mr. Chairman, if Mr. O'Connor is not coming back here for several days, I think perhaps it might be proper to have him state the witness to whom we may ask these questions, because there is a question I am rather ashamed to ask, but frankly, I have had, I think, four letters from bankers in my district, and they were men in charge, you might say, of the administration of the banks, but they were rather small banks, and I told them that, if they wished to I thought the chairman would give them permission to appear here, and they asked me to bring this to the attention of the committee, in the passage of the act, which is perhaps a more complete revision of the Banking Act, than anything for a long time.

They object to the prohibition against borrowing money by members of a bank, his own bank, because, if they wished to borrow anything, they could go to some other ank and borrow, but because it places them in the category, or a category that seems to them to rather reflect upon them.

The CHAIRMAN. Mr. Sisson, that is a matter of wide interest throughout the country, and of course of interest to the community. Let me suggest to you that there is a provision entitled "III" in this bill dealing with that particular matter, and it will come up for discussion when we reach it; and I might say, in that connection, you might advise your friends that we are attempting, and we expect, if the legislation passes, to liberalize that provision of the law.

Now, gentlemen, I am going to suggest, if you are through with Mr. O'Connor, we will meet again at 10:30, Monday morning, and Mr. Eccles will appear before the committee at that time.

Mr. MEEKS. Mr. Chairman, may I ask a question?

The CHAIRMAN. Yes.

Mr. MEEKS. Mr. O'Connor, are you putting your Chicago speech in the record?

Mr. O'CONNOR. Yes, I can do so.

Mr. MEEKS. I wonder if you have copies available that you can pass to the members? I would very much like to have a copy in advance, because we may not get to see it soon.

Mr. O'CONNOR. Thank you, Mr. Meeks.

(The address of Mr. O'Connor is as follows:)

ADDRESS BY J. F. T. O'CONNOR, COMPTROLLER OF THE CURRENCY, BEFORE THE CONVENTION OF THE AMERICAN BANKERS ASSOCIATION, AT CHICAGO, ILL., SEPTEMBER 7, 1933

Our common purpose justifies the acceptance of your gracious invitation. In this my initial appearance before the American Bankers Association, if some slight suggestion can be made to strengthen the financial structure of the Nation, my effort will be fully compensated. At your last annual convention had anyone predicted that every banking institution would be closed for several days, credit paralyzed, and tickers silenced, ridicule, sharp criticism, and condemnation would have greeted the suggestion. It happened. The old order had completely broken down. Will such a condition reoccur?

No finer example of patience and self-restraint can be found in our history than was exhibited by our people in these black days of March. With the storm raging in mad fury, with destructive waves breaking over the deck, a firm hand grasped the wheel, changed the course, substituted hope for despair, and arrived safely in the harbor. Other storms will come, no one will deny. Possibly we cannot prevent the storm, but we can build a ship the elements cannot destroy. The challenge is yours. The thrill of the opportunity appeals to us all.

Probably no provisions in the Banking Act of 1933, sometimes called the Glass-Steagall Act, have attracted so much attention as the insurance provisions. It is my sincere belief that the future of American banking rests in a large measure on proper and courageous management and the adoption of sound policies in the administration of the insurance provisions of the act. Fully realizing the magnitude of the operations involved, the pitfalls which must be avoided, and the nondiverging path which must be followed, as one member of the board of the Corporation, I approach the task humbly but with a grim determination of success.

The principle of guaranteed deposits is not new. Our Government established this on June 25, 1910, when President William Howard Taft advocated and secured the passage of the Postal Savings bill. Some deny this is an insurance or a guarantee. Let us not quibble about words. No one denies that the full faith and credit of the United States is pledged to the return of every dollar in the Postal Savings banks. Today our Government guarantees, or insures or promises, to return approximately $1,184,948,200. No one questions the ability of the Government to pay these deposits. The growth of these deposits during the past 2 years is interesting, if not alarming. Let me give them:

June 30, 1931	$347, 416, 749
June 30, 1932	784, 819, 402
April 30, 1933	1, 159, 794, 016

As already noted, the estimate for June 30, 1933, indicates an increase over April 30, 1933, of $25,154,184. No comment to bankers is necessary on these figures. Even a lawyer appreciates their significance. The Government requires security from the banks to insure these deposits. In this manner the banks guarantee their safe return. The postal depositor becomes a preferred creditor. The ordinary depositor in the bank is merely a creditor. Unlike a story I heard some time ago: A creditor called the president of a large corporation and said, "I see we're in the bosom of a receiver." The president corrected him saying, "You mean the hands." "Well, I do not know about such things." "Oh, don't worry, you are a preferred creditor." "A preferred creditor, am I? What does that mean?" "It means you know now you won't get anything while the common creditor won't know for a year or more."

No individual is permitted to deposit over $2,500 in the Postal Savings bank. There has been a growing demand from all parts of the country to permit unlimited deposits. If nearly $1,190,000,000 has been deposited in Postal Savings under a $2,500 limit, what would the deposit be if the individual deposit were unrestricted? When the insurance feature of the Glass-Steagall bill becomes operative, most of this huge sum should find its way back into the banks. Indeed, Congress would be justified in repealing the law entirely.

Let me briefly outline a few of the main provisions of the Banking Act of 1933 on this subject:

1. The Corporation has three directors: The Comptroller of the Currency and two directors, appointed by the President, who shall not be of the same political faith.

2. A "temporary Federal deposit insurance fund" will become operative on January 1, 1934, which will insure deposits in each member of the fund up to $2,500. Members of the fund will be all member banks licensed before January 1, 1934, by the Secretary of the Treasury and nonmember State banks with the approval of the State supervising authority, after certification to the Corporation of solvency and examination and approval by the Corporation. Both member and nonmember banks must pay to the Corporation an amount equal to one-half of 1 percent of the insured deposits certified as of the 15th of the month preceding the month they were admitted to the fund. One half of this payment will be made upon admission and the other half upon call by the directors of the Corporation.

3. The permanent insurance is effective on July 1, 1934, as to all national banks certified by the Comptroller of the Currency and all State member banks certified by the Federal Reserve Board upon such banks becoming class A stockholders in the Corporation, and nonmember banks have the benefit of such insurance until July 1, 1936, by becoming class A stockholders of the Corporation in compliance with the terms of the act.

4. In becoming class A stockholders, the banks must apply to the Corporation for class A stock in an amount equal to one-half of 1 percent of its total deposits

as computed in accordance with regulations of the Federal Reserve Board, with certain exceptions in the case of banks organized after July 1, 1934. One-half of the amount due for the stock shall be paid into the Corporation upon admission and one-half upon call by the directors of the Corporation.

5. Under the permanent insurance features of the act, net deposits are insured as follows:

One hundred percent not exceeding $10,000.

Seventy-five percent of the amount exceeding $10,000 but not exceeding $50,000, and

Fifty percent of the amount exceeding $50,000.

You will be interested in the progress made to date:

The Government, through the cooperation of the Federal Reserve banks, the Comptroller's Office, and the Reconstruction Finance Corporation, is making a survey of all the banks in the United States. The President called the attention of the governors of the various States to the provisions of the Banking Act of 1933 in a letter dated July 6. The letter was as follows:

MY DEAR GOVERNOR: You have no doubt given serious consideration to the provisions of the Glass-Steagall bill, known as the "Banking Act of 1933", which was approved by me on June 16, 1933.

This act contains far-reaching provisions with reference to State banks. In a very short time, to wit, January 1, 1934, certain State banks which secure a certificate of solvency from the proper State banking authority, and which after examination are found satisfactory to the Federal Deposit Insurance Corporation, will be admitted to the benefits of the insurance fund.

In order that State banks may receive the benefits of the act, it will be necessary in many States for additional legislation; in others, amendments to existing laws, and in others, constitutional changes. You will appreciate the necessity of immediate action in order that the benefits of this act will be as widely distributed as possible.

May I suggest to you that you call together representatives of your State banking department, together with leading State bankers, to discuss with you the necessary legislative changes or constitutional amendments to bring about the desired effect.

I call your particular attention to the following paragraph of the Banking Act of 1933, which is found under subsection (y) of section 8 (last paragraph), which reads as follows:

"It is not the purpose of this section to discriminate, in any manner, against State nonmember and in favor of National or member banks; but the purpose is to provide all banks with the same opportunity to obtain and enjoy the benefits of this title. No bank shall be discriminated against because its capital stock is less than the amount required for eligibility for admission into the Federal Reserve System."

Thanking you for prompt consideration of this matter, I beg to remain,

FRANKLIN D. ROOSEVELT,
President.

The general outline of the set-up of the Corporation has been tentatively approved by the President. I am in possession of the names of over 1,500 qualified men who are available to make examinations. These names have been submitted by the State banking commissioners and others, and they are qualified examiners who have had 5 years or more banking experience and who known the values in the States. Arrangements have been made with the Treasury for the necessary funds to carry out the preliminary work of the Corporation. Our first task is the examination of approximately 8,000 State nonmember banks which are on an unrestricted basis. I shall make the following suggestions to the Board immediately upon reorganization:

First, that each bank applying for insurance be furnished with blank forms to be completed by the banks setting forth each asset under a proper heading and the amount of its deposit liabilities and obligations to other creditors. This will save much time and the examiner will then check the item and appraise the same.

Secondly, that an examiner who knows the values in the particular State, with necessary assistants, be assigned to each State capital to work with the banking commissioner and all examiners in the State clear through the examiner at the capital. In this way the work will be decentralized. It is my belief that whenever a piece of work can be done in a State just as well as at the National Capital, it should be done in that State.

Thirdly, that the names of the banks insured and their location be given simultaneously.

There has recently been sent out to many of the banks of the country a letter in reference to the Federal Deposit Insurance Corporation from which I quote two sentences as follows:

"In the parlance of the street, the independent bank is to be 'ironed out.'"

"Powerful influences are at work to wipe out the small banks and the independent banker has been placed on the defensive."

I know of no more vicious, unwarranted, and untruthful propaganda. The present administration has demonstrated its policy of protection for the little fellow, whether individual or corporate. At a conference with the President on Tuesday afternoon, he authorized me to say to you, and through you to the country, that the object of the insurance provisions of the new bank act was to insure as many nonmember banks as possible. He discussed the details of the act with an amazing knowledge of its provisions. He discussed real values, appraised values, and liquidating values with a fine discrimination. "Injustice must be avoided." In that sentence, the Chief Executive summarized all his comment and direction.

No greater demand came from the people during the past session of Congress than that some form of guarantee or insurance for deposits be passed. The fact that the bill passed the House with but six dissenting votes and passed the Senate without a dissenting vote is evidence of the demand. It could not be ignored. Whether we favored the provision or opposed it, bank insurance is part of the Federal law. Let us examine some of the higher grounds which possibly justify its existence:

First, every depositor in theory has a right to his money. This law makes the theory a fact.

Second, it will banish the fear in every banker's mind of runs upon his bank. We should not again witness the very serious crisis which developed with the beginning of 1933 and which produced grave runs on practically every bank in the country, culminating on March 4 with currency demands amounting altogether to $1,630,000,000. This huge sum was withdrawn in cash by panic-stricken depositors.

Third, it will obviate the necessity for a postal savings bank and return to the banks over a billion in deposits.

Fourth, it will permit an extension of credit and a modification of cash reserves. This will particularly benefit small country banks and their customers. Liquidity means immediate marketability. The average town or small city has sound values but not a high degree of liquidity. Probably nothing in banking parlance has been so much misunderstood as the term "liquidity." The law provides that a certain percentage of a bank's assets shall be in cash and sound banking requires other assets to be liquid. Some well-meaning individuals and other demagogic persons have aroused communities because banks with frozen assets have not been permitted to reopen. They say while certain securities are not worth much today they will be worth face value in 5 or 10 years. If the depositor would accept this viewpoint and take a mortgage or a bond worth $500 for his deposit of $1,000 on the theory that the security would be worth $1,000 in a few years, our problem would be simple. The depositor may rightly demand his entire deposit in cash.

Fifth, the elimination of interest on demand deposits will save the banks many millions of dollars. The total amount paid during the past 5 years by member banks on demand deposits was $1,230,242,000, making an average of $246,048,500 per annum. Again the Federal Reserve Board fixes the rate of interest paid by member banks on time deposits. Is there any depositor who would not accept one-half of 1 percent less interest and know his deposit was insured, if such a step were necessary to save the insurance provision? Would any nonmember bank not cooperate to this extent? No depositor would object to paying two and one-half or up to five dollars to insure a $1,000 deposit. Besides, the United States Government is contributing $150,000,000, and approximately $139,000,000 will be contributed by the Federal Reserve banks, in addition to the one-half of 1 percent by the banks.

Sixth, now a point not generally discussed and offered here as a matter of opinion. It is my firm opinion that the insurance features of the law will save millions to our people. The high pressure and not too scrupulous salesman often plants the seed of suspicion as to a bank's solvency in the prospective purchaser's mind. The life savings of men and women have been withdrawn and invested in worthless securities or enterprises because of this fear. When the

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suspicions becomes a belief, the confidential relation between the banker and the depositor is destroyed. The very fact that the honest, highly trained, conservative banker has made errors in making investments is proof of the great danger of loss by those not trained in making investments.

The insurance feature of the bill differs from laws heretofore passed in two main respects, first, the participation of the United States Government in making a substantial investment in the capital structure, and secondly, in recognizing the sound insurance feature that risks should be spread over a large territory and not localized.

The test of admission of a bank to the insurance fund is determined upon its ability to pay all of its liabilities to depositors and other creditors, as shown by the books of the bank. In other words, the assets must be sufficient to accomplish this purpose (sec. 12B(e)). Information gathered from 4,836 national banks at the close of business on May 13, 1933, showed that 96.76 percent of the total depositors in national banks had deposits of under $2,500. The survey further showed that the average deposit was $183.17, and that these 96.76 percent, totaling 21,748,754 depositors, had 26.72 percent of the total deposits in the national banks as of that date, while 0.13 percent of depositors, totaling 28,356, had deposits of over $50,000, or 40.29 percent of the total deposits, which represented an average deposit of $211,820.85. It must be remembered that the deposits of over $50,000 represent deposits of State governments and their subdivisions as well as the large corporations of the Nation. No effort was made to distinguish between individual and corporate deposits.

The President has authorized me to give you the names of the men he has selected as directors of the Federal Deposit Insurance Corporation. The law requires that one of these members be a Democrat and one a Republican. The Comptroller of the Currency is named by law as the third member of the Board.

As the Democratic member, the President has selected Walter Joseph Cummings, of Chicago. Mr. Cummings is at present executive assistant to the Secretary of the Treasury of the United States. He was appointed by Secretary William H. Woodin on April 8, 1933. He was born in Chicago, Ill., on June 24, 1879, and is the son of Walter J. Cummings and Mary Cummings, of Chicago. He attended the Chicago public schools and Loyola University. In 1902 he entered the plant of the Cummings Car & Coach Co. at Chicago, Ill., for the manufacture of cars and trucks, acting as secretary and treasurer. In 1907 he became vice president of the company, and in 1918 was elected president of the Cummings Car & Coach Co. He also holds many important directorships, including the American Car & Foundry Motors Co., of New York; J. G. Brill Co., of Philadelphia; and is president of the Chicago & West Towns Railway Co., of Chicago; the Chicago & Calumet District Transit Co., of Chicago; and the Des Moines Railway Co., of Des Moines. Mr. Cummings was appointed by the Governor of Illinois in January 1933 as commissioner of Lincoln Park, Chicago. He has been identified with and acted in many civic organizations of Chicago, and at the present time is a trustee of Loyola University, a member of the executive committee of the Associated Charities of Chicago, and has taken a deep interest in the civic betterment of the city. He had conferred upon him the honorary degree of doctor of laws by Loyola University.

The delay in making the appointments on this Board was no doubt caused by the selection of the next member. As I have stated, the law requires that one of the members shall be a Republican, and the President had considerable difficulty in finding a Republican. Mr. E. G. Bennett, of Ogden, Utah, has been appointed by the President.

Mr. Bennett was born in York, Nebr., on April 23, 1888. He received his early training under Judge George W. Post, who controlled 12 banks in eastern Nebraska now operated by the McLeod interests. He was employed for 8 years by J. S. & W. S. Kuhn, Inc., who built irrigation, power, and other projects in the Snake River Valley of Idaho, and then became vice president and general manager of the First National Bank of Jerome, Idaho, and the Jerome Loan & Trust Co. During this period he made loans for Holland interests, loaning approximately $1,500,000 on irrigated farms in Snake River Valley. He acted as secretary of the Idaho agency of the War Finance Corporation, loaning $6,000,000 on livestock without loss. During the past 6 years and at the present time, Mr. Bennett has devoted his time to the Eccles and Browning interests in the capacity of vice president and general manager. These interests own and operate 28 banks in Utah, Idaho, and Wyoming, all but 3 of which are State banks. For the 4 years from 1924 to 1928, Mr. Bennett was a member of the executive council of the American Bankers Association, representing Idaho. In 1923 he was appointed by the Governor of Idaho with two others to the Bank Code Commission. The code prepared by the commission was adopted by the legislature in 1925. In the preparation of this code an exhaustive study was made of all the banking laws of all the States.

Some of Mr. Bennett's other connections are—president of J. M. & S. M. Browning Co.; president Browning Arms Co.; president Lindsay Land & Livestock Co., which company owns a 130,000-acre ranch (18,000 ewes and 4,000 cattle); president Lion Coal Corporation operating mines in Utah and Wyoming; president Eleventh Regional Agricultural Credit Corporation (Utah, Nevada, Arizona, and California).

Mr. Bennett's companies do not owe any money to anyone. His banks and companies are in excellent financial condition. No man knows better the problems of the State banker than Mr. Bennett. He will bring to the Board a sympathetic understanding of all those bankers who have assisted in building the West. No man has a better knowledge of the present banking situation in the country than Walter J. Cummings. For 5 months he has devoted his time at great personal loss to assist in rehabilitating the banking structure. He was drafted into the service by his close personal friend and business associate, Hon. William H. Woodin, Secretary of the Treasury. His experience in handling large financial problems makes him a valuable member of the Board. He knows the Treasury and all of its departments. This insures us that there will be no delay in getting the machinery in motion. These two sound and successful business men the President has called to a difficult task. All we ask is a fair trial.

There are several features of the Banking Act of 1933 which have raised innumerable questions of interpretation and of administration in which you may be interested. First and foremost are the problems which have arisen in connection with affiliates as definied by the Banking Act of 1933. The definition of affiliates of member banks as laid down by the act is very broad and technical and a literal interpretation of the law may lead to many situations which could not be foreseen and which I doubt the framers of the act meant to bring about. Let me give you a few illustrations:

We have a national bank, 96 percent of the stock of which is owned by a packing company. The packing company is a holding company affiliate. This corporation in turn owns or controls 200 other corporations scattered throughout the world. Is each one of these 200 corporations also an affiliate of a national bank? The national bank is required under the act to furnish report of its affiliates and to publish the reports of its affiliates under the same conditions as govern its own condition reports. I venture to state that the depositors of this national bank will be somewhat mystified by the publication of the reports of the 200 corporations.

The majority of stock of another national bank is owned by a church, a corporation sole. The church is an affiliate. It in turn has furnished all or part of the funds for other church buildings, a hospital, orphans' home, and other charitable institutions in a particular State, all incorporated and controlled by the first church. Are all of these institutions affiliates of the bank? Must the bank furnish the statements of these institutions and publish them?

A bank had as collateral to a loan the majority of stock of a hosiery corporation and foreclosed on the collateral to protect itself, thus becoming the owner of the stock. Is the hosiery corporation an affiliate? If it is, the bank cannot make a loan to it except on collateral which the corporation does not have and since the corporation is unable to borrow from other sources, the bank cannot protect itself.

There are but three illustrations of the thousands of problems which arise in connection with affiliates, and the Attorney General of the United States has been asked for his opinion with respect to some of these problems.

The Banking Act of 1933 provides in part:

"No executive officer of any member bank shall borrow from or otherwise become indebted to any member bank of which he is an executive officer."

Violation of the prohibition is a criminal offense. No definition of "executive officer" is given in the act. The question of what is an "executive officer" immediately faced the banks and the examiners. No ruling on a criminal statute by my Department would protect the banks. The opinion of the Attorney General was requested. He has advised that: "It is not the designation under which one is known, but the nature of his duties which characterizes him as an "executive officer." *Small* v. *Gibbs Press*, 225 N. Y. S. 141, 142."

He further stated: "It is the duty of the banks and of all officers who by any possibility might be affected to keep within the statute and to weigh carefully all the facts and circumstances (peculiarly within their provision) before acting."

He refers with approval to the statement in *Arkansas Amusement Corporation* v. *Kempner* (33 S. W. (2d) 42) to the effect that:

"An executive officer or employee is one who assumes command or control and directs the course of the business, or some part thereof, and who outlines the duties and directs the work of subordinate employees, as usually provided for in the articles of association, the bylaws, or a resolution of the directors.'

The practical administration of this section of the Banking Act of 1933 from an examining standpoint requires the Comptroller's Office to take the position that the following officials of a bank will de deemed, prima facie, to be "executive officers" for the purposes of said section, it being understood that such presumption may be rebutted on a sufficient showing: The president, a vice president, the cashier, an assistant cashier.

The facts in any given case may, as indicted by the opinion of the Attorney General, constitute other officers or employees, "executive officers" within the scope of the act.

It, of course, would be more satisfactory to have the definition of "executive officer" laid down by Congress, especially when, in weighing facts, one has a penal statute involved.

The section of the Banking Act with respect to extension of branch banking for national banking associations outside of the limits of the city, town, or village in which the association is situated, has raised some problems, particularly the language: "* * * If such establishment and operation are at the time authorized to State banks by the statute law of the State in question by language specifically granting such authority affirmatively and not merely by implication or recognition, and subject to the restrictions as to location imposed by the law of the State on State banks."

Under the wording of this provision of the Banking Act, national banks are not permitted to have branches outside of the city, town, or village in which they are located in some States where State banks are permitted to establish such branches. Two outstanding cases are those of Maryland and South Carolina, where nonmember State banks may establish branches, but member banks, whether National or State, may not establish branches under the wording of this particular statute. In connection with the establishment of branches, it was of course, stated before the act was passed by many that there would be a great rush for branches and they would be established rapidly. The statute became effective on June 16 of this year; practically 3 months have elapsed since its enactment. Only 37 branches of national banks have been established under its provisions. Of this total, 9 branches were established in communities which were without banking facilities, 2 branches were established for the purpose of taking over banking institutions in the hands of conservators, 12 were established to take over going institutions, and 8 were established to replace 8 branches of State banks taken over by a national bank. Accordingly, only 9 branches represented new banking facilities.

There is not time to go into all of the various problems which have arisen under the Banking Act of 1933, but I have given you a few illustrations which should be of interest.

There seems to be a great deal of misunderstanding by banks and the public generally with respect to receiverships of national banks. These statements are being made repeatedly:

"1. Receivership means all assets thrown on the market at once—forced liquidation."

In the first place it is obviously impossible to throw the assets on the market at once and, even could it be done, it would be poor policy. The Comptroller acts in a trustee capacity and his duty is to realize as much as possible for creditors. The average time required to fully liquidate a receivership is 5½ years.

"2. Receivers get commissions—expenses are heavy and eat up the trust."

The facts are that receivers of national banks are not paid any commission but a flat salary and the average salary is around $350 per month, varying as to the size of the receivership; and since one receiver in many cases handles more than one bank, the average salary per bank is about $1,713 per annum.

The total average cost of liquidation last year was but 3.2 percent of actual collections and the average for fully liquidating all banks in the past has been 3.9 percent of book value and 6.65 of actual collections.

I desire to touch for a few minutes upon the growth and work of the Comptroller's Office, as now constituted, as compared with the past. It is interesting to note from the first report of the Comptroller of the Currency to Congress, dated November 28, 1863, that there were 134 national banks and that the personnel of the Comptroller's bureau consisted of 8 persons, including the Comptroller. In 1865 the Comptroller reported 1,601 national banks with the personnel of the bureau 77 in number. It may be rightly said that those were the good old days with few problems. Let us see the condition in 1893—a panic year. Quoting from The Romance and Tragedy of Banking, by T. P. Kane, former Deputy Comptroller of the Currency:

"Every hour of the day and late into the night telegram after telegram was received announcing additional suspensions of banks or new complications which had to be promptly met. As many as 30 suspensions occurred in a single day, and for a time it looked as if every national bank in the system would succumb."

The Comptroller of the Currency that year in his report to Congress stated that 154 national banks suspended, receivers being appointed for 65. Problems? Yes, but today we face trust departments, savings departments, bond departments, affiliates, preferred stock, organizations, reorganizations, bond depreciation, other real estate, banks in conservatorship, and 1,123 banks in the hands of receivers. In touching on these 1,123 receiverships, the old story of the borrower who asked the banker if he had ever been in the pants business and, upon receiving the answer "No", stated: "Well, you are in it now", is certainly applicable to banks in receivership. I find that among the enterprises the Comptroller of the Currency is directing are: Hotels; coal mines; quarries; lumber manufacturing; vineyards; apartment houses; office buildings; farming; raising sheep and cattle; growing cotton, pecans, and citrus fruits; operating pickle factories, cold-storage plants, motor freight terminals, and a railroad. Incidentally, the railroad is operating at a profit.

At the present time in the Comptroller of the Currency's Office there are 216 national examiners, 297 assistant examiners, and 156 other employees; in the Reorganization and Conservators Division there are approximately 305 employees; and 271 employees in the Insolvent Division, not including receivers, conservators, their employees, or their attorneys. Besides using all available space in the Treasury Building, it has been necessary to secure the major part of a large modern office building opposite the Treasury.

A picture of what has been achieved in giving relief to depositors by the various governmental agencies is presented by the following figures:

On December 31, 1932, deposits in national banks amounted to approximately $18,500,000,000. On March 16, 1933, the frozen deposits in unlicensed national banks amounted to $2,200,774,000, representing approximately 12 percent of the aggregate amount of deposits on December 31, 1932. On September 5, 1933, frozen deposits in unlicensed national banks amounted to $746,731,000, representing 4 percent of deposits as of December 31, 1932. If we deduct the amount of frozen deposits of $440,099,000 which will be released immediately upon the consummation of the approved plans, the total amount of frozen deposits in unlicensed national banks will be $306,632,000, or 1.66 percent of the total amount on deposit on December 31, 1932.

On March 4, 1933, there were 5,938 operating national banks in the United States. Of this number, 4,509 were licensed to resume normal banking functions on March 13, 14, and 15, leaving 1,429 national banks unlicensed as of the beginning of business March 16. Within 174 days there have been 423 old banks licensed, 100 new banks chartered, and 372 plans of reorganization approved.

I desire to reaffirm what I stated in my address over the National Broadcasting System from Washington on July 19:

"No discrimination has been made between Republican dollars and Democratic dollars in closed banks. My department has assumed that the Republican depositor, although probably much less in need of his money than his Democratic friend, is just as anxious to get his share of the remaining 5 percent now in closed national banks. Of the many hundreds of depositors, creditors, stockholders, and officers with whom I have discussed plans of reopening, I have never inquired and do not know the politics of any. Let me say definitely and positively that the Comptroller of the Currency is interested in your plans for reopening of your bank and giving relief to the depositors and not in your politics. There have been some fine illustrations of self-sacrifice and true Americanism by officers and stockholders of many banks. Men and women have come forward and volunteered their 100 percent assessment, waived their deposits, subscribed for new capital, in order that the depositors should not lose a single dollar. I mention this because some are prone to mention only those connected with the banks who have tried to evade their legal and moral responsibility and have been compelled by legal proceedings to make their just contribution."

In conclusion, let me say that as politics have never entered into the consideration of any plan for reorganizing or reopening or the establishment of any bank or branch in any of the divisions of the Comptroller's Office, can I ask you to bear with me in the solution of difficult problems in the same spirit. In the great divine scheme of life, as individuals we play our part and pass on. Our places can be filled without the slightest interruption in the march of progress. My purpose is to serve a great country with my limited ability. If uncounted hours in the day and long into the night will bring forth a better understanding between my Department and the people, will make for a more permanent banking structure, the effort will not be counted in vain. Let us bring cold figures to life. Let us put a heart back into banking and let profits be subservient to service. Let us bring a great profession back to the leadership it once enjoyed. Let the inspiration of the names of great bankers of the past—men who tossed their fortunes into their country's exchequer to save its credit and win its wars—touch the inner recesses of our souls that we may imitate and serve.

(Thereupon, a recess was taken in the hearing until Monday Mar. 4, 1935, at 10:30 a. m.)

BANKING ACT OF 1935

MONDAY, MARCH 4, 1935

House of Representatives,
Committee on Banking and Currency,
Washington, D. C.

The committee met at 10:30 a. m., Hon. Henry B. Steagall (chairman) presiding.

The Chairman. Gentlemen, we have with us this morning Governor Eccles of the Federal Reserve Board, who will discuss title II of H. R. 5357, and I think Governor Eccles would like to proceed without interruption until he shall have concluded a preliminary discussion of the bill, after which, of course, he will be glad to answer any questions and furnish any information that may be desired by members of the committee.

Governor Eccles, we shall be glad to have you proceed in your own way for such time as you desire, without being interrupted.

STATEMENT OF GOV. MARRINER S. ECCLES, OF THE FEDERAL RESERVE BOARD

Mr. Eccles. I am sorry that I do not feel entirely up to par today. I have been laboring under a rather heavy cold. I had thought, at first, to make a rather extended verbal statement with reference to the legislation. I decided, however, on account of the way I feel, to make a brief written statement of the general outline of the legislation. I believe this will in a general way cover the philosophy underlying section 2 of the bill.

The Chairman. Title II?

Mr. Eccles. Title II of the bill. So that I will just proceed to read this statement, if I may.

In recommending banking legislation at this time, it is recognized that the Congress has before it an unusual number of urgent matters that are engaging its attention, and that legislation in order to deserve your consideration at this session must not only be important in general but must also be urgent at this particular time.

We are not unmindful of the fact that within the past 2 years you have passed the Emergency Banking Act, the Banking Act of 1933, the Securities Exchange Act, and other important pieces of legislation dealing with banks. One purpose of this legislation has been to meet emergency conditions, and it is now proposed to incorporate into permanent legislation the features of the emergency laws that have proved to be valuable.

Another purpose of recent banking legislation, and particularly of the banking bill of 1933 and of the portions of the Securities

Exchange Act that deal with powers of the Federal Reserve Board, has been to prevent the recurrence of speculative excesses which preceded the recent break-down of our banking machinery and were partly responsible for this collapse. These bills were largely inspired by the difficulties that came to a head in 1928 and 1929, and it is gratifying to know that we now have on our statute books measures that will go far toward preventing the recurrence of conditions such as prevailed during the speculative orgy of these years.

At the present time, however, there appears to be no immediate danger of excessive speculation. The present need is to so modify our banking law as to encourage the banking system to give a full measure of cooperation to efforts at economic recovery. It is even more important from the longer time point of view to so modify our banking structure and administration as to have it become an influence toward the moderation of fluctuations in employment, trade, and business. This would tend not only to avoid the particular evils that came to a head in 1928 and 1929, but to so regulate underlying conditions as to diminish the possibility of a speculative boom getting under way. For when speculation is once under way it is extremely difficult to control, and the only means of preventing excesses is to combat conditions that are favorable to their inception and early development.

In order to accomplish this it is necessary to improve our machinery of monetary control, which is the principal objective of title II of the proposed bill.

More specifically these objectives are to increase the ability of the banking system to promote stability of employment and business insofar as this is possible within the scope of monetary action; as a necessary step in that direction, to concentrate the authority and responsibility for the formulation of national monetary policies in a body representing the Nation; to modify the structure of the Federal Reserve System to the extent necessary for the accomplishment of these purposes, but without interfering with regional autonomy in matters of local concern; and finally to relieve the banks of the country of unnecessary restrictions that handicap them in the proper performance of their functions and thus to enable them to contribute more effectively to the acceleration of recovery.

In my opening remarks I wish to direct your attention particularly to four proposals incorporated in title II of the bill. Other provisions of the bill I wish to leave for your consideration, with the understanding that I shall be glad to answer any questions that you may wish to ask about them.

The four questions which I wish to discuss this morning are: (1) The proposal to combine the offices of chairman of the board of directors and governor of the Federal Reserve banks, and to have the appointments to this combined office subject to approval by the Federal Reserve Board (sec. 201 (1), pp. 38–41); (2) modification of the machinery for determining open-market policies of the Federal Reserve System (sec. 205, pp. 43–44); (3) transfer of the determination of eligibility requirements from the statute to the Federal Reserve Board (sec. 206, pp. 45–46); and (4) liberalization of provisions relating to real-estate loans (sec. 210, pp. 49–51).

1. COMBINING GOVERNORS AND CHAIRMEN

As you know, the present law provides that the Federal Reserve Board appoint 3 directors of each Federal Reserve bank and that 1 of the directors appointed by the Board be the chairman of the board of directors. It appears to have been the intention of the framers of the Federal Reserve Act that the chairman of the board of directors be the principal executive officer of each bank and the law makes him also the official representative of the Federal Reserve Board at the bank. In practice, however, it has developed that the directors appoint an executive officer for whom they have adopted the title of governor of the Federal Reserve bank, a title that is not mentioned in the law, and that these governors have become the active heads of the Federal Reserve banks.

The proposal in the bill is to recognize the existing situation by giving the governor of a Reserve bank a status in the law and to combine his office with that of the chairman of the board of directors. It is, of course, essential that the holders of these combined offices be approved by the Federal Reserve Board. The Board, you will note, will no longer appoint a chairman of the board, but will merely have the power to approve or disapprove the appointment of the governor, who will also be chairman of the board. In this proposal there is no encroachment on the autonomy of the individual Reserve banks. It merely reestablishes the original principle of the Federal Reserve Act that the Federal Reserve Board, which has responsibility for national policies and for general supervision over the Reserve banks, shall be a party to the selection of the active heads of the 12 Reserve banks. This change will work towards smoother cooperation between the Board and the banks and will establish within the banks a greater unity of administrative control than now exists. It will also result in considerable saving through the elimination of one of the two highest officers in each Federal Reserve bank.

2. OPEN-MARKET OPERATIONS

From the long-time point of view the recommendations dealing with changes in the machinery for determining and carrying out the open-market policies of the Federal Reserve System are essential. Open-market operations are the most important single instrument of control over the volume and the cost of credit in this country. When I say credit in this connection I mean money, because by far the largest part of money in use by the people of this country is in the form of bank credit, or bank deposits. When the Federal Reserve banks buy bills or securities in the open market, they increase the volume of the people's money and lower its cost; and when they sell in the open market, they decrease the volume of money and increase its cost. Authority over these operations, which affect the welfare of the people as a whole, must be vested in a body representing the national interest.

Under existing law open-market operations must be initiated by a committee consisting of representatives of the 12 Federal Reserve banks, that is, by persons representing primarily local interests.

They must be submitted for approval or disapproval to the Federal Reserve Board, and after they have been approved by the Federal Reserve Board, the boards of directors of the Federal Reserve banks have the power to decide whether or not they wish to participate in the operations. We have, therefore, on this vital matter a set-up by which the body which initiates the policies is not in a position to ratify them; and the body which ratifies them is not in a position to initiate them or to insist on their being carried out after they are ratified; and still a third group has the power to nullify policies that have been initiated and ratified by the other two bodies. In this matter, therefore, which requires prompt and immediate action and the responsibility for which should be centralized so as to be inescapable, the existing law requires the participation of 12 governors, 8 members of the Federal Reserve Board, and 108 directors scattered all over the country before a policy can be put into operation.

It requires no further explanation to show that the existing machinery is better adapted to delay and obstruction than it is to effective operation, and that it results in a diffusion of responsibility which prevents the necessary feeling of complete authority and responsibility by a small group of men who can be held accountable by the Congress and the Nation for the conduct of this matter that is of national importance.

The proposal in the bill is to set up a committee of 5, 3 of whom shall be members of the Federal Reserve Board and 2 governors of Federal Reserve banks. This proposal would have the advantage of creating a small committee with undivided responsibility. It is not clear, however, that this arrangement is the best that can be devised for the desired purpose. The Federal Reserve Board, which is appointed by the President and approved by the Senate for the purpose of having general responsibility for the formulation of monetary policies, would under this proposal have to delegate its principal function to a committee, on which members of the Board would have a bare majority, while governors of the banks would have 2 out of 5 members.

From the point of view of the Board the disadvantages of this arrangement are that a minority of the Board could adopt a policy that would be opposed to one favored by the majority. It would even be possible for one member of the Board by joining with the two governors to adopt a policy that would be objectionable to the seven other members of the Board.

The placing of this authority in such a committee would also have the disadvantage of giving one important power, the power of open-market operations, to the open-market committee, while other fundamental powers are vested in the Board. These powers could be utilized to nullify the actions of the open-market committee. For example, the committee might adopt a policy of easing credit, while the Federal Reserve Board would be in a position to tighten credit, either by raising discount and bill rates or by increasing member-bank reserve requirements. Also the Board, through its power of prescribing regulations for open-market operations, could conceivably interfere with the carrying out of the policies of the committee. While it is not contemplated that such extreme situations would occur, it does not seem desirable to amend the law in a manner that might result in such unreasonable developments.

Upon further study it would appear that the best way in which to handle this proposal would be to place the responsibility for open-market operations in the Federal Reserve Board as a whole and to provide for a committee of five governors of Federal Reserve banks to advise with the Board in this matter. The Board should be required to obtain the views of this committee of governors before adopting a policy for open-market operations, discount rates, or changes in reserve requirements.

Such an arrangement would result in the power to initiate open-market operations by either a committee of the governors or by the Board, but would place the ultimate responsibility upon the Federal Reserve Board, which is created for that purpose. In this connection I should like to quote President Woodrow Wilson, who in his address to the joint session of Congress on June 23, 1913, said:

> The control of the system of banking and of issue * * * must be vested in the Government itself, so that the banks may be the instruments, not the masters, of business and of individual enterprise and initiative.

3. ELIGIBILITY OF PAPER

It is proposed to give the Federal Reserve Board authority by regulation to determine the character of paper that may be eligible as a basis of borrowing at the Federal Reserve banks. This is particularly important at this time because it would encourage member banks to pay less attention to the form and maturity of paper that is offered by would-be borrowers and to concentrate their attention on the soundness of such paper. At present many banks are unwilling to extend loans to borrowers who have assets that are unquestionably sound because they lack the assurance that in case of a withdrawal of deposits they would be able to liquefy these assets at the Federal Reserve banks.

In times of emergency it has been necessary to remove existing restrictions and to give discretion in the matter to the Federal Reserve authorities, as was done under the Glass-Steagall Act of 1932. This act, however, was passed after a great many banks had gone to the wall at least partly because of lack of eligible paper and its provisions insofar as they relate to borrowing from the Reserve banks, have now expired. I think they expired yesterday.

What is proposed is not, as has been sometimes alleged, a policy of opening the doors of the Federal Reserve banks to all kinds of paper, regardless of its soundness. On the contrary, it is proposed to place emphasis on soundness rather than on the technical form of the paper that is presented.

Experience under emergency laws shows that the Federal Reserve banks and the Federal Reserve Board have exercised caution and, though they have extended credit on ineligible assets to the extent of $300,000,000, all but $1,500,000 of this has been paid back and the banks have suffered no considerable losses. It would appear safe, therefore, to intrust discretion in the matter to the Federal Reserve Board, which is always in session and, therefore, in a position to consider emergencies promptly without being under the necessity of proclaiming them by an appeal to Congress and thereby aggravating the situation, and being obliged to wait for Congress to be in session and to act on the matter.

Another phase of this problem is that the total volume of paper eligible for discount held by member banks at the present time is only about $2,000,000,000, or less than 8 percent of the resources of the banks, and even in 1929 it was only about $4,000,000,000, or a little more than 12 percent. While this amount is sufficient in the aggregate to provide access to the Federal Reserve banks, there were many individual banks that did not possess sufficient eligible paper. Even more important than that, is the fact that in a period of timidity the banks tend to refrain from making loans, except on paper eligible for discount at Federal Reserve banks. This is even now a factor causing liquidation in many communities and preventing adequate expansion of credit in others.

A bank that would conduct its business on the theory of having only such assets as can be disposed of at will in times of crisis, when the national income has been cut in two, cannot serve its community adequately. Such a bank would confine its operations to the purchase of the most liquid open-market paper, with the consequence that it would neglect its local responsibilities and would nevertheless find it difficult to earn enough from the low returns on such paper to cover expenses and dividends. The banks should be in a position to meet the needs of their communities for all kinds of accommodation, both short and long term, so long as the credits are sound, and they ought to have the assurance that all sound assets can be liquefied at the Federal Reserve bank in case of an emergency.

4. REAL-ESTATE LOANS

Closely allied to this matter of eligibility is the proposal that the limitations on real-estate loans be modified so as to permit member banks better to supply the needs of their communities for mortgage loans. This proposal does not introduce a new character of loan, it merely relaxes existing limitations on real-estate loans which national banks have made for 20 years. What the bill proposes is to modify the requirements so as to make them more realistic and to enable the member banks better to serve their communities. Coupled with the provisions in regard to eligibility, these proposals ought to result in greater willingness of member banks to lend on real estate and, therefore, to an improvement in the mortgage market and a stimulation of construction which is essential to business recovery.

Member banks hold about $10,000,000,000 of the people's savings, and it is therefore proper and necessary that they invest a part of their funds in long-time undertakings. The separation of commercial banking from savings banking may be theoretically desirable, but it cannot be accomplished in this country without disrupting existing machinery, while the need for increased activity in building is urgent. Member banks are suffering from the competition of many Government and other agencies that are entering the field of real-estate loans, and it is a matter of self-preservation for the banks to be able to hold and expand their activities in this field.

The details of the bill as proposed may have to be modified. The problem is a difficult one because the laying down of specific percentages of value presents many perplexities. In some regions, and at some times, a 75-percent loan on real estate is conservative, while at other times a 50-percent loan may be too liberal. It may be best in this matter, as in others, to vest discretion in the Federal Reserve Board to prescribe such rules and regulations about real-estate loans as in its judgment would operate most effectively in the public interest.

OTHER PROPOSALS IN TITLE II

Other sections of title II of the bill which I have not discussed may be briefly enumerated: Provision that directors of the Federal Reserve banks shall not serve for more than 6 consecutive years. This would prevent crystallization of any one interest in the management of a Reserve bank. A change in the qualifications of members of the Federal Reserve Board to make these qualifications more descriptive of the functions of the Board. An increase in salary of future appointive members of the Board and provision for pensions. Grant of power to the Board to assign specific duties so as to be relieved of detail. Placing of obligations guaranteed by the United States Government on the same basis as direct obligations of the Government. Repeal of collateral requirements against Federal Reserve notes. These requirements serve no useful purpose and have been sources of serious trouble at critical times. Clarification of the authority of the Board to raise or lower reserve requirements—the bill as introduced authorizes changes in reserve requirements for different districts or classes of cities. It might be modified by eliminating changes by districts and classifying cities into two groups—(1) Reserve and Central Reserve cities and (2) other cities. Authority for the Federal Reserve Board to waive capital requirements for admission of insured banks into the system prior to July 1, 1937, when all banks, in order to be insured, must be members of the Federal Reserve System. This might be broadened so as to authorize the Board to waive not only capital but all requirements and to permit existing banks to continue permanently with their present capital, provided it is adequate in relation to their liabilities.

TECHNICAL PROVISIONS

Title III of the bill contains a number of sections proposed by the Comptroller of the Currency and by the Federal Deposit Insurance Corporation. Sections in which the Federal Reserve Board is interested are in the nature of technical improvements of a noncontroversial nature of the same general character as those contained in the so-called "omnibus banking bill" which was reported favorably by the Banking and Currency Committees of both Houses of Congress in June 1934, but failed of enactment in the closing days of the Seventy-third Congress.

For example, a provision that a holding-company affiliate, which is a holding company by accident and is not engaged in the business of holding bank stock, shall be exempted from the requirement of obtaining a voting permit. Another example is the provision that member banks for the purpose of calculating reserve requirements shall be allowed to deduct from gross deposits the amounts that are due them from other banks rather than be allowed to deduct these amounts only from the deposits they hold for other banks. The existing provision has resulted in injustice to country banks, which hold no deposits for other banks, and are, therefore, unable to get the benefit of the deduction which city banks can make. There is also a proposal intended to simplify the provisions of the Clayton Antitrust Act in regard to interlocking bank directorates and to facilitate the administration of these provisions by the Federal Reserve Board.

Provisions in title III, as well as in title II, are still being studied and improvements and modifications in technique and in phraseology are being developed. I shall, therefore, appreciate an opportunity to submit to the committee for its consideration a number of amendments to the bill before final action is taken. It would also be helpful if the committee would permit the Board's counsel to cooperate with the committee's counsel in the final perfecting of the phraseology of the bill.

Thank you.

The CHAIRMAN. Gentlemen, in view of the physical difficulties under which Governor Eccles is laboring this morning, I have assured him that we would excuse him, when he had finished his general statement. Governor Eccles, if you desire that we do so, we shall be glad to let you go on tomorrow morning, and the committee will meet at 10:30 o'clock.

(Whereupon the committee adjourned until 10:30 a. m., Tuesday, Mar. 5, 1935.)

BANKING ACT OF 1935

FRIDAY, MARCH 5, 1935

House of Representatives,
Committee on Banking and Currency,
Washington, D. C.

The committee met at 10:30 a. m., Hon. Henry B. Steagall (chairman) presiding.

The Chairman. Gentlemen, we will come to order. Governor Eccles, the committee will be glad to have you resume your discussion of title II of the bill. You may proceed as far as you desire without interruption.

STATEMENT OF HON. MARRINER S. ECCLES, GOVERNOR, FEDERAL RESERVE BOARD—Resumed

Mr. Eccles. I made a general statement yesterday, and it occurred to me that it might be helpful to the members of the committee if I discussed, more or less informally and possibly in more detail, some of the features of the bill.

It is proposed to combine the office of the chairman of the board of directors and the Governor of the Federal Reserve bank. At the present time each of the 12 Reserve banks has 9 directors. Six of those directors are elected by the stockholders of the banks, that is, the member banks; three of them are appointed by the Federal Reserve Board.

These directors are appointed for 3-year terms. Of the 6 directors appointed or elected by the member banks, 3 are bankers, known as "class A" directors; 3 must be selected from commerce, agriculture, or industry, and are known as "class B" directors. One of the three directors appointed by the Federal Reserve Board, known as "class C" directors, is selected or appointed as chairman of the board of directors of each Federal Reserve bank. He is also the Federal Reserve agent. He is a full-time, highly paid official; and originally it was conceived that he would be the executive head of each Federal Reserve bank.

The governors of the Federal Reserve banks are not mentioned in the Federal Reserve Act. The act provides that the directors of the bank shall select such officers and employees as are necessary to conduct the affairs of the bank.

The title of "governor" was given by the nine directors to the person selected by them as the operating head of the bank. In practice, the position of the governor has become an outstanding and important position, and in nearly every instance he has become the head of the bank. He is not a director of the bank; he is elected by the board of directors; the nine members of the board of directors.

The Federal Reserve Board has no legal relationship with the governor of the bank, has no responsibility in his selection except that it passes on his salary. Its official relationship with the bank is through the chairman and Federal Reserve agent, whom the law designates as the Board's official representative at the Federal Reserve bank.

It is proposed, in this legislation, as a matter of efficiency, coordination, and good organization, to do away with this dual relationship and to combine the office of governor with that of chairman, making the governor and the chairman a class C director. The board of directors of each Federal Reserve bank will select the governor and the chairman; but this selection must be subject to the approval of the Federal Reserve Board.

You will observe that the Federal Reserve Board will not have the power of appointment of the chairman, which will be given to the local board and combined with the office of governor; the appointment will be subject to the approval of the Federal Reserve Board.

This will make for better coordination and economy, will do away with the possibility of cleavage, by reason of the dual organization of the chairman, appointed by the Board in Washington, and the governor, selected by the local board.

Although the directors of the banks are appointed for a period of 3 years only, in practice many of the directors have served since the beginning of the Federal Reserve System. It is thought advisable to limit the term of office of all of the directors to two consecutive terms, totaling a period of 6 years. This is proposed to avoid the crystallization of control or authority in any one group or combination.

It is felt that, in each Federal Reserve district, there are many able men to represent the bank members and also commerce and industry, as well as the Board at Washington, which appoints the three class C directors; and that the public nature of the Reserve System is such that it would be to the interest of the System to have a limit upon the terms of the directors.

It is recognized that there may be a loss of some very able men as the result of this restriction, but it is believed that there will be more gained as a result of this policy than will be lost.

It is interesting to note that two, and I believe three, of the Federal Reserve banks have adopted the policy, without it being prescribed by law, of limiting the terms of their class A and class B directors, that is, the directors elected by the member banks, to 3 years. The New York bank and the Dallas bank, and I think the Atlanta bank, rotate the offices of their class A and B directors. They find this in the interest of harmony among their member banks; and it is felt that, if it is in the public interest to do that in the case of those banks, it would be well to do it in the case of all banks and to place the limitation to 6 years in the law.

Since this proposal was made, there has been considerable discussion, and I find that, almost universally, it is looked upon with a great deal of favor by the banks throughout the country. I find that there is considerable feeling among many of them that there has been a certain amount of crystallization of control in small groups.

I met with a group of bankers on Friday, and without exception, they were all very favorable to that restriction.

Admission of insured nonmember banks: I am discussing this briefly, in the order in which the proposals appear in the bill—the admission of insured nonmember banks is in section 202. It is recognized that many of the nonmember banks could not readily qualify as members of the Reserve System, and that a very great hardship and injustice would be imposed upon them, if they were required to become members of the Federal Reserve System under the present legislation, and under the rules and regulations for membership. It is, therefore, proposed that the Federal Reserve Board should have authority to waive the capital requirements.

I suggested yesterday, in connection with this particular feature of the bill, that the authority for the Federal Reserve Board to waive the capital requirements for admission of insured banks into the System, prior to July 1, 1937, when State banks are required to be members of the Reserve System in order to be insured, might be broadened, so as to authorize the Board to waive not only the capital requirements, but all requirements, and to permit existing banks to continue permanently with their present capital, provided it is adequate in relation to their liabilities.

I think it is desirable to have unification of the banking system, and I recognize that possibly the most likely way of getting it is through all banks becoming members of the Federal Reserve System.

In many instances, the capital of nonmember banks, is less than the minimum amount required—$50,000, and their volume of business is such that they do not require and cannot possibly use and support a capital of $50,000 with an adequate surplus, which is also desirable.

It is also recognized that certain of the rules and regulations for membership would make it very difficult for many banks to qualify under those rules and regulations; and it is, therefore, the desire of the Federal Reserve Board to so modify the law and its rules and regulations as to make it possible, under reasonable conditions, for nonmember banks to get the benefits of membership. I believe those benefits are very real. Particularly would that be true if the present law is amended in some of the particulars as provided for in the proposed bill. I refer to the change in the present eligibility features; also the recognition of the desirability of using the savings and time funds in longer term lending, or in the real estate loan field. These provisions would give to many of the nonmember State banks the support that otherwise would not be available to them, if it were possible for them to continue to operate as nonmember banks.

In section 203, it is recognized that it would be desirable to change the present language with reference to the qualifications for membership on the Board, as a recognition of the fact that the functions and duties of the Federal Reserve Board are such as to make it a body representing the Nation, rather than any group or combination of groups. In recognition of that, it is provided in the bill that future appointive members of the Board shall be men who are qualified by education or experience or both to participate in the formulation of economic and monetary policies, which seems to me to be the central and most important function of the Federal Reserve Board.

It is recognized that membership on the Federal Reserve Board is one of the most important, responsible, and powerful positions of the Nation. It is, therefore, believed that the position should attract, by reason of its importance and responsibility, the best qualified men in the Nation to deal with these monetary and economic problems. It is felt that the men on the Board should be independent and, therefore, it is recognized that their compensation should be such as to enable them, without having to have an independent, private income, to live in Washington in the manner that their position would require. It is proposed that the compensation for future appointive members be increased to $15,000 per year, the salary now received by members of the Cabinet. Their salary was originally equal to that of Cabinet members, but later the Cabinet salaries were increased. The proposal is to reestablish this equality. It is also proposed that there be a pension or retirement provision, so that members of the Board who have severed their outside connections and serve in this position, will not feel a dependency that otherwise they may feel.

I do not believe the pension provision in the bill fully and adequately meets the situation. It provides that any of the present members may retire at the age of 70, and that future appointive members must retire at the age of 70. It also provides that, upon retirement, they will receive a pension of $12,000 per year, when they have served the full period of 12 years, or more, and a proportionate amount when they have served not less than 5 years. It would seem to me that, in order to attract the ablest men obtainable for this position, to make them willing to accept positions on this Board as careers, and to sever all other connections, a pension should be provided for future appointive members, irrespective of the age at which their terms may expire.

It seems to me that this would have the effect of inducing these men to accept positions of this sort during the most active and remunerative period of their lives; otherwise, they might not be willing to accept.

It does not seem fair to ask a person, of the caliber that Board members should be, to accept a position and serve for a 12-year term—we will say from the ages of 48 to 60—and at the end of the period of 12 years, if not reappointed, to be obliged to go out and undertake to reestablish connections, which were severed and neglected for a period of 12 years.

It would seem to me that, in the public interest, it would be well to provide that, if a member is not reappointed, he would receive the full pension, if he has served a full term or longer; but if he is offered a reappointment and prefers not to serve, of course he should not be given a pension. I believe that would make for greater independence on the part of the members of the Board.

As to the term of the office of Governor of the Board: There has been a good deal said about the provision in the proposed legislation that the term of the Governor as a member of the Board shall expire when he is no longer designated as the Governor by the President.

The present law provides that the Governor shall be designated by the President to serve at his pleasure, the designation being from among the Federal Reserve Board members. As a practical matter, when the Governor is no longer designated as Governor by the President, it is because the President is desirous of having someone else serve as Governor.

Mr. GOLDSBOROUGH. As I understand it, you approve of that provision?

Mr. ECCLES. What is that?

Mr. GOLDSBOROUGH. You approve the provision allowing the President to remove the Governor, whenever he sees fit?

Mr. ECCLES. Well, I have no objection to it. I think that, as a practical matter, it is reasonable. In some of the other central banks there are similar provisions with reference to the executive heads of the banks.

It seems to me that an administration is charged, when it goes into power, with the economic and social problems of the Nation. Politics are nothing more or less than dealing with economic and social problems. It seems to me that it would be extremely difficult for any administration to be able to succeed and intelligently deal with them entirely apart from the money system. There must be a liaison between the administration and the money system—a responsive relationship. That does not necessarily mean political control in the sense that it is often thought of.

Does that answer your question, Mr. Goldsborough?

Mr. GOLDSBOROUGH. Yes; from your standpoint, I think it does.

Mr. ECCLES. Referring again to the term of office——

The CHAIRMAN. Suppose you let me ask a question right there: Is not the practical situation such that the administration has that power and may exercise it, but under this bill there will be a technical recognition of that power and a definite fixing of responsibility, at least within limitations?

Mr. ECCLES. Well, the only change—I do not think it will be material, but the only change in this bill over the present legislation is that when the Governor is no longer designated as Governor by the President, his term as a member of the Board will expire, whereas, at the present, when he is no longer designated as Governor, his term as a member does not expire. This means that if he is no longer designated as Governor and he does not resign as a member, there will be no vacancy on the Board to which the President could appoint the person he desires to designate as Governor, unless he designates an existing member of the Board. There is this disadvantage under the existing law: When a member is no longer designated as Governor and resigns as a member—which is the only thing that a Governor could do, and a person who would not do that would certainly not be a proper person to act as Governor—he is precluded for a period of 2 years from entering the banking field. That is a deterrent in the present law to a man accepting that office. If he is taken from the banking field, he is required to sever all connections with the banking business for an indefinite time, that is, for as long as he is designated as Governor, and that may be for 2 or 3 or 4 years. When he is no longer designated as Governor, he resigns as a member; and, if he has not served out his term as a member, he is precluded for 2 years afterward from entering the banking field again.

If he has served out his term as member, he may immediately enter the private field.

Now, what I should like to propose here is that the Governor's term as a member do not expire when he is no longer designated as Governor; that is, leave the law as it is with reference to his term as a member, but provide that, if he chooses to resign as a member when he is no longer designated as Governor, his term as a member be considered to have been fulfilled.

Mr. HOLLISTER. That is not what this new statute says, is it?

Mr. ECCLES. No; I am offering this as a suggested change: Whereas the bill provides that he shall automatically cease to be a member of the Board when he is no longer designated as Governor, I am suggesting that it be changed so as to provide that, if he does not choose to continue to serve as a member when he is no longer designated as Governor, he would be free to enter the banking field, without taking a 2-year vacation.

Mr. GOLDSBOROUGH. Your view is that they should resign voluntarily, and the 2-year application should apply; but if they are removed as Governor and they see fit——

Mr. ECCLES. It should not apply.

Mr. GOLDSBOROUGH. It should not apply?

Mr. ECCLES. That is right.

Mr. GOLDSBOROUGH. That seems to me to be sound.

Mr. ECCLES. It seems to be fair and will remove a deterrent; and it seems to me that it will accomplish the object of making it a more attractive position in the future than it has been in the past.

Mr. HOLLISTER. Would it not also attract something else, or accomplish something else? This is drafted to give the President the opportunity, if he cares to do so, to make a clean sweep, to completely clean up the whole Federal Reserve Board in a few days, does it not?

Mr. ECCLES. Well, of course, I think that if we are going to conceive of a President that would resort to what would be considered sharp practice, he would possibly have more direct ways of cleaning it up than that. I think a President that would resort to that sort of thing would possibly have other ways of meeting the situation.

Mr. HOLLISTER. Presidents have in the past, unfortunately, done things that some of us would not back up; but, as a matter of fact, as the bill is drafted, it permits the President, if he cares to, to remove successively every member of the Federal Reserve Board, appoint him as Governor, and undesignate him; whereupon, he immediately retires from the Board?

Mr. ECCLES. Yes; that is correct.

Mr. HOLLISTER. So the suggestion you make would at least eliminate the possibility of that happening, when we had a man in the White House that might adopt such sharp practices?

Mr. ECCLES. Yes.

Mr. CROSS. Mr. Chairman, may I make a suggestion as a member of the committee?

The CHAIRMAN. Certainly.

Mr. CROSS. I would like to make this suggestion: That Mr. Eccles be permitted to go ahead and finish his statement; and then that he submit the amendments that he would suggest; and then when he gets through with his statement, just as Mr. Goldsborough suggested the other day, each member of the committee be given a chance to ask questions, because every member has many questions, or a number of questions, on this section that they would like to ask. I am afraid that, if we start like this, we will never finish or get anywhere. That is my suggestion.

The CHAIRMAN. Well, I certainly expect that every member of the committee will have the opportunity you refer to, and I will recognize members in an orderly way, so that every member will be allowed to ask questions.

Mr. CROSS. The point is, we will not have a coordinated idea of this by going in and out, and I think it is much better to let him finish, and then later on let him bring his proposed amendments to the bill, and then we can take up those amendments and let him discuss those amendments in a much more uniform way, and every member will get a grasp of the bill. That seems to me to be the best way to proceed.

The CHAIRMAN. All right, Mr. Eccles, you may proceed.

Mr. ECCLES. Assignment of duties: There is no controversy over that question. It is just a practical way of enabling the Board to meet the problems of increased responsibility that are placed upon them by delegating to others many of the routine duties, so long as they do not involve questions of policy.

Open-market operations: Inasmuch as this was covered quite fully in my statement yesterday, I do not believe that I can add very much to it. There will likely be a good many questions that will develop in connection with that, because, under that heading, the whole question of monetary control heads up.

I explained yesterday the way the open-market operation is now organized, the manner in which the bill provides for it to be operated, and the amendments suggested to the proposals in the bill.

Eligibility for discount: The eligibility requirements of the present law do not seem to me to meet the changed conditions that we now have in the Nation, compared with the conditions that existed at the time the Federal Reserve was established. The amount of eligible paper available now held by banks is a very small part of the total resources of the banks. Even in 1929 it was only slightly over 12 percent of their loans and investments, and today I understand it is less than 8 percent. Approximately $2,000,000,000 is the total amount of the paper which would be considered eligible by the banks themselves. It was found, when the depression commenced and as it continued, that the banks did not have eligible paper to meet their shrinking deposits, brought about by the general liquidation of bank loans and by hoarding; and that, in order to avoid closing they were forced to sell such bonds as they had upon the market. These bonds were considered, at one time, to be secondary reserves, because they were listed. Banks also brought pressure upon all loans which came due during the period, and were forced to refuse new credit, feeling, of course, that they had to have as large cash reserves as possible and be as liquid as possible. They were bringing pressure to collect loans that came due, and to sell the securities that they had, wherever they could do so without taking too large a loss. That attitude on the part of the banks throughout the Nation was largely due, it seems to me, to the fact that they did not have eligible paper in sufficient quantities to meet the demand and could not get help at the Federal Reserve banks unless the paper was eligible.

Therefore, in an effort and under pressure to get liquidity, they froze themselves so completely that they finally closed the entire banking structure. So it was found out that, in the final analysis, in a depression, there is no liquidity, except that liquidity which can be created by the Federal Reserve or the central bank through its power of issue.

This was finally recognized when great damage had been done, when thousands of banks had been closed unnecessarily, when millions of individuals and institutions had been forced to the wall through the lack of available credit, or through pressure to pay existing debts. Millions of depositors lost hundreds of millions of dollars as the result of those closings.

We finally recognized that we did not have to have eligible paper and we did not have to back our currency with gold or eligible paper or even with Government bonds. We finally recognized that, in order to get the banks open, we could take any sound asset into the Reserve bank and issue Federal Reserve bank notes. When that happened nobody wanted their money, the runs stopped, and liquidation stopped to a very great extent. Certainly, the pressure was very greatly relieved.

Now it seems to me that it is only being a realist to recognize that the Reserve banks, subject to rules and regulations made by the Reserve Board, should have the power to meet emergencies, should have the power to loan to member banks upon sound assets, rather than see the banks close, or rather than see unnecessarily drastic liquidation forced upon the community.

This provision does not mean inflation. Before the banks today, as a whole, would have any occasion to use the Reserve System, they would have to extend billions and billions and billions of dollars of credit, because of the excess reserve position that they now occupy. But, if the provision is there, it will make the banks feel altogether different about extending credit today. It will make them recognize that they do not have to have 90-day or 6-month paper in order to make loans, when that type of demand for credit does not exist to more than a very limited extent.

This, to my mind, is one of the most important features of the legislation at the present time. It will tend to do more toward inducing recovery through credit expansion than any other feature of the bill. The banking system must be made, to provide the money and credit required, if it is going to justify its existence. At the present time, that is largely provided by the Government. The banking system, the commercial banking system——

Mr. GOLDSBOROUGH. You say it is being provided by the Government?

Mr. ECCLES. To a very large extent.

Mr. GOLDSBOROUGH. We were under the impression that the Government borrowed the money that it is now providing, from the banks; is that not correct?

Mr. ECCLES. That is very true. The banks are willing to extend credit on Government bonds.

Mr. GOLDSBOROUGH. We have provided the banks with $13,000,000,000, about, have we not?

Mr. ECCLES. Well, I do not know the exact amount, but——

Mr. GOLDSBOROUGH. That is an approximation.

Mr. ECCLES. But whatever amount of Government bonds the banks have purchased—it is not $13,000,000,000, but, including what the Federal Reserve System has, I think it is nearly $13,000,000,000—the Government is doing the lending through the various Government lending agencies, such as the Home Owners' Loan Corporation, the Farm Credit Administration, and the Reconstruction Finance Corporation. Those are the three most important agencies and, of course, we know they have put out billions and billions of dollars, and the banks have largely taken Government bonds and bonds guaranteed by the Government, and the Government, in substitution, has taken the loans of the individual and the corporations. So that it has been a process of the banks liquidating their private loans, and the Government taking them over, and the banks providing the funds to take Government bonds or bonds guaranteed by the Government. And, of course, if continued, it seems to me that the banks are going to have very great difficulty in justifying their existence.

Mr. GOLDSBOROUGH. When they can only live by the Government furnishing nearly one billion dollars a year in interest, which they do not earn, it seems to me your statement is worthy of very serious consideration.

Mr. ECCLES. I recognize that, and I have also told many of the banks that the provisions of this legislation with reference to this eligibility feature, and with reference to this real-estate loan feature, are to give them an opportunity to utilize their funds in the direct field of lending and get the Government out. Otherwise they will find that the Government will have taken over the banking business, not because the Government wanted to, but because the banks forced it to.

Purchase of United States guaranteed obligations: It is provided that obligations guaranteed by the United States Government should be put on the same basis as direct obligations. There seems to me to be no justification for discrimination; that they should be eligible for purchase by the Reserve banks without regard to their maturity, in the same manner that direct obligations of the Government are eligible for purchase by the Federal Reserve banks.

Collateral for Federal Reserve notes: It is provided that the position of Federal Reserve agent as such shall be eliminated and that the position of chairman of the Federal Reserve bank shall be combined with that of the governor. The Federal Reserve agent acts as a trustee, holding the collateral against which Federal Reserve notes are issued, at least 40 percent in gold certificates and the balance in eligible paper or Government bonds, or both. It was thought, originally, that the amount of currency outstanding at any time was influenced or regulated by the amount of commercial paper, which represents the activity or the volume of trade or business. It has been found that there is very little relationship between the volume of Federal Reserve notes and the volume of commercial borrowing. Of course, that is due to the fact that currency, as such, plays so small a part in our money system and that bank credit or deposit currency plays a major role. The amount of currency or Federal Reserve notes outstanding will depend upon the demand for currency by member banks. The member banks discount or borrow from the Reserve banks in order to maintain their required reserve balances with the Reserve banks. Member banks draw currency to meet the demands of their customers. It is not felt that the collateral put up back of the Reserve notes in any way restricts the use of currency. It is not felt that collateral adds anything to their security. They are now guaranteed by the United States Government; they are a first lien on all the assets of the Reserve banks. Whenever notes are issued or deposits created by the Reserve banks, there are assets to offset the liabilities of the Reserve banks, whether the liabilities consist of notes or of deposits of their member banks.

There would seem to be no more reason to secure notes which they issue than to secure deposit liabilities to their member banks. The Reserve banks are required to hold gold certificates equal to not less than 40 percent of their notes outstanding, and gold certificates or lawful money of not less than 35 percent of their deposit liability and——

Mr. Wolcott. Gold certificates?

Mr. Eccles. Well, of course, they have no gold. There is no proposal to change that. The assets of the banks, on the other side, consist of gold certificates and other money that they may hold, and Government bonds and bills or rediscounts.

Mr. Hancock. Could you properly call those notes "asset currency"?

Mr. Eccles. What is that?

Mr. Hancock. Could you properly call those notes "asset currency"?

Mr. Eccles. I do not just understand what you mean.

Mr. Hancock. I do not want to begin questioning you, but right on that point you made the statement that it was not necessary that notes have any particular banking value.

Mr. Eccles. Yes.

Mr. Hancock. In that they constitute a lien against all of the assets of the banks.

Mr. Eccles. That is right.

Mr. Hancock. Now, would you consider such notes as asset currency?

Mr. Eccles. Well, they are the obligations of the banks that issue them and are guaranteed by the United States Government. They are not asset currency, in that they are not backed specifically by this or that particular asset or assets, except to the extent that there is at least 40 percent of gold certificates held, and there would be other certificates back of them. The liabilities of the bank would be offset by its assets. So, to that extent, there are assets in the form of gold certificates, Government bonds, or loans and discounts, back of all the notes issued, just as there are back of all of the deposits of the bank. The value back of the Federal Reserve notes is determined by the assets of the Reserve banks. In 1932 it was found impractical to restrict the issue of these notes as they were restricted, when gold was leaving the country very rapidly and when the banks held very limited amounts of commercial paper. The requirements of the law had to be suspended in 1932, and Government bonds had to be accepted as substitutes for commercial paper as the basis for issuing notes, in order to release the excess amount of gold that had to be held in the absence of commercial paper. So it was found that the restriction imposed at the time, and the only time when the provisions of the law were tested at all, they had to be suspended.

The CHAIRMAN. It might be well to remember definitely the date of that action.

Mr. ECCLES. Well, you probably remember it. It was in 1932, February 27, 1932.

Reserve requirements: The Federal Reserve Act, as amended by the act of May 12, 1933, provides that, with the consent of the President, when an emergency is declared to exist, the Federal Reserve Board has power to change the reserve requirements of member banks. It is proposed to recognize this emergency provision as a permanent provision and to give to the Board the power to change reserve requirements, without declaring that an emergency exists and without the approval of the President. This is a function of monetary control almost equal in importance to open-market operations, and it is felt to be necessary that the Board have this power, particularly in order to control an inflationary condition, should one develop.

It is conceivable that the reserves of the member banks may be greatly in excess of the amount of Government bonds and paper held by the Reserve banks. The sale of those securities in the market would not be sufficient to absorb the excess reserves; and therefore, the increase of reserve requirements would come into use as a means of controlling an inflation of credit. It would be expected to be used only as a method secondary to open-market operations. Changes in reserve requirements would be used at a time when open-market operations failed to meet the situation.

Mr. CROSS. I might suggest that I remember the conditions that existed in the world, the speculation on the stock exchange; do you think it would be wise to have a provision so that you could designate certain particular banks, where they had increased their reserve, rather than apply to all banks, everywhere, at any time?

Mr. ECCLES. I do not believe so. I think money is too much like water; it seeks a place where it can——

Mr. FORD. Seeks it own level?

Mr. ECCLES. Yes; it seeks a level, and of course that level is based upon the return it can get.

We have proposed here that changes in reserve requirements might be a pplied to two classes of cities: Central reserve and reserve cities in one class and country banking areas in the other. It is conceivable that different reserve requirements could be applied to the reserve cities, if that is where speculation was going on and where the excess of reserve was, which is usually the case. There is an element of time in money seeking its level. Just what it is, I do not know that anybody can say. But increases in reserves might be applied first to the reserve cities and then later to the other areas, if it seems to be necessary, rather than to apply them at the same time universally. I do not believe that you could consider it beyond that. I do not believe it would be practicable to apply it to individual banks. The Federal Reserve Board has the power now to regulate margin requirements on collateral and brokers' loans, which is one of the most effective instruments of speculation control, I think, now available. I believe that, had it been available in 1928 and 1929, it would have possibly been helpful in controlling or restricting the speculative orgy that we went through.

The CHAIRMAN. Governor Eccles, the House has been in session for a little while, and there are matters that require the attendance of Members, and I am sure you will be glad to desist until tomorrow, anyway. We will adjourn until 10.30 o'clock tomorrow morning, and we expect to have the pleasure of having you back again with us.

(Whereupon the committee recessed until 10.30 a. m., tomorrow, Wednesday, March 6, 1935.)

BANKING ACT OF 1935

House of Representatives,
Committee on Banking and Currency,
Washington, D. C., Wednesday, March 6, 1935.

The committee met at 10:30 a. m., Hon. Henry B. Steagall (chairman) presiding.

The Chairman. Gentlemen, we will come to order. Some of us have to appear before the Committee on Rules this morning, and I have to leave in a few minutes. I am going to suggest that, unless Governor Eccles decides to proceed further without interruption, that the committee will now proceed to discuss with him title II of the bill. If you desire further time without interruption, we shall be glad for you to have it. We do not want to hurry you in the least. It is our desire to permit you to have ample time to express your views, in your own way, fully, after which the committee, of course, will desire to interrogate you.

Mr. Eccles. I have finished my principal statement.

Mr. Kopplemann. May I ask a question?

The Chairman. Certainly.

Mr. Kopplemann. There may be some questions that I want to ask on title II, but I am not prepared to do that today. I suppose that Governor Eccles will be here tomorrow?

The Chairman. Yes; you will have ample opportunity to do that. I am taking it for granted, of course, that that will be done, if it is necessary to meet your convenience.

Mr. Eccles. I finished the discussion yesterday of the proposals, with the exception of the one relative to the real-estate loans.

The Chairman. The committee will be glad to hear you further on that provision, or any other, without interruption, if you so desire.

Mr. Eccles. I finished them all with the exception of that yesterday, and it seems to me to be one of the important issues, and it might save time to say something about that.

The proposal is to amend the act to permit the national banks, as well as other member banks, to make first-mortgage loans on improved real estate for a period up to 20 years; that is, if the loans are amortized so that they would be paid off over that period of time; to reduce the period from 5 years to 3 years in cases where the loans are not amortized, and to increase the amount that they can loan from 50 to 60 percent of the value of the real estate.

It is also proposed to increase the amount, the total amount of bank funds that can be loaned, from 50 percent of time funds of a bank up to 60 percent, including in the amount loaned, however, other real estate excepting the banking houses.

You recall that I suggested yesterday that the proposed bill be amended, if we think it advisable to amend it, so as to give the Federal Reserve Board the power to determine the conditions of real-estate loans by regulation, the reason for this being that to try to put into the statute a limitation of 60 percent of the amount of savings will work a very great hardship on many State banks. We find that some of the State member banks and many of the State nonmember banks already have in excess of 60 percent of their time funds in real-estate loans. It would seem, therefore, that they would be required to cease making real-estate loans and to liquidate the loans they had as they fell due.

Also, it seems that to try to fix in a bill or in a statute a provision permitting 75 percent of the appraised value of property might not be desirable. It is felt that the situation would be better met if the Board had the power to fix the rules and regulations to meet this matter; that it would make it much more flexible than if it is put in the statute.

The member banks of the country have about $10,000,000,000 of savings or time funds. The New England area and the New York area are largely served by mutual savings banks. More than 50 percent of the deposits of the banks, outside of that area, consist of savings deposits. These funds are equivalent to the funds that the mutual savings banks are receiving from the people in the area that they serve. The banks are required to pay interest on these time funds. The maximum rate of interest at the present time is fixed at 2½ percent. It is impossible for these banks to pay that interest and to loan these funds on short-time paper.

In the first place, there is not available a sufficient amount of short-time commercial loans to utilize more than a fraction of the demand deposits, much less the savings deposits; and as a result the banks hold a very large volume of idle funds.

There has been no restriction imposed upon banks with reference to their investments in long-term bonds. They have been permitted not only to invest all of their savings funds but as much of their commercial funds as they desire, in long-term bonds, railroad bonds, utility bonds, foreign bonds, and industrial bonds. I cannot see that it is so much more desirable to permit banks to invest in long-term listed bonds than it is to loan their funds on improved real estate on an amortized basis in their local communities.

The fact that bonds were listed and, therefore, supposed to be marketable, was considered a justification for the investment of funds in bonds as compared with the investment in real estate. The depression proved that the ready market for bonds was only there at prices that bankrupted the banks, if they were forced to sell in the market that existed. More banks became insolvent as a result of the depreciation of their bond accounts than as the result of their real-estate loans. The fact that bonds were listed and were greatly depreciated put the banks, when the examiners came into a condition of insolvency, because of the difference between the quoted market price and the cost of the bonds; whereas in the case of real-estate loans it was not expected that there should be a ready market for them, and so long as they were not in default, they were considered to have the value of the amount of the loan. It was the depreciation shown on the bc ls and stocks, because of the quoted market, that impaired and ir uany cases wiped out the capital of the banks.

It seems to me that, if we want to be so restrictive in the matter of real-estate loans, because they are long-term investments of funds which are likely to be drawn out on demand, we should also be restrictive with reference to the investment of funds in long-term bonds. I believe that the banks should be permitted to invest their funds in long-term bonds and in long-term amortized mortgages. Particularly is that true with reference to their savings or time funds. The reason is that otherwise they have no way to use their funds, except to buy Government bonds, or bonds guaranteed by the Government.

Mr. GOLDSBOROUGH. You mean you think it is the duty of society to support the banks?

Mr. ECCLES. No; I am not saying that. I am talking about the condition that exists.

Mr. GOLDSBOROUGH. As far as society is concerned, it is interested in banks only insofar as the banks are useful to society?

Mr. ECCLES. That is correct. Either the banks holding these $10,000,000,000 of time funds must be prepared to lose those funds to the savings and loan associations, to mutual savings banks, or to others, or they must be put in a position to use the time funds in the long-term investment field.

I am convinced that it is not possible for the majority of banks in this country to operate with demand deposits alone. The volume of these funds is not adequate for profitable operation except in the larger institutions, and to take time deposits away from the banking system would reduce the size of many banks to the point where they would be unable to exist.

If our private banking system is expected to provide credit in other ways besides buying Government obligations or obligations guaranteed by the Government, then it seems to me that some of the provisions of this proposed legislation are essential, the one with reference to eligibility and the one with reference to real-estate loans.

There is nothing new about national banks loaning on real estate, since they have made such loans for 20 years. They have loaned, however, for a limited period of 5 years on a straight mortgage, which makes for a much more unsound loan than a longer-term amortized loan.

I believe that covers what I have to say, Mr. Goldsborough, and I will be glad to answer any questions.

Mr. GOLDSBOROUGH. Suppose we begin the regular examination. Mr. Cavicchia has a question.

Mr. CAVICCHIA. Mr. Chairman, I think this would be the proper place in the record for the Governor to tell us, if he knows, to what amount the mortgages of national banks are held or were held in 1933 or today, if he knows.

Mr. ECCLES. I do not know off-hand, but I have it here. On October 17, 1934, under the law in effect, the national banks had authority to lend up to $3,400,000,000. Under the new proposal the limit would be about $4,400,000,000 for national banks and about

$6,800,000,000 for all banks. The total amount of actual loans on real estate by all member banks at the end of 1934 was $2,273,000,000.

Mr. GOLDSBOROUGH. Governor Eccles, you wanted to say something else?

Mr. ECCLES. I was going to say that in connection with my discussion of the provisions of the bill I have suggested certain proposed amendments or revisions for your consideration. I would like, in closing, to call those to your attention in the order in which they were suggested.

Mr. GOLDSBOROUGH. As this hearing naturally will be protracted, we are not going to hurry you, and you may do so.

Mr. ECCLES. In section 201, the first section discussed, it was suggested that the governors and chairmen of the Federal Reserve banks be approved by the Federal Reserve Board every 3 years rather than annually so that their terms as governors and chairmen would coincide with their terms as class C directors.

Mr. GOLDSBOROUGH. What page is that on, please?

Mr. ECCLES. That is section 201. That is the one with reference to combining the offices of chairman and governor.

Mr. WILLIAMS. On page 39 of the bill.

Mr. ECCLES. This, as you will notice, is a slight modification, and it is just offered as a suggestion.

There has been some criticism about the necessity of approving the appointment of the governors each year, whereas they will be appointed as class C directors for 3 years. I personally can see no necessity of approving their appointments every year and feel that it is well to consider the suggestion that they be approved every 3 years instead.

Section 202: On the question of admitting insured nonmember banks to the Federal Reserve System, the suggestion is that the Board have authority to waive not only the capital requirements but all other requirements for admission, and that the Board be permitted to admit existing banks to permanent membership, without requiring an increase in capital, provided that their capital funds are adequate in relation to their liabilities.

Mr. GOLDSBOROUGH. When you refer to the capital, you mean the capital and surplus combined?

Mr. ECCLES. What is that?

Mr. GOLDSBOROUGH. You mean the capital and surplus combined?

Mr. ECCLES. The law requires $50,000 capital at the present time, and many banks——

Mr. GOLDSBOROUGH. I know, but I think you say, "Providing its capital is adequate"?

Mr. ECCLES. No; I would think you should take the capital and surplus in determining the adequacy.

Section 303: The suggested modification of the pension provision is for the purpose of giving Board members a greater degree of independence. It has been suggested that each member of the Board, regardless of age, who has served as long as 5 years, whose term expires and who is not reappointed, shall be entitled to a pension on the same basis as though he were retiring at the age of 70. I discussed that to some extent yesterday.

Section 203: It has been suggested also that a Governor of the Federal Reserve Board, who is not redesignated by the President may, if he chooses, continue his membership on the Federal Reserve Board. That is the way the law is now, and the new bill that is being considered, as you will recall, provides that his term as member of the Board shall cease when he is no longer designated as Governor. It has been suggested that, as a result of that, the President could designate each member of the Board and then no longer designate him, and finally create a new Board completely. So, in order to eliminate that criticism, this is the suggested amendment: That the Governor could continue as a member of the Board even if he is not designated as Governor; but that if he resigns from the Board upon not being redesignated, it would be considered that he had served out his term and he would not be precluded, by reason of having resigned under those circumstances, from entering business for a period of 2 years.

In section 205, it is suggested that authority over open-market operations be vested in the Federal Reserve Board, but that there be created a committee of 5 governors of the Federal Reserve banks selected by the 12 governors of the Federal Reserve banks, and that the Board be required to consult this committee before adopting an open-market policy, a change in the discount rates, or a change in member bank reserve requirements.

Mr. GOLDSBOROUGH. Is there any interpretation in your suggested amendment as to what the consultation would consist of? Expressing it another way, would the Board be bound to accept the suggestion of these five men, or any one of them?

Mr. ECCLES. No. It is a question of giving the governors a hearing and making a record before the Board can act; but the Board would have the final responsibility for the action.

Mr. GOLDSBOROUGH. That is the intent, but I am not sure it is entirely clear. Of course, that can be clarified.

Mr. ECCLES. Yes; that is the intent. The Board would be charged with the responsibility and they would have the power to initiate, but before taking action they would be required to advise with and get an expression of the views of the committee of the governors, or the governors could initiate and come to the Board and make their recommendations for the consideration of the Board.

Mr. FORD. Should there be a time limitation on how long you have to wait for that consultation?

Mr. ECCLES. Well, I would provide that, of course, the Board should be able to make rules with reference to that.

Section 209: It is suggested that the Board should not have the power to change the reserve requirements by Federal Reserve districts. I discussed that, I think, to some extent yesterday. It has been suggested, further, that the member banks be classified in the two groups, one comprising member banks in the central reserve and reserve cities, and the other all other member banks. Changes in the reserve requirements, therefore, would have to be either for the country as a whole, or for the financial centers, as against the country districts.

Section 210: Real-estate loans: It has been suggested that the conditions on which real-estate loans may be granted by member banks be left to the discretion of the Federal Reserve Board, to be determined by regulations. I see no objection to accepting also some geographical limitation as to where loans could be made, that is, some specified distance from the banking houses. Of course, there is no limitation as to the field where banks can loan funds on bonds, but there seems to be a good deal of opposition to the elimination of the geographical limitation on real-estate loans. I do not believe it is of sufficient importance to have any disagreement over.

Well, now, those are the suggested modifications.

Mr. FORD. Just one word on that geographical limitation: In cities where the Federal Reserve banks to whom the various banks have to go for these loans, if the geographical limitation is put in there, very often there is very keen competition between cities and the city in which the Board is located, and if it were limited, it might mitigate against another city that did not have a bank, as to the character of loans that they would be willing to discount. With the geographical limitation, I think, in many instances, it might have a very bad effect.

Mr. ECCLES. You mean in the case of real-estate loans?

Mr. FORD. Yes, sir.

Mr. ECCLES. Well, I do not just get the point of your question.

Mr. FORD. Let me illustrate it in another way: Let us say that the main branch of the Federal Reserve is at San Francisco. Well, now, the geographical limitation, for instance, leaves the city of San Diego out of that limitation; and if there were some loans coming in from there, and there happened to be competition, for instance, in water transportation between those two points, and somebody on that Board was anxious to work a little against San Diego, it might be possible and something like that might come up, because it has come up in other things.

Mr. ECCLES. Well, in the case of San Diego, in that case San Diego would discount with the Los Angeles branch.

Mr. FORD. That limitation would not touch the branches?

Mr. ECCLES. The limitation is a mileage limitation from the bank that makes the loan, the idea being that the bank in an area should loan funds in the area in which it is acquainted, where the officers can personally be informed as to the property upon which they are lending; whereas, if there is no geographical limitation, the funds may be loaned in far-removed areas, a thousand or two thousand miles away, as the case may be.

Mr. FORD. If it applies to branches, that is all right.

Mr. ECCLES. The advantage of taking the limitation off is this: That in an area that has a surplus of funds beyond the demand for real-estate loans, it could invest those funds through some correspondent institution where there is a shortage of real-estate money, just as our insurance companies in New York and other points loan money over the United States and building and loan companies have loaned in a more or less wide area, and as the mutual banks loan in far-removed areas.

Mr. GOLDSBOROUGH. Mr. Hancock, you may proceed, if you desire.

Mr. HANCOCK. Mr. Chairman, I have listened with intense interest to the very able and enlightening statement made by the Governor of the Federal Reserve Board with respect to the purpose and philosophy of this important measure, and to his detailed explanation of its mechanics. It occurs to me, however, that since it is such an important and far-reaching measure and is somewhat intricate, that the committee should arrange immediately to have the Governor's testimony reduced to writing so that we may have a chance to fully analyze and digest it before we go into the questioning of the Governor. I hope the clerk will arrange to have this done at once.

I am not so much concerned with the mechanics as I am the purpose and philosophy of the bill. How it will be administered is, of course, vitally important.

I want to ask the Governor what is the difference between this measure and an outright central bank?

Mr. ECCLES. Well, I do not know just what you mean by "central bank." You mean by that a bank that is owned by the Government, and a bank with branches?

Mr. HANCOCK. I would like to have an explanation of that, and then I will ask you another question.

Mr. ECCLES. There are a good many different kinds of central banks and——

Mr. HANCOCK. Well, let me ask you this, Governor: What would be the practical difference between the system proposed herein and the Federal monetary authority that the committee last year studied, conducted hearings on, and considered?

Mr. ECCLES. I am not familiar with what the committee worked on last year. I could not give you a comparison between Federal Reserve operations and what was proposed under that bill, because I am not familiar with it.

Mr. HANCOCK. Well, briefly, here is what the Federal monetary authority undertook to do: It undertook to set up what you might term a supreme court of finance insulated against political and commercial banking domination, and vested in that supreme court of finance or authority the sole note-issuing power of the Nation. It would have owned and controlled all of the gold, all of the metallic base; and it would have had the right to control the open-market operations through the sale and purchase of Governments, the control of the rediscount rate, and other essential powers to control or regulate the volume and cost of money for the national welfare.

Mr. ECCLES. Speaking of the central bank, the Federal Reserve System has always been expected to perform certain functions of a central bank. It was set up on the basis of a certain regional autonomy, due, I suppose, in part, to the opposition to centralization in this country at the time the Federal Reserve System was set up, and due, also, in part, to the size of the country and the different economic conditions that existed in the different regions. The Reserve Board was set up as a coordinating agency for these 12 banks, which have 25 branches.

The proposed bill in no way changes the physical structure. The ownership of the Federal Reserve bank is left with the member banks. In most of the countries of the world, the central bank is a privately owned institution. Instead of being owned by the member banks, it is owned by the public.

There is no change being made in the number of directors, 9 directors, and the majority of them are selected by the stockholders of the member banks—6 of the 9. A limitation is being put, however, upon the terms of these directors. The general structure of the bank is not being changed.

It is proposed, however, that the appointments of governors should be approved by the Board. That is so that they would be in a more direct relationship, a more responsive relationship to the Federal Reserve Board, so that the Board's coordination of the system would be through the governor, rather than through the chairman and agent. This is the reason for the proposed combination of the offices of Governor and Chairman. Such coordination would be further effected through the Board's control over open-market operations and discount rates. The Board today approves the discount rates. There is no change in the matter of the discount rates proposed in the bill, but there is a change regarding the open-market operations.

Mr. HANCOCK. And that is the heart of the bill, is it not?

Mr. ECCLES. Well, it is the most important feature and——

Mr. HANCOCK. That is the main method or means by which you control the supply of money?

Mr. ECCLES. Well, the question of reserve requirements is also a feature secondary——

Mr. HANCOCK. Secondary?

Mr. ECCLES. I think secondary to the other features.

Mr. HANCOCK. But the open-market operation is the primary and most effective feature?

Mr. ECCLES. That is right. The other is secondary. The open market is the primary feature.

Mr. HANCOCK. And under the terms of this bill, the open-market operations are vested entirely in a Government board?

Mr. ECCLES. No; vested in the Federal Reserve Board under this bill if changed in the manner which has been suggested.

Mr. HANCOCK. Yes, but under this bill, that Board is appointed by the President and confirmed by the Senate?

Mr. ECCLES. That is right, for terms of 12 years, and the open-market power is vested in the Board. Today the Board has a veto power over open-market policy. The governors have an open-market committee. The 12 governors elect a committee of 5, and that committee is a committee charged with the responsibility for the initiation of open-market operations. The Federal Reserve Board either approves or disapproves or induces them to modify their program; but the Board cannot initiate. And then, if the policy is initiated by the open-market committee and is approved by the Board, the Board is not in position to require that the banks carry out the policy. So it is proposed in this bill to place the authority and responsibility in a small body, and the Board——

Mr. HANCOCK. Under the bill proposed you can initiate the policy and then enforce its execution, can you not?

Mr. ECCLES. That is right.

Mr. HANCOCK. So it really gives you complete control over the money supply?

Mr. ECCLES. That is right. Now, to that extent, it is centralizing that function to a greater extent than it has ever been centralized. Responsibiliy is always felt more keenly when it becomes a personal responsibility, and it seems to me it is desirable to place that responsibility in a small body, either in the Board or somewhere else.

The responsibility for the exercise of these important functions of monetary control should be in one body, either the Board or some other body. It should not, to my mind, be divided to such an extent that it can result in obstruction, lack of action, lack of coordination, and lack of a feeling of responsibility.

There are many important functions the Reserve banks have outside of the open-market operations, and there is no idea of taking away from the regional banks all of the functions which they now have. As a matter of fact, if the Board is given the authority it is requesting here in the bill, to delegate some of its authority, I believe that there are some of the duties that the Board could delegate to the regional banks beyond the responsibilities the banks now have. The regional banks carry the reserves of the member banks. The regional banks pass upon the credits to the member banks. It is through the regional banks that the Board operates in the approving of banks for membership, in the issuing of voting permits, in the examinations of banks, in the matter of reduction of capital structure, or in the matter of consolidations. All of the important relationships with all of the banks and the public in the area where the Reserve banks are, are handled by the management and directors of those banks; and there is no idea of taking away any part of this, or attempting to centralize those functions here in the Federal Reserve Board.

Mr. HANCOCK. In effect, Governor, does not this bill undertake to bring back home the sovereign power vested in the Congress to coin money and regulate the value of it?

Mr. ECCLES. Well, it brings to the Federal Reserve Board the power, and, of course——

Mr. HANCOCK. And through that Board back to Congress?

Mr. ECCLES. That is right, because——

Mr. HANCOCK. Is it not an unpleasant fact, Governor, that this power has been farmed out to private interests for years and years?

Mr. ECCLES. Well, the power really has not been exercised to any great extent. Up until 1922 there was not any recognition of the fact that, by the open-market operations, you affected the supply of money. There was no special machinery for open-market operations in the original Federal Reserve Act. In 1922, during a period when some of the banks were buying securities as investments, it was observed that it influenced the situation in New York, and they began to realize that these 12 Reserve banks, acting independently, in buying and selling for their own investment account, from a purely earning standpoint—in other words, operating as commercial banks would—had a real influence and effect on the money market. The result of that was a self-appointed committee of governors to work together, so as to have a coordinated program of buying and selling; and I believe it was not until 1933 that the open-market committee was recognized in the law.

Mr. HANCOCK. Governor, based on your statement yesterday, would it be unfair to interpret this bill as the last clear chance to save the autonomy of private banks of America?

Mr. ECCLES. Will you state that question again?

Mr. HANCOCK. I said, would it be fair to interpret this bill as the last clear chance to save the private commercial banks in America from their own destruction?

Mr. Eccles. Well, that would be a question rather difficult for me to answer.

Mr. Hancock. I am asking you the question, Governor, in the light of what you said yesterday.

Mr. Eccles. I think this bill will certainly tend to make it possible for the private banking system to function in a much more satisfactory and adequate manner than it has in the past.

Mr. Hancock. Nothing could be more desirable.

To use the expression that you used before the Senate committee in 1932, this measure, idealistically speaking, is designed to bring the money world back into relations with the real world, is it not?

Mr. Eccles. Well, it is designed to create a condition of stability, stable business, we will say, so far as it can be done through monetary policy. The important thing today is not so much, as so many people believe, to increase the quantity or volume of money, as it is to increase the velocity of money that is already in existence.

Mr. Hancock. I believe you take the position as I do that the velocity of money has a greater effect upon business activity than the quantity or volume?

Mr. Eccles. The volume of money is a very important element, and I think that, in a period of great business activity and full employment, or reasonably full employment, to reduce the quantity of money is very effective in controlling inflation. A small reduction in the quantity of money, through open-market operations, in certain periods, would be very effective.

Mr. Hancock. It always, however, tends to decrease business activity?

Mr. Eccles. That is right, and it is—well, it would tend to decrease business activity, and possible excess reserves would be wiped out. That would force the banks into borrowing, and that would materially restrict credits and raise rates, and tend to slow up the volume of business. However, when you permit a condition to develop, such as has developed during the past 4 or 5 years, when you first had a great period of deflation, of loans held by the banks, and bills held by the Reserve banks were allowed to run off, the volume of money was being extinguished at a terrifically rapid rate. From 1929 to the period of the bank holiday, about one-third of our total bank deposit money was extinguished, largely, through the liquidation of bank credit. This liquidation was forced upon the banks in part by their inability to go to the Federal Reserve banks with assets and meet the withdrawals of depositors, who were hoarding their funds, because of banks failing.

Mr. Hancock. It was an emergency situation and the very time the banks should have stepped in boldly as a rescuer or savior? Of course they were no able to go as far as they could go if this bill is passed.

Mr. Eccles. Well, two things seem to me to have been necessary.

Mr. Hancock. In other words, the Reserve banks were affected by the same emotional disease that the member banks were; is that not correct?

Mr. Eccles. They were increasingly restrictive in the kind of paper on which they would extend credit, and, of course, the law put limitations on the type they could take. Now, as to whether or not, by acting sooner or acting more vigorously in the open market, they could have stopped the period of deflation, that is, of course, a debatable question. Some will argue that had they acted more vigorously and sooner than they did, when there was a tremendous shortage of funds due to hoarding and due to the gold that was pulled out of the country and went abroad, that it would have turned the tide of deflation.

Mr. HANCOCK. There was never, during that period, coordinated action on the part of the Federal Reserve System as a whole, was there? Were not some banks operating at cross purposes with others?

Mr. ECCLES. I do not know. I do not know exactly what you mean by "coordinated."

Mr. HANCOCK. I mean this: That some of their actions were not in unison or accord with a national policy, looking to unified operations for the good of the entire country?

Mr. ECCLES. Well, I think the governors met and discussed the problem, and I think they also met here in Washington with the board and——

Mr. HANCOCK. I do not think there is any question about their having met, but what unified effective policy did they agree on?

Mr. ECCLES. Well, they reduced the discount rate, and they bought securities in the market, beginning with the autumn of 1929, but more vigorously after the passage of the Glass-Steagall Act in February 1932.

Mr. GOLDSBOROUGH. I will say that they continued that until the danger of the passage of the Goldsborough bill was over, and then it immediately stopped.

Mr. HANCOCK. Governor, what constructive thing did the Federal Reserve Sytem do, after deflation was halted, to aid in bringing about recovery? Would you mind telling this committee that?

Mr. ECCLES. Well, of course, in view of the fact that the entire banking structure collapsed and had to completely close, it is difficult to imagine how anything very much worse could have happened.

Mr. HANCOCK. Well, I believe in your statement made before the Senate committee in 1932——

Mr. ECCLES. 1933; in February of 1933.

Mr. HANCOCK. You referred to the fact that you considered the Federal Reserve System an emergency system; is that correct?

Mr. ECCLES. Well, I do not think so. I would not consider the Federal Reserve System an emergency system; it is a system that certainly should be able to regulate the volume of money. If the banks and the money system under capitalism cannot meet the emergency, the Federal Reserve System is the only agency we now have to do it. In other words, through the Federal Reserve System, we say that we succeeded in financing a war; and we know now this contributed very greatly toward the financing of the extraordinary expenditures of the war, in the absence of putting on taxes high enough to do that.

The Reserve System has, of course, been very helpful in the clearing of checks, and it has been a very great improvement over the system that was employed prior to the Federal Reserve System. It has speeded up immensely, immeasurably, the clearing of financial transactions throughout the country.

Mr. HANCOCK. Governor, if we had put on sufficient taxes during the war period, a large part of our present financial difficulties would have been avoided, would they not?

Mr. ECCLES. Well, I do not know that I could agree to that. I do not think that the financial troubles of the present are due to the war. We do not lack and did not lack in 1929 any material and physical thing that we had before the war and after the war. We had an increase in our total man power and in our capital production facilities.

The CHAIRMAN. Let me interrupt. Did not we experience our greatest period of prosperity in all of our history subsequent to the war and prior to this panic?

Mr. ECCLES. We had replaced every physical loss, and even the loss of man power as the result of the war by a very great amount from the end of the war up to 1929.

Mr. HANCOCK. Well, Governor, is it not a fact that our present war debts largely represent profits made during and out of the war?

Mr. ECCLES. Well, certainly, during the period of the war, we did not consume and use, as a nation, more than we produced. As a matter of fact, during that——

Mr. HANCOCK. And in that way, we did not impoverish ourselves?

Mr. ECCLES. We did not impoverish ourselves at all, because we used much less than we produced, because we furnished the Allies a tremendous amount of goods, which created the interallied war debts; so there was no occasion for a huge war debt, if the population had all been put upon a basis whereby there would have been no advantages to any group or class, and there would have been no profits as a result of that operation.

In other words, if the resources of the Nation had been mobilized in the interests of the Nation, for war purposes, we would not have needed any inflation, we would not have needed the credit that was extended. Our present situation indicates we are just as able now, in this country, to meet the problems of the depression as we would be to meet the problems of war. No one would question the fact that our ability to fight a war would depend upon the men and materials and our capital facilities in the form of our factories, systems of transportation, and so on. The question of money would not be the measure of our ability to fight a war in this economy of abundance. Neither is our ability to fight the depression in this economy of abundance a problem of money.

Mr. HANCOCK. It is a question of distribution?

Mr. ECCLES. Yes; it is a question of distribution. The depression, to my mind, was not brought about through a shortage in the volume; and by an increase in the volume of money after 1929 it would not have been possible to have avoided the depression. It might have deferred it or delayed it; but so long as we had such an inequitable distribution of wealth production as currently produced, so that our capital production facilities were all out of balance with the buying power of the people, the velocity was sure to slow up and a depression was inevitable.

Mr. HANCOCK. Governor, with respect to the question of debt—and then I will get to this bill again—I want to ask you this question, do you think a nation can impoverish itself by employing its men and materials in improving its equipment and resources?

Mr. ECCLES. No; I cannot see how a nation can impoverish itself by adding to or producing wealth. In my opinion, we might impoverish certain individuals if we do not distribute the wealth that is produced through giving employment.

Mr. HANCOCK. Then all we need today in this country of rich resources is, for our money to go to work; is that correct?

Mr. ECCLES. That is correct.

Mr. HANCOCK. Will this new bill help to restore confidence and put it to work?

Mr. ECCLES. Well, I cannot answer that; I can only express an opinion. It is my belief that it will; it is one of the factors that will help; it will make it possible for the banks to lend funds in fields in which they have been unwilling and unable to lend before. Whether or not they will find borrowers is another question. There is a great absence of people who are willing to borrow, even on long terms, or on any terms.

In connection with what I said, in order that I may not be misunderstood, I happened to read the other day an account of the last report of the Brookings Institute, which finds that the excessive savings went into speculation: Too much thrift held slump cause. It seems to me that has a very important bearing upon this question of the volume and quantity of money and the velocity of money.

Mr. HANCOCK. Said in a different way, you mean that too much labor went into capital goods?

Mr. ECCLES. That is right. [Reading:]

The institution, in the third of a series of investigations to ascertain whether maldistribution of income is a primary cause of the depression, found that the first need is for greater spending for goods rather than more savings.

Money going into savings, the report made public last night points out, is not immediately spent for consumption, and the rapid growth of savings in the twenties resulted in too much money going into speculation and not into actual buying of goods.

The report disputed several traditional economic concepts. Theoretically, according to one school of thought, savings go into the expansion of plant and other physical facilities, but the institution found that so much money was saved that there was a plethora.

Instead of going into either consumption goods or capital goods, it went into speculation which served to inflate the prices of securities and to produce financial instability.

In announcing the report, the institution cautioned that it did not suggest the individual of moderate means should, as a matter of policy, save less, but that "the problem is one of aggregate savings in proportions to aggregate consumption."

The phenomenon of an excessive supply of savings is, the report said, something new. In the past there has usually been a dearth of savings, with resulting difficulties in expanding the Nation's productive facilities.

The report further disputed the theory that business expansion begins with expansion of capital goods, holding rather that such expansion begins after people begin to buy.

The report noted that "a large part of the savings of individuals and business corporations has gone to finance Government deficits" since the depression.

The same institution, as I recall, gave the figures ofthe distribution of the national income—I think it was in 1929—showing that one-tenth of 1 percent of the families at the top of the list received the same income as 42 percent of the families at the bottom of the list; or in other words, the average income, per family, at the top, was equivalent to the average income of 420 families at the bottom.

Mr. HANCOCK. In the peak year, Governor, in 1929——

Mr. HOLLISTER. Pardon me, but I want to ask what report that is that he is quoting from?

Mr. ECCLES. That is the report of the Brookings Institute, The Capacity to Consume.

Mr. Goldsborough. And that is the 42 percent the Brookings Institute wants to spend?

Mr. Eccles. Well, the thing that they find is that that 42 percent was not responsible for very much saving. The one-tenth of 1 percent, of course, were unable to use their income in consumers' perishable and durable goods; and they, therefore, had to find an outlet in the investment field, or in the field of capital or producers' goods, until we reached a point where our capacity to produce was all out of relationship to our ability to consume but not our capacity to consume and——

Mr. Hancock. Which is a whale of a difference?

Mr. Eccles. Yes; our problem is no longer one of production, which it has been for generations, while we were building the country, while we were a debtor Nation, and when we had a rapidly increasing population.

Our problem is one of distribution. By distribution we mean not the distribution of the existing wealth but the distribution of the wealth production as it is currently produced; and the most effective day to do that, in times of prosperity, is through the income-tax system. One of the greatest mistakes, I think, that was ever made during a period of prosperity was to reduce income taxes rather than to maintain them at the high war point and use the funds collected to reduce the Federal debt; and then when unemployment developed to use the Federal credit to take care of unemployment.

Mr. Hancock. Governor, I think that same report to which you referred just now also showed this startling information: That in the peak year, 1929, 68.9 percent of the American families had gross incomes of less than $1,500.

Mr. Ford. May I make an observation there, Mr. Chairman?

The Chairman. Yes, Mr. Ford.

Mr. Ford. In 1929 there were 22,000,000 people in the United States, at the peak of our prosperity, who were living at or below the subsistence line; there were 45,000,000 people that were just getting by; there were 25,000,000 that were fairly well off; there were 15,000,000 that were rich; and there were 10,000,000 wallowing in wealth; and those are figures which were gotten out by a responsible organization.

Mr. Fish. And what is the subsistence line?

Mr. Ford. It is just being able to live by a little help from the country or relatives or somebody else; just getting by.

Mr. Fish. On the basis of income, it depends on the cost of living, but what is a subsistence income?

Mr. Ford. Well, I do not know what it is, because it depends on the section. It might be $15 in one part of the country and might be $25 in another and $40 in another, depending on what part of the country you live in.

Mr. Hancock. Governor, do you subscribe to the thought or belief that the control of a nation depends upon the control of its credit?

Mr. Eccles. I do not know that I understand your question.

Mr. Hancock. By that question I mean that unless the Nation, through its central Government, controls the credit or note-issuing power of the Nation the Nation cannot be used for the protection and welfare of all of the people?

Mr. ECCLES. Well, I think there must be a control over the money system.

Mr. HANCOCK. That means credit, does it not?

Mr. ECCLES. It is not necessary to control the credit relationships of individuals among themselves, nor the credit corporations extend on accounts, and so forth.

Mr. HANCOCK. Of course not; but our money system is 90 percent credit or check currency. You made that statement before the committee.

Mr. ECCLES. Well, 90 percent of our payments are made by checks on deposits, which is credit money; and it is necessary for a nation to exercise control in the public interest over the money system.

Mr. HANCOCK. Well, now, this bill is designed to insure control of the credit of the Nation in the interest of the Nation as a whole, is it not, and without interference with the normal functioning of the banks?

Mr. ECCLES. That is correct.

Mr. FORD. Otherwise, socialize it?

Mr. ECCLES. Well, it depends on what you mean by "socialize." Of course, I read yesterday a statement of Woodrow Wilson's conception of the Federal System, and I do not need to go beyond the statement of the President in whose administration the organization of this System was set up.

Mr. HOLLISTER. What is the purpose of that statement, Governor?

Mr. ECCLES. It is the purpose of setting up the System. He said:

The control of the system of banking and issue must be vested in the Government itself, so that the banks may be the instruments, and not the masters, of business and of individual enterprise and initiative.

Mr. HOLLISTER. Did anybody ever suggest that the Government should have the control of issue?

Mr. ECCLES. He has suggested the control of issue——

Mr. HOLLISTER. Did anybody else ever set up the contention that the Government was only for issue?

Mr. ECCLES. The theory was that these banks would control the issue.

Mr. HOLLISTER. It was not the Government. The banks were not identical with the Government, and nobody ever suggested that, did they?

Mr. ECCLES. That is true, but the thought was, that the Federal Reserve Board and the chairmen of these banks, who were appointed, were the representatives of the Government, or the people through the Government.

Mr. HOLLISTER. The Federal Reserve Board was, but not the Federal Reserve System?

Mr. ECCLES. The chairman of the Federal Reserve banks was appointed by the Federal Reserve Board, and was at that time looked upon as the executive head of the banks.

Mr. HOLLISTER. And the chairman appointed by the Board was to completely control the individual Federal Reserve banks?

Mr. ECCLES. No; the Federal Reserve banks, of course, were to be controlled by their board of directors.

Mr. HOLLISTER. Who were not Government appointees?

Mr. ECCLES. That is right.

Mr. HOLLISTER. Except certain of them?

Mr. ECCLES. That is correct.

Mr. HANCOCK. Governor, I wanted to ask you one more question. Do you think that the legitimate consumer demand or requirements for credit in this country can and will be met, as long as banking is a career?

Mr. ECCLES. Why, yes; I think so.

Mr. HANCOCK. I asked you that question because I understood you to refer to the fact that by providing independence or competence for Federal Reserve Board directors they could take hold of such positions and make careers of them and not have to look to outside income.

Mr. ECCLES. That is right.

Mr. HANCOCK. It is my thought that banking should never have been a career but always a profession. I hope you understand what I mean.

Mr. ECCLES. Are you speaking of the private commercial bank, or are you speaking of the Federal Reserve bank?

Mr. HANCOCK. I am speaking of all kinds where the public is involved and their welfare at stake.

Mr. Chairman, they are all the questions I care to ask at this time, but I reserve, of course, the right to discuss with the Governor the various sections of the bill. In your absence I made a request that the hearings up to now be printed, because it is humanly impossible for any man to digest all of the statements and suggestions made by the Governor, without having a written statement before him.

Mr. ECCLES. Let me answer Mr. Hollister's question about the control of issue because my associate has brought to my attention this statement in the law:

The Board shall have the right, acting through the Federal Reserve agent, to grant in whole or in part, or to reject entirely, the application of any Federal Reserve bank for Federal Reserve notes.

Mr. HOLLISTER. In other words, the Federal Reserve Board may limit the issue of notes, but may not increase the issue of notes at will?

Mr. ECCLES. That is right.

The CHAIRMAN. Gentlemen, it is probable that the H. O. L. C. bill will be taken up in the House tomorrow. I am not in a position to say definitely about that, but I will know in a little w hile. I thought we would not have any meeting of the committee tomorrow, and we appeared before the Rules Committee and asked for a rule, and we asked that we be given 1 day for debate of something like 4 hours on the bill. We are hoping that request will be granted. As soon as I can see the Speaker I can ascertain whether the bill will come up tomorrow or not. If it does, I wish you gentlemen would help me give information about it. If the bill comes up tomorrow, I suggest that the committee hold a meeting tomorrow afternoon at 3 o'clock, and just as soon as I can get that information I will have it telephoned to your office.

Suppose we say that we will meet at 3:30 this afternoon if the bill comes up.

Mr. HANCOCK. If the bill does not come up tomorrow, Governor Eccles will come back. Is that correct?

The CHAIRMAN. If the bill does not come up, Governor Eccles will come back; yes.

(Thereupon, the hearing in the above-entitled matter was adjourned temporarily.)

BANKING ACT OF 1935

MONDAY, MARCH 11, 1935

HOUSE OF REPRESENTATIVES,
COMMITTEE ON BANKING AND CURRENCY,
Washington, D. C.

The committee met at 10:30 a. m., Hon. Henry B. Steagall presiding.

The CHAIRMAN. Gentlemen, we have Governor Eccles with us this morning to resume the discussion of this bill, H. R. 5357, and it is Mr. Williams' time to ask questions, if you desire, Mr. Williams.

Mr. WILLIAMS. All right. Governor Eccles, I understand the main purpose of title II of this act is to enlarge and further centralize the powers of the Federal Reserve Board, in order that it may have increased influence and power over the expansion and contraction of credit of this country. That is to be done mainly through the open-market committee, fixing discount rates and controlling the reserves of the member banks. Those are the agencies through which it is to operate. Am I correct in that assumption?

Mr. ECCLES. That is correct.

Mr. WILLIAMS. Now, to what extent by the operation or by the use of these agencies by the Federal Reserve Board, can the general commodity price levels in this country be controlled, in your judgment?

Mr. ECCLES. It is impossible to say. The proposal to give to the Federal Reserve Board, with the advice of the Governor's committee, the responsibility for the use of these monetary controls, the discount rate, the reserve requirements, and the open-market operation is for the purpose of maintaining stable business conditions, insofar as this is possible by monetary means. A stable price level does not necessarily mean stable business conditions.

It seems to me that we are far more interested in full employment than we are in stable prices. If stable prices at some given index figure would leave an army of unemployed, it does not seem to me that this is the objective that would satisfy this country.

Mr. WILLIAMS. Well, you will agree, will you not, that it is very desirable, as far as possible, to have stable prices?

Mr. ECCLES. Yes; I agree to that.

Mr. WILLIAMS. And that the purchasing power be the same yesterday, today, and forever, you might say, so far as we can make them so?

Mr. ECCLES. I agree that wide and rapid fluctuations in prices are inflationary and deflationary and tend to create conditions that are unfavorable to business stability.

Mr. WILLIAMS. I judge you are not in favor of fixing certain commodity price levels as the goal toward which the Board should strive in its expansion and contraction policy?

Mr. ECCLES. I would prefer that it be not made the central objective of the banking bill.

Mr. WILLIAMS. Do you think it is practicable to do that?

Mr. ECCLES. I do not think it is.

Mr. WILLIAMS. On the other hand, there is considerable criticism in the country of the policy which places, entirely without any limitation, the matter in the hands of a few men, or the Board, this great authority; do you think there is any danger along that line?

Mr. ECCLES. The control over the volume of money and credit that the Federal Reserve Board can exercise through its use of three instruments of monetary control, would not necessarily tend to expand the amount of money in use in a depression such as we have at the present time.

Mr. WILLIAMS. Right in that connection, in the use of this word "money", what do you mean?

Mr. ECCLES. I mean demand deposits and currency.

Mr. WILLIAMS. Bank credit?

Mr. ECCLES. Yes; bank credit, deposits in commercial banks and currency. More precisely it is deposits subject to check, exclusive of bank float and interbank deposits, plus United States Government deposits.

Mr. WILLIAMS. Bank demand deposits?

Mr. ECCLES. That is right.

Mr. WILLIAMS. And currency?

Mr. ECCLES. Yes; that is right.

Mr. WILLIAMS. Is that what we mean when we talk about money now?

Mr. ECCLES. That is right.

Mr. WILLIAMS. I want to have that understanding as we go along.

Mr. ECCLES. That is correct.

Mr. WILLIAMS. Now, you say it would not necessarily result in expansion, that the policy should not or might not result in expansion during a period of depression?

Mr. ECCLES. You may create excess reserves through your open-market policy, but unless the borrowers are willing to borrow from the banks, and the banks are willing to lend to borrowers, you would not create a further increase in your money supply. You would increase the reserves of member banks, which would make for an inducement for the banks to lend and tend to result in a reduction in rates of interest, making for cheap money; but you must have borrowers who are willing and able to borrow before you can create additional money.

Mr. WILLIAMS. Is there no relation between the quantity of money and the volume of business that the country does?

Mr. ECCLES. No exact relation. The volume of money is an important factor, but the use of that money is an equally important factor in determining the amount of business.

Mr. WILLIAMS. Well, now, going back, for instance, to 1928, with a certain volume of money at that time and amount of business, how does that compare, we will say, with 1933?

Mr. ECCLES. In 1928 it was estimated that the national income was about $83,000,000,000. According to the Department of Commerce's figures, in 1933 the national income was about $47,000,000,000. The money supply in June 1928 was $26,400,000,000 and in 1933 it was $19,900,000,000. The ratio of the national income to the volume of money was 3.12 in 1928 and 2.35 in 1933. That brings out the point that I think you have in mind. I would estimate that in 1934, with a national income somewhere between $50,000,000,000 and $55,000,000,000, with an average volume of money of around $23,000,000,000, the number of times that your volume of money turned over was very little over two times. At the same rate of velocity that existed in 1928 and 1929, with the present volume of money, the national income should now exceed $75,000,000,000, which indicates that simply increasing the volume of money does not increase the national income proportionally. It seems to me that the reason for that is quite obvious.

The distribution of the ownership of money determines whether or not it is going to be put into use. Money is put into use by corporations and individual investors, who are led to believe that there is a profit in the investment or use of funds.

Mr. WILLIAMS. Well, then, did the increase in the volume of money build up reserves in the banks of the country? Would that not stimulate business itself, to the extent that it would make more money available, and would lead the banks, by reason of the unusual and unnecessary amount of money on hand, to try to get it out into the field of action? In other words, it would not be earning them anything, and it would furnish them an incentive to lend on more reasonable and better terms, would it not?

Mr. ECCLES. It has caused a very great reduction in interest rates, which is an inducement to the borrower, to the extent that the borrower can use the money profitably. Money is created by debt. Our banking system creates money——

The CHAIRMAN. Right there, Governor Eccles, you say money is created by debt; you mean by that, bank credit?

Mr. ECCLES. Yes; that is right. I mean that the banking system, the process of loaning money, extending credit, increases bank deposits. In the absence of individuals and corporations who are willing and able to borrow, the banks have created additional funds by purchasing Government bonds. The purchase of Government bonds has increased bank deposits.

Mr. WILLIAMS. Well, the volume of money times the velocity represents the national income, does it not, but they have both got to be there——

Mr. ECCLES. They have both got to be there; yes.

Mr. WILLIAMS. You have got to have volume and velocity like you have in physics to have momentum?

Mr. ECCLES. That is right. You cannot have velocity of the means of payment unless you first create a means of payment. You may create a means of payment and if it is in the hands of those who are unwilling to spend it, you do not create business activity.

Mr. WILLIAMS. Now, Governor, let us go to the question in this second title here of issue by the Federal Reserve banks. This act, as

I understand it, removes the necessity for any specific collateral back of any particular issue?

Mr. Eccles. That is right.

Mr. Williams. And simply permits the banks to issue upon their assets? Of course, all of that is to be done under the rules and regulations of the board, I assume, the Federal Reserve Board? Now, in other words, who is going to control how much they issue?

Mr. Eccles. The volume of notes issued depends in the first instance on the demand for cash by the public and more remotely on the amount of deposits the Federal Reserve banks have created for their member banks, either by extending loans to them or by open-market operations.

Mr. Williams. Who is going to determine whether an issue has back of it sound assets, or not?

Mr. Eccles. The Federal Reserve banks' credit departments will determine that by the type of loans or type of credit which they extend to the member banks.

Mr. Williams. Now, let me see that I understand. The policy that has been heretofore followed has been that the Federal Reserve agent has had charge of that, has he not, or a representative of the Board?

Mr. Eccles. The Federal Reserve agent holds the collateral, consisting of gold certificates, eligible paper, and Government bonds. Originally it had to consist of gold and eligible paper. The Glass-Steagall Act of 1932 permitted Federal Reserve notes to be backed by Government bonds in the absence of a sufficient amount of commercial paper.

Mr. Williams. The application for issue is made to the Federal Reserve agent?

Mr. Eccles. That is right.

Mr. Williams. And he was required to have sufficient assets, in his judgment, back of that issue; that is, they were required to put up with him particular assets on a particular issue that they called for; is that correct?

Mr. Eccles. It was figured as a whole, the total amount of notes that each Federal Reserve bank had outstanding, backed by gold certificates and bonds and other collateral that was deposited with the Federal Reserve agent. But it seems to me that, in order to understand what is back of the Federal Reserve notes, we must consider the balance sheet of the Federal Reserve bank. The liabilities of the Federal Reserve bank to the public consist chiefly of deposits of the member banks and of Federal Reserve notes.

Against these liabilities the Reserve banks hold assets, consisting of investments in bills, Government securities, discounts to its member banks, and gold certificates.

It is impossible to issue Federal Reserve notes as liabilities without either an offsetting decrease in deposits or an offsetting increase in assets, in the form of gold certificates, Government bonds, eligible bills, or loans to member banks; and the only question that could arise regarding the security back of Federal Reserve notes would be in connection with loans which the Federal Reserve bank made to the member banks. If they made loans which were bad, whether eligible paper or whether loans secured by what would be considered as sound assets, and the losses on those loans were in excess of the capital and surplus of the reserve bank, then in theory the United States Government would have to be called upon to make good the guaranty of the Federal Reserve notes outstanding. But that is the only way in which there could be any question as to the backing of the Federal Reserve notes. At all of the central banks, except the Federal Reserve System and the Bank of England, notes are issued without any specific backing.

Mr. WILLIAMS. Now, Governor, I want this clear in my mind——

Mr. HOLLISTER. May I ask one question right there, Mr. Williams?

Mr. WILLIAMS. Yes.

Mr. HOLLISTER. Is it not true, however, that there is a statutory limit in most of the countries as to the amount of that issue?

Mr. ECCLES. Well, I could not say.

Dr. Goldenweiser advised me there is no such statutory limit.

Mr. WILLIAMS. Let me ask you this question: In the application of a reserve bank under our present system, to the Federal Reserve agent for an issue, has that application ever been denied?

Mr. ECCLES. I do not think so.

Mr. WILLIAMS. When an application is made, who passes on it?

Mr. ECCLES. That is a formal matter; it is almost an automatic operation. The amount of notes that any Reserve bank requires to meet the demands of its deposits would be turned over to it by the Federal Reserve agent in exchange for the necessary collateral lodged with the Federal Reserve agent.

Mr. WILLIAMS. Now, are you saying that would be left entirely to the Federal Reserve banks?

Mr. ECCLES. The amount of issue will be determined by the call which the member banks make for currency, and when they make a call for currency they must have deposits with the Reserve bank, just as an individual who wants currency must have funds in a commercial bank to be able to draw down that currency.

Mr. WILLIAMS. The part I am trying to get at is whether or not the central Board, the one that has control or the one you want to place more power in—whether or not they have control over the amount of issue of each one of these Federal Reserve banks?

Mr. ECCLES. The Federal Reserve Board has technical control over the amount of issue under the present law, but it has found that it is useless to control note issue after the member banks have acquired deposits, and under the proposed law the Federal Reserve Board would not have this purely technical or theoretical control. The reason that the control is only theoretical is that, when member banks wish to withdraw their deposits in cash, no Reserve bank can refuse to pay out the cash, and the Federal Reserve Board cannot take the responsibility for preventing it.

Mr. WILLIAMS. Then, the Federal Reserve agent simply is an administrative officer; he has no discretion about it, but he is simply a trustee with these funds in his hands?

Mr. ECCLES. The Federal Reserve bank would have to close if the member banks asked for currency in lieu of their accounts and were refused.

There is no more justification for requiring specific collateral back of Federal Reserve notes, which are the liabilities of the Reserve banks, than there is for requiring specific security to be pledged against the deposits of the Federal Reserve bank. Why should Federal Reserve notes outstanding be given a preferred status over the deposit liability of the Reserve banks?

Mr. WILLIAMS. Then, do you think it is a sound policy for the Government to guarantee these notes and at the same time have no control over their issue at all?

Mr. ECCLES. I do not think that a controlled issue would be a particle different than an issue that is not controlled, because the Reserve banks are required to issue currency whenever member banks have deposits and desire to draw down those deposits in currency. It is in the determination of the volume of credit extended to member banks for the purpose of creating the deposits that the real control of the note issue lies. They cannot draw down currency unless they have established balances with the Reserve bank, and have put up acceptable assets, in which case they can drawn down their deposits in currency in the same manner that any individual depositor of a commercial bank is able to draw his deposits in currency. Whenever a bank is unable to pay out the deposits in currency, that bank must close.

Mr. WILLIAMS. They are turning out currency on what they call "acceptable assets" as security?

Mr. ECCLES. Who is?

Mr. WILLIAMS. The Federal Reserve bank? If a member bank wants to borrow money, how do they get it?

Mr. ECCLES. They put up collateral.

Mr. WILLIAMS. Who passes on that collateral?

Mr. ECCLES. The Federal Reserve banks.

Mr. WILLIAMS. And they get money for it? That is, the member banks get money for it?

Mr. ECCLES. Yes; they get credit.

Mr. WILLIAMS. And that is guaranteed by the United States Government?

Mr. ECCLES. They get deposit credit for it.

Mr. WILLIAMS. Of course, that is money?

Mr. ECCLES. Yes; that is right.

Mr. WILLIAMS. And the Government itself is back of it, and still it is simply the deposit of eligible security in the judgment of the Federal Reserve bank?

Mr. ECCLES. That is right.

Mr. WILLIAMS. And they have entire control and jurisdiction over it?

Mr. ECCLES. Over the assets which they will take, yes.

Mr. WILLIAMS. And pass on the question as to whether they are good or bad?

Mr. ECCLES. That is right.

Mr. WILLIAMS. All right.

The CHAIRMAN. Governor Eccles, do you mean that they have entire control over the kind of assets they accept? They pass upon the acceptability of assets entered as collateral as to solvency and technical eligibility, but when it comes to fixing the rules of eligibility under the present law, they are governed by the rules laid down in the act, are they not?

Mr. ECCLES. That is correct. They have discretion as to the acceptability of assets or as to the type of paper which they will take from member banks, subject at the present time to the eligibility requirements of the Federal Reserve Act.

In the future, if the present eligibility features of the act are removed and discretion given to the Federal Reserve Board to determine the eligibility requirements, the Reserve banks would have discretion within the rules and regulations laid down by the Federal Reserve Board. However, it would not be mandatory and it is not mandatory in the present law, that the Federal Reserve banks loan to member banks. They simply have authority to loan to member banks upon what is considered eligible paper.

The proposed amendment would give the Federal Reserve banks the power to loan to member banks on paper submitted to them, provided it met the requirements laid down by the Federal Reserve Board.

Mr. WILLIAMS. Yes; I understand the only difference in the existing law and the proposed law in that respect is, as it is now it is a part of the statutory limitation, and the other is to leave it to the rules and regulations of the Board as to what is eligible?

The CHAIRMAN. Let me ask you a question right there now: This might happen, technically speaking, that under the new law the Board could make regulations defining the eligible paper which would be more restrictive than the rules fixed in the present law, or if the Board saw fit, it could liberalize those rules, but it could work either way?

Mr. ECCLES. I think so.

The CHAIRMAN. So it does not work arbitrarily in either direction?

Mr. ECCLES. That is right.

The CHAIRMAN. Under the new bill, that is correct?

Mr. ECCLES. That is correct, yes.

Mr. WILLIAMS. What, in your opinion, should be the policy in that respect, liberalized or made more restrictive?

Mr. ECCLES. I think it would depend a great deal upon the conditions that confronted the country. In 1930 and 1931 it would have been in the interests of the banking system and in the interest of the entire country if the Federal Reserve banks had been permitted to loan to member banks on any sound assets, when many of them had very little or no commercial paper. The failure of the member banks to be able to borrow from the Federal Reserve banks forced a condition of great deflation. It forced the banks to refuse to extend loans as they fell due, and forced them to sell their bonds, their securities on the market. It resulted in liquidating or extinguishing, through credit contraction, about $20,000,000,000 of our total bank deposits, including time deposits. A good deal of that, of course, was the result of tying up deposits in closed institutions; but the total volume of deposits was greatly reduced, partly because of the inability of the member banks to get relief by going to the Federal Reserve bank, until we finally liquidated our banking structure to such a point that it became entirely frozen and closed.

And in getting it open, we finally had to recognize, as an emergency matter, that the Federal Reserve banks could loan to their member banks on all sound assets and that the Federal Reserve banks could issue notes secured by any sound assets, without resort to gold, Government bonds, or eligible paper.

The CHAIRMAN. Now, let me interrupt you with something that should be said right here. It not only went to the extent that you have pointed out, but as an emergency measure we provided that such loans might be made to nonmember banks and currency issued to nonmember banks on the same rules and regulations; is that not what happened?

Mr. ECCLES. That is correct.

The CHAIRMAN. So we were forced to do that in the hour of distress, instead of having anticipated and provided for it in advance?

Mr. ECCLES. Yes; Mr. Chairman, that is correct.

Mr. WILLIAMS. Right in that connection, to what extent has it worked?

Mr. ECCLES. When people can get their money, they do not want it. I think the law was very effective, because it stopped banks from closing. Instead of the Federal Reserve being required to make loans to meet the demand, money which had gone into hoarding to the extent of anywhere from $1,500,000,000 to $2,000,000,000 in currency that was drawn from the banks beyond what was the normal use or need of currency, tended to come back into the banks. That enabled the banks to pay off the Federal Reserve banks, so that the amount of borrowing by the member banks from the Reserve banks today is practically negligible; whereas, in 1933, it was very large.

Mr. WILLIAMS. Then instead of increasing the necessity for borrowing has actually decreased it?

Mr. ECCLES. The requirements; yes.

Mr. WILLIAMS. That has actually decreased?

Mr. ECCLES. That is right.

Mr. WILLIAMS. There has been no demand upon the Federal Reserve Board since the passage of this act, I take it, from what you say, to borrow upon these general assets, I will say, which were not heretofore eligible, such as real-estate securities, long-term bonds, and things of that kind; there have not been any of them offered as security to the Federal Reserve banks for the purpose of obtaining loans?

Mr. ECCLES. I think it is section 10 (b) of the Federal Reserve Act, as amended by the Emergency Banking Act, which says that, under exigent circumstances, member banks are permitted to borrow from Reserve banks on their time or demand note secured to the satisfaction of the boards of directors of the Reserve banks. There was some use made of that provision, but not very much, because it put a bank in a position, where it applied for credit under the terms of that provision, of admitting that it was in great distress and exigent circumstances that it required special treatment by the board of the Federal Reserve bank, which meant that a bank would only resort to that, would only use the borrowing right, as the very last resort.

Mr. WILLIAMS. To what extent are real-estate loans used for the purpose of acquiring loans from the Federal Reserve?

Mr. ECCLES. I could not say to what extent, but there has been some borrowing from Reserve banks on bills payable backed by real-estate mortgages, and other collateral put up to secure the notes of the banks.

Mr. WILLIAMS. It is the intention of this bill, as I understand it, to so amortize real-estate loans as to make them eligible for discount?

Mr. ECCLES. Not for discount.

Mr. WILLIAMS. Well, for loans?

Mr. ECCLES. Yes.

Mr. WILLIAMS. As security for loans?

Mr. ECCLES. Yes; the bill provides that the act be amended to authorize Federal Reserve banks, subject to the regulations of the board, to discount for a member bank all commercial, industrial, or agricultural paper, and to make advances to a member bank on its promissory notes secured by any sound assets.

Mr. WILLIAMS. And that includes real-estate loans, of course?

Mr. ECCLES. Collateral loans, bonds, or any other sound assets.

Mr. WILLIAMS. And the purpose of this—not of this section, but of the real-estate section—is to so liberalize real-estate loans, by amortizing them over a long period of time, as to make them eligible as a permanent policy, to encourage additional loans by national banks and member banks on real estate, in order that they can, if necessary, dispose of those in time of distress and get money from the Federal Reserve banks?

Mr. ECCLES. So long as the commercial banking system is permitted to take savings deposits, I see no reason why those savings funds cannot be loaned on amortized real-estate loans in the community of the bank.

Mr. WILLIAMS. I agree with that, myself. I absolutely agree with that, but the purpose is, as far as it can be done, to liquefy real-estate loans?

Mr. ECCLES. Yes.

Mr. WILLIAMS. I think we all agree that that cannot be done as a policy, but as far as it can be done——

Mr. ECCLES. In a depression, only the Federal Reserve can liquefy assets. Real-estate loans are no different than any other type of paper in a great deflation.

Mr. WILLIAMS. Of course, they have been, for the reason that there has been no place to discount them.

Mr. ECCLES. In a great depression there is no other place to go. And they do not have to be real-estate loans. They may be loans on collateral, or they may be investments in bonds. When the market is depressed, as it was for a period of several years, that meant bankruptcy for any bank that liquidated its assets on the existing market, and that condition tended to close many banks.

Mr. WILLIAMS. Is it the thought of the Federal Reserve Board that there should be no limitation at all, upon these amortized real-estate mortgages?

Mr. ECCLES. You mean no limitation as to the percentage——

Mr. WILLIAMS. No; I do not mean on the percentage of valuation, but on the amount of the loan on each individual property.

Mr. ECCLES. There is no limitation now, under the real-estate provision of the National Banking Act under which they have operated for 20 years, with the exception of the limitation of 10 percent of the capital and surplus on any one loan.

Mr. WILLIAMS. Real-estate loans have not heretofore been eligible for discount with the Federal Reserve bank, except as an emergency measure?

Mr. ECCLES. There is over $2,000,000,000 of real-estate loans in member banks.

Mr. WILLIAMS. Have they been able to put those loans up with the Federal Reserve bank?

Mr. ECCLES. Only when an emergency was created and then they were permitted as an emergency matter to do that.

Mr. WILLIAMS. That is exactly what I say, except as an emergency measure, they never have been eligible for loans?

Mr. ECCLES. That is right.

Mr. WILLIAMS. This act proposes to make them eligible?

Mr. ECCLES. That is right.

Mr. WILLIAMS. And it is not thought to place any limitation, at all, upon them?

Mr. ECCLES. You mean limitation as to——

Mr. WILLIAMS. As to the amount? Here is an apartment house or hotel, or some other business institution, on which they want to make a loan of $100,000,000, for example——

Mr. ECCLES. One bank is limited in the amount of a loan they can make to any one borrower to 10 percent of its capital and surplus. So it has that limitation on it.

Mr. WILLIAMS. There is to be an increase under this act?

Mr. ECCLES. No; there is no change in it, at all.

Mr. BROWN of Michigan. As a matter of fact, it is a decrease, that is, 10 percent of the time deposits?

Mr. ECCLES. No; any bank can loan any borrower up to a total of 10 percent of its capital and surplus.

The CHAIRMAN. You mean that a loan can be made on any collateral or without collateral?

Mr. ECCLES. That is right. That has always been a provision of the Banking Act.

Mr. WILLIAMS. There is a provision in here, is there not, limiting it as applied to real estate?

Mr. ECCLES. No; the limitation is 50 percent of the time deposits and 50 percent of the appraised value of the property, which is the only limitation in the present act with reference to real estate.

Mr. WILLIAMS. It is expanded to what it was, in effect?

Mr. ECCLES. It is proposed to increase it from 50 to 60 percent, but the 60 percent also includes other real estate which is not included in the 50 percent in the present law.

Mr. WILLIAMS. Then loans to each institution heretofore have been limited to 25 percent of the capital and surplus on real estate?

Mr. ECCLES. Or 50 percent of its time deposits, whichever was greater.

Mr. WILLIAMS. What I am trying to get at is, it is expanded and enlarged, or is it not?

Mr. ECCLES. Yes; from 50 to 60 percent and up to 100 percent of its capital and surplus, whichever is greater.

Mr. WILLIAMS. Instead of 25 percent, it is now extended to the full amount of its capital and surplus?

Mr. ECCLES. Yes.

Mr. WILLIAMS. Or 60 percent——

Mr. ECCLES. Of its time deposits.

Mr. WILLIAMS. Of its time deposits?

Mr. ECCLES. Right. I suggested that those limitations be taken out of the act and the Federal Reserve be charged with the responsibility of determining regulations with reference to the real-estate loans.

Mr. WILLIAMS. Do you think there ought to be no limitation in that respect in it, except the regulations and rules of the Board?

Mr. ECCLES. That is right.

Mr. WILLIAMS. Or whatever limitation they saw fit to place?

Mr. ECCLES. That is right.

Mr. WILLIAMS. It ought not to be made a statutory provision?

Mr. ECCLES. That is right.

Mr. WILLIAMS. For the reason that it would give them more flexibility in the local communities, in the different localities, and at different times, under differing conditions?

Mr. ECCLES. Many of the nonmember State banks have, at the present time, more than 60 percent of their time deposits in real-estate loans, and some of the member State banks have more than 60 percent. That would mean that those banks would be required to liquidate their real-estate loans, in order to comply with the 60-percent requirement. Many State banks are not limited in the amount of their deposits that they can loan upon real estate.

Mr. WILLIAMS. I am very much concerned about this provision regarding real-estate loans, because I have been under the impression, by reason of the fact that these loans were short-term loans, not amortized loans, the banks were not able to handle them at all in a period of depression.

Mr. ECCLES. You mean under the present bill?

Mr. WILLIAMS. Yes; under the present act, the law as it is now?

Mr. ECCLES. That is correct.

Mr. WILLIAMS. And this act proposes to amortize them over a period of years and make them eligible for discount and furnish a market, somewhat, for them when the time comes when the banks have to have their money. I think, myself, it is a very wise provision in the law.

I believe that is all I care to ask at this time.

Mr. FORD. Might I ask a question, Mr. Chairman, just a question?

The CHAIRMAN. Yes; indeed.

Mr. FORD. Suppose the Federal Reserve has taken considerable volume of real-estate loans, what provision is there for the Federal Reserve bank, itself, to dispose of them, should they want to?

Mr. ECCLES. There would be no occasion for the Federal Reserve bank to dispose of them, so long as the member bank that borrowed the money was solvent. The member bank would owe the Federal Reserve on its bills payable, secured by mortgages which it had taken.

Mr. FORD. Suppose a member bank failed?

Mr. ECCLES. The Federal Reserve bank would be required to liquidate that mortgage or collect it or sell it, just as any other asset.

Mr. FORD. It could sell it, though?

Mr. ECCLES. Yes; it could sell it.

Mr. FORD. It is not just put in there and held static?

Mr. ECCLES. No; it would liquidate any asset or loan of the member bank which it held just the same as the member bank would undertake to liquidate the loan of an individual or corporation borrower.

Mr. WILLIAMS. Governor, there is this question that I want to ask you before I finally quit: Under our present system, or under the system proposed in this bill, what do the Federal Reserve banks pay for the privilege of issuing money?

Mr. ECCLES. They do not pay anything.

Mr. WILLIAMS. Do not pay anything?

Mr. ECCLES. No.

Mr. WILLIAMS. Now, as you know, there is considerable agitation, a good deal of comment in the country, about the Government owning these institutions. What would be the difference in effect if the Government did own them?

Mr. ECCLES. The individual member banks are the owners today. However, they are limited to 6 percent dividends on their stock. The earnings of the Reserve System in excess of 6 percent are held by the Reserve banks, and at one time——

Mr. WILLIAMS. Right in that connection, do they not belong to the stockholders?

Mr. ECCLES. Not under the law, not beyond the 6-percent dividends.

Mr. WILLIAMS. Of course, I understand we had, by legislation, to take it away from them. They were claiming to own it, were they not?

Mr. ECCLES. Yes; I think that there possibly was some claim to that effect. Personally, I would see no objection to requiring that the earnings of the Federal Reserve banks, beyond the limitation of 6-percent dividends to member banks, should be turned over to the Government when the surplus of the Reserve banks has reached an amount equal to its capital.

Mr. WILLIAMS. If the Government, however, can own and operate them as successfully as private institutions have done, why not give the 6 percent to the Government rather than to the private banks, as well as the reserves and the surplus?

Mr. ECCLES. It is now provided in the law that, in case of liquidation, any surplus remaining, after the payment of all debts, dividend requirements, and the par value of the stock, shall be paid to and become the property of the United States. I see no advantage in the Government taking over the stock of the Reserve banks.

Mr. WILLIAMS. It would not cost the Government anything to do that, would it?

Mr. ECCLES. I think it would; yes. The Government could not take over the stock without paying the member banks, any more than the Government could purchase any other asset without it costing it anything.

Mr. WILLIAMS. The purchase of the stock is already in the Federal Reserve banks, the purchase price of it?

Mr. ECCLES. That is right.

Mr. WILLIAMS. And if you took it over, it would simply own it instead of the Federal Reserve System owning it; the funds then with which the stock was paid for would be in the hands of the Government, would they not?

Mr. ECCLES. No; the United States Treasury would have to make payment to each member bank for its stock in the Reserve System, and the stock would be transferred from the ownership of the individual member banks, which own stock in the respective Federal Reserve banks——

Mr. WILLIAMS. Then, in taking over the System, we would get the assets that belong to the bank, that were paid in there by the member bank, would we not, for their stock?

Mr. ECCLES. When you bought the stock held by a member bank in the Federal Reserve System, you would naturally have—that is, the Government would naturally have the assets represented by stock which it purchased. That is correct.

Mr. WILLIAMS. And that is sound, really, after all; it would not cost the Government anything?

Mr. ECCLES. It might be—it would not cost it in the sense that it would be paying out funds without getting an equivalent asset; it would be an investment, rather than an expense, but it would cost the same——

Mr. WILLIAMS. They would get the stock?

Mr. ECCLES. That is right.

Mr. WILLIAMS. The stock the member banks now own? Now, I believe I asked a question awhile ago, that if the Government can own and operate the banks and issue money, instead of private institutions, why not do that and save the 6 percent that we are now paying.

Mr. ECCLES. You would not save 6 percent. For the Government to buy the stock, it would be required to raise the money that is used to purchase the stock, and in raising that money it would borrow it. If it borrowed it or raised it as they raised funds for other purposes, it would be required to pay whatever interest the Government debt was required to bear, in order to float the funds to get the money to buy the stock.

At the present time, the last offerings of Government securities bore a rate of 2⅞ percent; so in that case, you would save 3⅛ percent, the difference between 6 percent and 2⅞ percent.

Mr. WILLIAMS. Even so, why not save it?

Mr. ECCLES. The answer is, perhaps, that there is no more reason for the Government to invest in this business so long as it controls the money supply, than in any other business.

Mr. HOLLISTER. Might I ask one question there?

Mr. WILLIAMS. Yes; go ahead.

Mr. HOLLISTER. That would be on the theory that you could necessarily buy the stock at par. There is nothing, is there, in the law which would permit the Government, unless it is some new theory of confiscation hitherto unannounced—there is nothing by which the Government could expressly pay the member bank which owns a particular amount of stock in a particular Federal Reserve bank—there is nothing by which the Government could compel that bank to sell its stock at par if it chose to put a price on it of $200 or $300 or $400, is there?

Mr. ECCLES. That is a legal question that I do not feel I am prepared to answer.

The CHAIRMAN. Let me suggest that if you answer that question you also tell us what you would do about the stock of the State bank that is a member of the Federal Reserve System.

Mr. HOLLISTER. I am assuming that the Government is trying to buy stock in a Federal Reserve bank owned by individual member banks. That would be a matter of contract between the Government and each individual stockholder bank as to what the Government would be willing to pay and what the member bank would be willing to surrender its stock for.

Mr. Eccles. That would seem to be the situation, and that is a legal question.

Mr. Hollister. If you are not prepared to answer the question, I would rather not interfere with Mr. Williams. I do not want that to remain open without some comment, but I will refer to it later.

Mr. Wolcott. May I ask a question, Mr. Williams?

Mr. Williams. Well, yes.

Mr. Wolcott. Do I understand there is about $450,000,000 in that fund which has been turned over to the Federal Treasury over and above this 6 percent that was used—or we used one-third of it, did we not, in subscribing for stock?

Mr. Eccles. The Federal Deposit Insurance Corporation? That was $140,000,000——

Mr. Wolcott. Was it not one-third of that fund?

Mr. Eccles. No; it was more than one-third. The Treasury put $150,000,000 and the Reserve System——

Mr. Wolcott. $149,000,000?

Mr. Eccles. I think it was $140,000,000.

Mr. Wolcott. $139,000,000, I think it was.

Mr. Eccles. It made a total of $290,000,000 that was supplied by the Reserve banks and the Treasury.

Mr. Wolcott. Out of this Reserve System?

Mr. Eccles. Out of the surplus of the Federal Reserve bank.

Mr. Wolcott. That could be used in payment of interest on these bonds, and after that the full 6 percent and all over and above that would go to the Government?

Mr. Eccles. You mean, then——

Mr. Wolcott. This reserve that is already in it——

Mr. Eccles. Yes; but that money was paid out by the Reserve banks to the Federal Deposit Insurance Corporation, and therefore the Reserve banks no longer have those funds. Those funds are owned by the Federal Deposit Insurance Corporation and——

The Chairman. Let me correct you just a moment.

Mr. Wolcott. We reimbursed the Federal Reserve bank for that, did we not?

The Chairman. We did not give any money to the Federal Deposit Insurance Corporation, but we merely subscribed to its capital stock.

Mr. Eccles. Yes.

Mr. Wolcott. Indirect loans——

Mr. Eccles. You do not think that the capital stock has very much value, then, do you? The law provides that the stock of the Federal Reserve banks can receive no dividends.

The Chairman. Tim will tell that.

Mr. Eccles. The first banking bill——

The Chairman. It has made pretty good profit up to now.

Mr. Eccles. Title I of the banking bill provides that the Federal Deposit Insurance Corporation's capital of $290,000,000 can be reduced to a nominal amount, and the balance put to surplus, so there would not be an impairment of capital, if it became necessary to put up these funds.

Mr. WILLIAMS. I would like to remark, in that connection, that so far as I am concerned, that will not be done, because I believe the banks themselves ought to bear that burden.

Now, coming back to the original proposition, Governor, whether or not the Government, as a practical proposition, can own and operate the Federal Reserve banks on as sound a financial basis, and render the same service and save these expenses, in the long run, if you have dividends that are being paid to the banks on the stock—if that can be done, why should it not be done?

Mr. ECCLES. I believe that the ownership of the stock by the Government would not necessarily be of any particular benefit or value in the operation of the Federal Reserve System. I believe that through the adoption of the provisions of this bill, the control would be effective and the responsibility fixed, and it should be just as effective in operating the system in the public interest as it could be operated if the Government owned the stock. It gets down to a matter of human intelligence. The management of the banks or the management of the System would have to be directed in some manner by some means. I see no reason why a management selected with the Government owning the stock would insure the System being operated in the public interest anymore than would be the case with the members of the Federal Reserve Board being appointed by the President of the United States, as is now provided, and the governors and chairmen of the individual banks selected by the local directors of the bank, subject to the approval of the Federal Reserve Board. There is a great advantage in keeping regional ownership and interest in the Reserve banks.

Most of the central banks of the world are privately owned. The bank which is just being set up in Canada, after a good deal of investigation and study and consideration, is owned by the public. I understand the stockholders elect the directors, but the Governor of the bank must be approved by the finance minister, and he has very great power and responsibility.

It is not so much who owns the bank as it is the way the bank is set up and the responsibility with which it is charged.

Mr. WILLIAMS. Is it your thought that Government-owned central banks can operate as economically and as efficiently and as much in the interest of the people of the country as our present system?

Mr. ECCLES. I do not think that the fact that it may be Government-owned, in and of itself, should make any difference. It may be operated as efficiently and it may not be operated efficiently. That, as I say, gets to the human problem, after all.

Mr. WILLIAMS. The ownership of it, in that respect would make no difference?

Mr. ECCLES. I do not think so, not necessarily. If the management of the banks, the personnel of the board consisted of efficient men who would feel independent to use their best judgment and thought in carrying out the affairs of the institution, the ownership would make no difference. If, on the other hand, people were appointed to operate the system for purely political reasons, rather than with reference to their qualifications, and they were made to feel subservient to the point where their best judgment was not exercised, then of course the system, under those conditions, would be badly and inefficiently and ineffectively operated.

Mr. WILLIAMS. Of course, the central idea in this legislation here, as is stated at the very beginning, is to try to increase and centralize the power in the Federal Reserve Board over the System, and I think properly so because I think that the Government and Congress and the administration should have control of the monetary system. It is a national system, of course, and there should be some central authority and central power responsible for it. The purpose of the bill is to create centralized authority, with complete management of the corporation or system.

Mr. ECCLES. With the board, which would be charged with responsibility for the monetary policy, working with and under the advice of the Governors' committee. There are many functions that would be carried out by the individual regional reserve banks, under the direction of their boards of nine directors.

Mr. WILLIAMS. But nothing that would influence the national monetary policy, without the consent of the central board?

Mr. ECCLES. That is right, except that the Governors would influence the policies of the board, as a result of their counsel and advice.

Mr. WILLIAMS. And that would be true whether they were representing the system governmentally owned or individually owned, would it not? Right in that connection the counsel that you propose of five——

Mr. ECCLES. Representing the 12 Governors.

Mr. WILLIAMS. What function does the advisory counsel now perform? Why could it not do the work proposed by the five?

Mr. ECCLES. I think it is more proper to have the executive heads of each of the 12 banks select their committee for the purpose of advising with reference to the policies, than to have the council advise. The Governors are in much closer touch with monetary problems. The members of the council are appointed, one from each Federal Reserve bank district by the Federal Reserve banks, and I think they consist entirely of commercial bankers from the Federal Reserve districts. They are in touch with the individual problems of their particular banks and their particular communities but I do not believe would be as able or as qualified——

Mr. WILLIAMS. They perform a very valuable function; that is, do they or do they not?

Mr. ECCLES. I have not been on the Federal Reserve Board except for a few months, and I have only had occasion to meet with the advisory council on two occasions. It would, therefore, be difficult for me to judge as to just how important the functions of that body have been over the life of the System.

Mr. FORD. Might I make a comment, Mr. Williams, please?

Mr. WILLIAMS. Yes.

Mr. FORD. Mr. Eccles, does not the demand for more complete control on the part of the Government indicate that the heretofore private control has not proved satisfactory to the Congress or the country?

Mr. ECCLES. I would not say that we had had private control. I think one of the principal difficulties of the money system has been that we had not placed the responsibility definitely upon any one body and given it the power and authority to carry out the responsibility that was imposed upon it.

Mr. FORD. It is too wide-spread, and they have been forced to operate and do what the Board wanted to do——

Mr. ECCLES. We did not have a statutory open-market committee until the Banking Act of 1933 created one of 12 Governors, and charged that body with responsibility for the initiation of the open-market operations and gave to the Board the power of approving or disapproving the recommendations of the Governors. But even then if the Board approved of recommendations of the Governors, one or all of the 12 banks could refuse to participate in the operation.

Mr. WILLIAMS. Has not the Board had that open-market policy through the years?

Mr. ECCLES. The Board was not charged by law with the duty of formulating an open-market policy.

Mr. WILLIAMS. None at all? Have they not intended to control, in any way, the expansion and contraction of money through open-market operation, through their advice and instruction to the member banks, and through their own operations?

Mr. ECCLES. The Board has acted in all these matters, but without a clear mandate of law.

Mr. WILLIAMS. They made no effort—do I understand that the Board itself has never made any effort at all along that line until the open-market committee of 1933?

Mr. ECCLES. The Board has attempted to influence the money market through changes in discount rates—that is, its right to approve of the discount rates—and it has even changed discount rates on its own motion. The need of the open-market operation was recognized in 1922, and a voluntary committee of governors was organized to carry out the open-market policy or program.

Mr. WILLIAMS. They had that policy then?

Mr. ECCLES. The open-market committee of the governors had the responsibility for that program. The Board itself has not been charged specifically with the responsibility for the open-market policy.

Mr. WILLIAMS. I understand, as a matter of law, but they have actually adopted the policy, have they not?

Mr. ECCLES. To what extent I cannot say. I am not as familiar possibly as I should be with the detailed history of the operation of the Board.

Mr. CROSS. May I ask a question just on that?

Mr. WILLIAMS. Yes.

Mr. CROSS. Now, is it not a fact that the Board, in April 1923 or May 1924, brought its pressure on the open-market committee and had them to buy $510,000,000 of Government securities and reduced the rediscount rate from 4½ percent to 3 percent, and, as a result, put the wholesale commodity price level up to 11 percent, and the agricultural products up to 20 percent, and this action was repeated a number of times, and brought about the beneficial effect when they did it?

Mr. ECCLES. I do not know to what extent the open-market purchases and reductions in the rediscount rates had an effect upon the price level. It is true, I think, that, under certain conditions, to reduce the interest rates and increase the supply of money would be effective in increasing business activity, just as to increase the interest rates and reduce the quantity of money would tend to restrict business activities, and slow up borrowing, and possibly start a process of liquidation.

I do not believe that anyone can say to what extent open-market policy can be responsible for recovery or for depression.

The Swedish money management is one of the most interesting, I think, that we have in the world today and possibly has been as successful, or looked upon as being as successful as that of any other country, and the governors of the Swedish bank, in February 1932, made this statement:

It follows that when forming its policy in view of fluctuations in the price level the Riksbank cannot but take into account the causes of such changes in prices. For it is essential to determine whether price movements are caused, e. g., by increased tariffs, altered exchange rates, or a tendency to inflation on the domestic market which may be looked upon as primary in relation to exchange rates. In any such analysis of price conditions, naturally other price indexes besides the Riksbank's own index of consumers' prices will also be taken into consideration. Obviously, in their endeavor to create as stable economic conditions as possible, the governors are also taking into account other factors than mere changes in the price level, particularly conditions affecting productivity and stocks in various industries.

The CHAIRMAN. Gentlemen, it is evident that we cannot continue much longer, in view of the business in the House. I am going to suggest that we adjourn until tomorrow morning at 10:30, and resume with Governor Eccles.

(Thereupon a recess was taken in the hearing until 10:30 a. m., Tuesday, March 12, 1935.)

BANKING ACT OF 1935

TUESDAY, MARCH 12, 1935

House of Representatives,
Committee on Banking and Currency,
Washington, D. C.

The committee met at 10:45 a. m., pursuant to adjournment, Hon. Henry B. Steagall (chairman) presiding.

The Chairman. The committee will please come to order.

Mr. Eccles, you may proceed now. Mr. Williams, do you have further questions?

Mr. Williams. I think not, Mr. Chairman.

The Chairman. All right, Mr. Cross.

STATEMENT OF MARRINER S. ECCLES, GOVERNOR OF FEDERAL RESERVE BOARD—Continued

Mr. Cross. Governor, you agree with the proposition that it is the duty of Congress to regulate the value of money, don't you; that is, Congress, acting through its agency which it sets up, shall do it? Of course, Congress itself does not do it.

Governor Eccles. I think that is a sovereign power given to Congress.

Mr. Cross. In the Constitution.

Governor Eccles. In the Constitution.

Mr. Cross. Now if that is the duty of Congress through its agency which it sets up, which of course, is the Federal Reserve System, don't you think that that agency ought to be independent of any outside influence or interests?

Governor Eccles. The agency should represent the Nation as a whole and should not be under the domination or control of any group or groups.

Mr. Cross. Should not the agency they set up, they being responsible and having the duty to perform, which they have delegated to that agency, should not that agency be independent of any outside agencies that come in with a different purpose in view?

Governor Eccles. It is my view that the Federal Reserve Board should be as independent as it is possible to create a body of that sort, charged with the responsibility of monetary policy in the public interest.

Mr. Cross. Now, Governor, isn't it a fact that the member banks of the Federal Reserve System are constantly wanting to go out in an opposite direction to what a wise policy would dictate, and that they are constantly wanting to inflate when they should not, and constantly wanting to deflate when they should not?

Governor ECCLES. Well, of course, there are a good many thousands of member banks, and I don't believe there is any uniformity of opinion. Inflation is brought about by creating a condition of easy money, expressed in low rates and excessive reserves, in a period when there is great business activity and hence a willingness to borrow.

Mr. CROSS. Yes. But now the point I am driving at is this, isn't it a fact that the member banks, and I am asking this just to get your reaction on this, are inflating when they should not be, and are deflating when they should be inflating? Here is what Governor Harrison of the New York Federal Reserve Bank said in the hearing in 1932, page 53:

It is almost inevitable that the Federal Reserve System, or any central bank, will always have to go contrary to what the banks are doing. When they are deflating, we have to put pressure on them, and when they are deflating we have to boost things up. I think that is what we should do.

Isn't it a fact that the member banks, when they are trying to make money for their stockholders, in times when prices are high, they want, of course, to keep extending credit, credit, credit, and inflating, and naturally their class A directors—and class B directors, who are largely under the control of class A directors—wish to keep going forward and expanding, and don't you think that is a conflicting interest contrary to what the Federal Reserve System is intended to do?

Governor ECCLES. Of course, all I have is the record. From 1926 up to 1930, there was a very small variation in the supply of money. There was no inflation in the volume or the quantity of money from 1926 to——

Mr. CROSS. You refer there to all money—credit money?

Governor ECCLES. That is right; I refer to all money. I include in that demand deposits of member banks and of nonmember banks, and the currency outside the banks, in a word the entire circulating medium.

Mr. CROSS. That is over what period?

Governor ECCLES. That covers the period from 1926 to 1930.

Mr. CROSS. Will you please answer for me this question: There was a vast difference in velocity in those years?

Governor ECCLES. Yes; that is correct.

Mr. CROSS. And the Federal Reserve System can step in and control velocity, can it not?

Governor ECCLES. I don't think that the system has as much influence or velocity as it has on volume of money. I think the velocity of money is influenced more by the tax system than by monetary policy. Velocity slows up as business activity declines, or as deflation develops.

With the national income in 1929 estimated at beyond 82 billions, with the money volume at that time 264 billions, there was a velocity of 3.12; that is, each dollar on the average turned over 3.12 times in the course of the year in the process of making up the income of the community.

Whereas, in 1933, with the national income diminished from 82 billions to 46 billions, and the volume of money reduced from 26.4

billions to 19.9 billions, income velocity had declined in that period to two and a third.

Mr. CROSS. Yes; I understand, that Governor.

Now Governor, isn't it a fact that in order to control the situation you must still have a fixed policy and step in in time? "A stitch in time is worth nine", as one of the governors explained here in his testimony.

In 1929, Governor Harrison was insisting that something be done to stop the inflation, but it delayed too long, until the crash came, and of course then when that happened it was almost impossible to do anything. But it is shown by the record before that they would go out, putting out more securities, putting out more credit, more money, when the commodity prices rose, and then when they would stop that and sell, the reverse was true, because when you sell you take from the member banks their reserves, and that of necessity causes them to rediscount which they don't like to do, and that has the effect, of course, of steadying things, and slowing matters up—keeping them from rediscounting so much.

In order that I may get your reaction on some of these things, I will quote from the testimony of Dr. Sprague who appeared before the committee, I believe, in 1923:

> There would be, I think, an advantage from the passage of the bill. I probably agree with you that the defects in the operation of the Federal Reserve System are not so much errors of judgment they have made, but rather in the hesitating manner in which at times policies have been decided upon and then executed.

Without a goal to go to, and the boards come and go, the present Board may be gone in a short while, and with no goal to go to, the individuals differ and hesitate, and don't you think that is one of the great troubles, not having any goal to go to?

Governor ECCLES. You mean without a specific provision or objective required?

Mr. CROSS. Yes.

Governor ECCLES. You mean required as a part of the law?

Mr. CROSS. Yes; for Congress to set down the purpose, and have it the purpose of Congress, rather than to just turn the Board loose and let them go ahead as they did in 1928, as my recollection of the testimony shows, or 1924, when the Presidential election was coming on and they determined they should have prosperity. So, therefore, they got out and they bought Government securities, $510,000,000, shooting the price level up 11 percent, the farm products 20 percent, and built up commodity prices. Then, after that, they reversed the process, but no election was then coming on.

Now if you have a goal to go to, so they can't just shoot things up and down for some ulterior motive, they are fastened to an anchor, and don't you think it would be wise to have such a provision in the law?

Mr. WILLIAMS. You mean a price level, do you, Mr. Cross?

Mr. CROSS. Yes.

Governor ECCLES. I don't think there should be a mandatory provision to reach a certain price level. It may be of interest in that connection to consider the preamble of the recent law creating the Bank of Canada. It is short and might be considered as a basis for our own. It doesn't definitely fix a price level, but it does fix an objective:

> Whereas it is desirable to establish a central bank in Canada to regulate credit and currency in the best interests of the economic life of the nation, to control and protect the external value of the national monetary unit, and to mitigate by its influence fluctuations in the general level of production, trade, prices, and employment, so far as may be possible within the scope of monetary action, and generally to promote the economic and financial welfare of the Dominion.

Mr. CROSS. They will all say that, of course. Everybody agrees to that, but isn't it a fact that our system is such, as I suggested, we go out and do a thing when a Presidential election is coming on, without any guide as to what the purchasing power of a dollar should be, no relation to the commodity-price level, and then turn them loose? They not only hesitate, but when they do jump, they will jump because of some purpose that is actuating them like a Presidential election.

For instance, let us take Dr. Sprague, who said in his testimony, "I have reached the conclusion that a stabilization amendment might prove serviceable."

Now, that was his testimony during that same time, in 1928.

Don't you think experience has shown those people that they couldn't have a stable policy under those conditions?

Now, I want to get your reaction on some more of his testimony.

Now, Dr. Miller, in the hearings in the Senate, in 1931, said:

> It was my opinion expressed several times, in discussions at Federal Reserve meetings in the opening months of the year 1929, that the Federal Reserve System was drifting, that it was in the midst of a perilous situation without a policy—

and won't that, in your opinion, continue to be the case unless you have got a goal to go to?

Governor ECCLES. I think there should be a goal, but the goal shouldn't be a fixed-price level. I think the goal should be stable business conditions because if you have a goal of——

Mr. CROSS. Who is to determine what stable business conditions are? The Board? They differ here.

Governor ECCLES. Yes; it has got to be left up to the Board, which should not be considered a political body. The law makes the Board a nonpartisan body, on which political parties as such are not represented and appointments to which are for periods of 12 years.

Mr. CROSS. That is true, but you know human nature doesn't change, and it is just like the *Dred Scott case* in the Supreme Court. People don't change. And what we want to do, it is my idea that we get something here where they are anchored to something.

For instance, now, here is the testimony of Governor Harding:

> The American monetary system is a good deal like a ship at sea without adequate equipment of rudders and compass to guide it.

Don't you think they need something to guide them, something to go to?

Governor ECCLES. I don't believe that a fixed-price level is a guide that we should have. We might have a stable price level on the basis of some index, and yet have a great deal of unemployment.

Nobody would be satisfied if you reached a 1926 price level and continued to have a national income of 50 billion dollars instead of 80, and 10 million people unemployed.

Mr. CROSS. Yes, but Governor, the question of unemployment depends upon profits, doesn't it?

Governor ECCLES. Not altogether——

Mr. CROSS. I won't run my factory unless I make a profit, will I?

Governor ECCLES. That is true.

Mr. CROSS. If I make profits, I employ people.

Governor ECCLES. That is right.

Mr. CROSS. And when I employ people that increases purchasing power.

Governor ECCLES. That is right.

Mr. CROSS. And when they have that increased purchasing power they are going to buy, and I will continue to produce, but if you let matters run wide open and I keep expanding, then there is bound to be a reaction, and I throw a lot of people out of employment and I destroy purchasing power.

Don't you think it is better to have a stable purchasing power in relation to a wholesale price level?

Governor ECCLES. This is an interesting chart here that Dr. Goldenweiser gives me. It shows that the price level in England was very stable from 1931 to 1934, but the amount of their unemployment fluctuated considerably.

Mr. CROSS. Yes; I have seen some of the charts.

Governor ECCLES. But I mean——

Mr. CROSS. But, now, Governor, in reference to England, did you read the book by Sir Charles Morgan Webb, in which he in substance says that they regulated gold from 1823 on down to 1914 because they were the only creditor nation of the world and they were carrying the commerce of the world, and that it benefited them as a creditor nation? Did you read that work?

Governor ECCLES. No; I didn't. It seems to me that the Federal Reserve System can control to quite a large extent, not entirely, however, the volume of money, by its power over discount rates and its open-market policy.

Changes in the volume of money in the hands of the people, however, depend also upon the willingness of people to borrow and the willingness of banks to lend.

Mr. CROSS. Yes, Governor; but what I am trying to get at now is to try to show you how confused the Federal Reserve Board has been in the past. Now, for instance, here Dr. Miller testified in 1928, and he says:

> It is my opinion that the Federal Reserve mind at the present time is more perplexed than it has been since the troublesome period of 1920 to 1924; that it is in a state of mental confusion.

Why was that and what is there to keep it from remaining in a state of mental confusion unless you have some goal to go to?

Governor ECCLES. I think there should be a goal, but I don't think the question of prices——

Mr. CROSS. Well, name the goal you think is the proper one.

Governor ECCLES. The goal is stable business conditions and full employment.

Mr. CROSS. All right, they had that all the time, didn't they? It is just the same as the goal in the law now, isn't it?

Governor ECCLES. In the existing law the Federal Reserve Board is not charged with the responsibility of creating a condition either of stable prices or of full employment.

As I understand it, the responsibility of the Federal Reserve System is to supply the credit needs of commerce, agriculture, and industry.

Mr. CROSS. All right, now let us go back to Congress. It is the duty of Congress under the Constitution to furnish money, adequate money, a medium of exchange, and regulate its value.

Governor ECCLES. That is right.

Mr. CROSS. How can Congress regulate that value unless it fixes the price level?

Governor ECCLES. I don't say that prices are not part of the consideration. I think that every effort should be made to maintain stable prices, but stable prices should not be the sole and paramount objective, so that the Board would be directed to maintain stable prices and not to consider total production and employment at all.

Mr. CROSS. Yes; but you take the wholesale index of prices in the market, which are arrived at by taking the mean price, where some may go way up and some way below, but you hold a mean level of prices. Now, if you don't use that, you have got no measure of value, have you? Unless you use that, what other measure of value could you figure for money?

Governor ECCLES. I am not sure that I can say. Gold, of course, hasn't proven to be a very satisfactory measure of value and the buying power of money, measured in goods and services, of course, is the value that the people are interested in.

Mr. CROSS. Governor, I want to ask you this question, You don't think we are helpless in the midst of plenty to feed and clothe, with man power to produce—that we are helpless and these things come on and then there is no help for it? Do you think that?

Governor ECCLES. I stated the other day that I don't believe that any monetary policy alone will result in stable business. Simply dealing with the volume of money, so far as it is possible to influence or affect the volume of money through the controls that the Reserve System has, cannot give you full prosperity. This is because distribution of wealth production——

Mr. CROSS. Yes.

Governor ECCLES. Is a very important element, and that gets back to the problem of the tax system. The banking system can influence the volume of money——

Mr. CROSS. Now, Governor, I understand that.

Governor ECCLES. And the tax system, it seems to me, must influence the velocity of money.

Mr. CROSS. Well, now, Governor, let me get this. Of course, I don't think the tax system is so important that we are ever going to get anywhere with it except to stop enormous fortunes by higher taxes in the upper brakets. But now suppose you have got a small community such as they had in the early days, when people would come in to the fairs and exchange their products, their things; and they followed the law of supply and demand perfectly, did they not?

Governor ECCLES. Yes.

Mr. CROSS. Now, the dollar or the monetary unit of a country is supposed to reflect as a mirror the workings in that country of the law of supply and demand for things; so if the country has plenty of everything, if that law of supply and demand were followed just like they would come together and exchange what they have, everybody would have plenty and would not be hungry and distressed and ruined and broke. Now, don't you think the monetary unit ought to perform that function?

Governor ECCLES. The monetary unit ought to; but the monetary unit can't be made to perform that function simply through monetary policy. Placing the means of payment in the hands of people who will spend is the thing that determines employment, business activity, and price levels.

The ownership of the money is an important element in the use of the means of payment. If there are corporations, owning large unused balances of funds, which cannot find a profitable place to use or invest those funds, those funds don't go into circulation.

Mr. CROSS. That is true, but if you had prices at the point where they could invest and make some profits——

Governor ECCLES. But the——

Mr. CROSS (continuing). They would invest.

Governor ECCLES. The prices would not induce them to invest. It is the profit opportunity that induces them to invest, and where you already have a great unutilized capacity because the people as a whole lack the buying power to purchase the goods produced, there is no incentive to invest in further capital goods.

Mr. CROSS. Governor, don't you think the whole theory is that we are helpless—and so far as the Federal Board is concerned we needn't look to that for relief, not for much relief—that there are all kinds of things out yonder that you can't reach and touch, and therefore we just have to follow along?

Governor ECCLES. No; I think that the monetary factor is 1 of the 3—1 of the 3 important control measures of our capitalistic system. The volume of money can largely be controlled through a banking system.

The distribution of funds which is a factor in their velocity must be controlled through the income-tax system, and employment must be regulated through a public-works system.

When the volume of money is adequate to support a certain price level for a given volume of production, and unemployment begins to develop, and as a result prices begin to decline, it is likely to be because productive facilities are out of balance with the consumers' buying power, and velocity of money is declining.

Mr. CROSS. Yes; but you don't want to let it get to where that happens. If you are going to let contractions take place, and as a result all over the country where bonds have been issued for school districts, road districts, municipalities—and you say that the dollar today or next month will double in purchasing power, so that that individual must pay twice in real value because there is no value in money so far as keeping and clothing is concerned—he must pay twice as much in real value to pay the taxes and to pay the interest on his mortgage if he has one—it becomes an impossibility. It means a general liquidation and discontent and trouble and threatened bankruptcy.

Governor Eccles. It does, if you let the national income decline. The purpose of our tax system and the public-works system is to keep up production when private business fails to keep up full employment. The loss to the Nation, when the national income declines through unemployment, is a loss we cannot afford.

Mr. Cross. And your idea is to do it through public works, public enterprises?

Governor Eccles. That is right.

Mr. Cross. Each time you do that you borrow a good many billions of dollars, don't you?

Governor Eccles. You wouldn't have very much to do if you did it at the right time, before you allowed deflation to proceed very far. The amount that it would require at the beginning——

Mr. Cross. That is, more or less, just a guess, isn't it? If you keep on running these billions up, who is paying that tax but the public? And if you get 50 billions and a hundred billions, the fellow who pays it has got to collect it back off the people. There are bonds which they have got to collect off the people in taxes.

Governor Eccles. Who pays the difference between the 85 billion of national income and the less than 50 billions of national income—who pays that 35 billions?

Mr. Cross. The fellow who has got the loans on his land. The people who have the loans foreclose the mortgages and get the land, and they keep it until they can resell it to these fellows again, those who can buy. They have to take that loss. But my idea is to get a stable purchasing power in your monetary unit, so that it can't happen that if a man goes out and puts up a factory and has to borrow money, and he borrows this money and builds the factory and expands it, and the first thing he knows the purchasing power of that dollar doubles and trebles, and he is sunk.

Governor Eccles. You may fix a stable purchasing power as a requirement of the monetary policy of the Federal Reserve Board, or any other Board, but I don't know what methods they could use to maintain or to reach that objective.

Mr. Cross. Don't you think it could be kept by using the rediscount rates? In other words, using the reserves—the reserves in the banks—couldn't you use the open-market operations?

Governor Eccles. No monetary policy alone by simply attempting to regulate the volume of money will maintain a stable national income or——

Mr. Cross. I don't say "volume" alone. I mean volume and velocity. Can't you control it through the rates, loaning of the reserves, and rediscount rates and open-market operations—wouldn't that have an effect on the velocity as well as the volume?

Governor Eccles. To the extent that a reduction of rates and an increase in the supply of money would tend to stimulate velocity; yes. But so long as there is an inequitable distribution of wealth production which results in excessive saving we will have depressions.

Only by pulling back that part of our savings that we cannot profitably use in new capital goods and using those funds to give employment to those who become unemployed can we maintain a balance.

The Government must be the compensatory agent in our economy through the money system, through the tax system, and through a public works system.

Mr. Reilly. I think the committee will have to go now. The committee will adjourn now.

(Whereupon, at 11:25 a. m., an adjournment was taken until Wednesday, Mar. 13, 1935, at 10:30 a. m.)

BANKING ACT OF 1935

WEDNESDAY, MARCH 13, 1935

HOUSE OF REPRESENTATIVES,
COMMITTEE ON BANKING AND CURRENCY,
Washington, D. C.

The committee met at 10:30 a. m., Hon. Henry B. Steagall (chairman) presiding.

The CHAIRMAN. The committee will come to order. Mr. Cross, you may continue with your examination of Governor Eccles.

STATEMENT OF MARRINER S. ECCLES, GOVERNOR FEDERAL RESERVE BOARD—Continued

Mr. CROSS. Governor, you may have thought, from my questions, that I am in a critical mood. I want to say I think this bill provides for a tremendous improvement over what we have, and I think you are a big improvement over governors we have had heretofore; so do not think I am criticizing you.

Check money, for all practical purposes, performs the functions of legal tender money, does it not?

Governor ECCLES. Yes; it does.

Mr. CROSS. The easier credit is, the greater the volume of credit, and the greater the number of check dollars, the less the dollar will buy; is not that so? When credit is easy there are plenty of check dollars, check money, and that means prices are up, does it not, and therefore the purchasing power of the dollar is down, is it not?

Governor ECCLES. That would be expected to follow. The easy money——

Mr. CROSS (interposing). That is almost axiomatic, is it not?

Governor ECCLES. Easy money, through the banking system, by creating low interest rates——

Mr. CROSS (interposing). That is a fact, is it not, that it is axiomatic; that when credit is easy there is a large volume of credit, and that inevitably means that times are good and prices are up, and profits are up, and people are borrowing, and there is a supply of check money like there was in 1928 and 1929?

Governor ECCLES. Of course, your general prices go up when means of payment in the hands of people who will spend increase faster than production.

Mr. CROSS. Is the proposition I put to you true or not?

Governor ECCLES. I think that is generally the case, but it certainly is not always so. Witness the present situation.

Mr. CROSS. Then the tighter credit is, the less credit there is, the fewer number of check dollars there are; that is true, is it not?

Governor ECCLES. Yes; I think that is true.

Mr. CROSS. That being the case, then the more the dollar will buy, will it not?

In other words, as credit dries up, check money, the purchasing power of the dollar increases, does it not?

Governor ECCLES. Not always.

Mr. CROSS. Now, Governor, do you not think the velocity theory of money is more or less a meaningless fiction?

Governor ECCLES. No.

Mr. CROSS. Now, along in 1928 and 1929 we had a situation where our credit money, our check money did about 90 percent of the traffic duty of the country, did it not?

Governor ECCLES. I think those were the estimated figures. I do not know how accurate they are, but that would be approximately correct.

Mr. CROSS. That is what they put it at, about 90 percent?

Governor ECCLES. Yes.

Mr. CROSS. Now, if all of that check money had vanished or dried up, 90 percent of the money had dried up, the traffic of the country had vanished, had it not?

Governor ECCLES. Unless the deposits were drawn out in currency.

Mr. CROSS. If you have 5½ billion in currency, we will say, and we are talking about the check part of it, and practically 90 percent of it was gone, then you had left your legal-tender money, which was about 5 billion, we will say?

Governor ECCLES. Yes.

Mr. CROSS. Now, if nine-tenths of that money was check money; that is, 90 percent, and you had 45 billions in check and 5 billions in legal-tender money, and the 45 billion had vanished, it is not to be assumed that it did not all go out?

Governor ECCLES. I do not know that I understand your point.

Mr. CROSS. If your check money had vanished like the mist—it is a kind of phatom money, but it does the work of the country in all its functions. Say that 90 percent of the traffic was done through check money, and we will say that is nine-tenths of the total, and one-tenth of the business was done, we will say, with legal-tender money, there being nine times as much check money as legal-tender money, and the check money disappears, and you have only left your legal-tender money, of course, then 45 billion in check money would have vanished, would it not?

Governor ECCLES. If it disappeared, that would be the case.

Mr. CROSS. If your credit dried up like the mist, then it would disappear, would it not?

Governor ECCLES. Yes.

Mr. CROSS. And if you then had 5 billion in legal-tender money, and then that 5 billion had kept on performing the duty of transferring the property and the goods of the country at the same speed at which it was traveling when you had your 45 billion of credit money, it would have been doing only one-tenth of the amount of traffic duty that was being done by the whole amount of credit money plus the currency or legal-tender money, would it not?

Governor ECCLES. If the total amount of money is reduced by nine-tenths, then that one-tenth or the remaining money would be doing——

Mr. CROSS (interposing). Traveling as fast as it always had been, it would have been one-tenth, would it not?

Governor ECCLES. I do not know whether it would have been traveling that fast.

Mr. CROSS. Assuming that it would be traveling as fast as it was in 1928 and 1929, with the 45 billion gone, it was doing only one-tenth of the work; if it was doing the same amount of work after the crash as before the crash, is not that true?

Governor ECCLES. If the velocity of the funds does not change, if the volume is reduced nine times, of course, your volume times your velocity would be one-tenth of what it was.

Mr. CROSS. Surely; that is simple mathematics.

Governor ECCLES. Yes.

Mr. CROSS. Now, is it not a fact that in figuring velocity you give credit to the work being done by the credit money when times are good, and the legal-tender money, in fact, is not going any faster than afterward, except that the credit money vanishes and you no longer can figure what the credit money is doing to the legal-tender money? In other words, you give credit to the legal-tender money, and when times are good you say the currency amounted to 5 billions, and it was going at such and such a speed; but you are giving credit to the legal-tender money for all that is being done by 45 billions of credit money, are you not? Is not that the way you count velocity?

Governor ECCLES. No; it is not.

Mr. CROSS. How do you count it? You cannot tell how often it swaps hands.

Governor ECCLES. The national income is the number of times that your volume of money——

Mr. CROSS. Of what money?

Governor ECCLES. All money.

Mr. CROSS. All right.

Governor ECCLES. There is no distinction so far as the working of the money is concerned between currency and checking accounts; they both perform the same function in the money system. I mentioned yesterday the difference in the velocity figures.

Mr. CROSS. Let me get this concretely, if I can, so I can understand it.

Take, for instance, the situation in 1929. At what velocity do you say money was traveling at that time?

Governor ECCLES. What would be termed as the income velocity; that is, the relationship of money to the national income——

Mr. CROSS (interposing). What was the velocity of money at that time? Say we had 50 billion, counting the credit money and the legal-tender money, what was the velocity at which all of the 50 billion was traveling?

Governor ECCLES. We had, in 1929, 26.4 billions——

Mr. CROSS (interposing). Of all money?

Governor ECCLES. Of all money.

Mr. CROSS. Checking——

Governor ECCLES (interposing). And currency; that is right. That eliminates, of course, your interbank deposits. These are the figures I got from the Federal Reserve statistical division.

Mr. GOLDSBOROUGH. That does not include savings money?

Governor ECCLES. No; you cannot include savings money any more than building and loan money.

Mr. CROSS. The checking accounts, plus the legal tender, amounted to 26 billions?

Governor ECCLES. That is right. The national income was 82 billions, according to the Department of Commerce figures, or, to be exact, 82 billion 300 million.

Mr. CROSS. What do you understand as the national income?

Governor ECCLES. It represents, as I understand it, the income received in the production of all goods and services.

Mr. CROSS. What do you count as goods?

Governor ECCLES. It would be capital goods as well as perishable goods, buildings, factories——

Mr. CROSS (interposing). And lands?

Governor ECCLES. Equipment; no land.

Mr. CROSS. Just buildings?

Governor ECCLES. Buildings—factories and equipment; all kinds of goods. The total volume of bank debits was estimated to be between 1,000 and 1,200 billion. In other words, the actual turnover of money was about 40 times a year, I think.

Mr. CROSS. Governor, now you say capital goods, and then you say the income was 80 billion. Where do you get the income at 80 billion? What do you mean by that?

Governor ECCLES. The money value.

Mr. CROSS. Of all capital goods, buildings, and so forth?

Governor ECCLES. The money value of what was produced in any particular year. If in the year 1929 the value of all foods, clothing, and capital equipment of all kinds produced in that year was a certain amount, that would be income, after the elimination of duplications—for instance, if you start to figure the value of wheat that is sold to the miller, then the miller sells to the wholesaler and the wholesaler sells to the retailer. When you take the total check transactions, they run between a thousand billion and twelve hundred billion, and it takes into account all of those relationships. But the national income only takes into account what is produced, and by considering it once, and not in the various transactions through the methods of production and distribution. That is the national income.

Mr. CROSS. I am getting at the question of velocity. You say you had 26 billion of all kinds of money. Upon what basis do you figure the velocity of the 26 billion?

Governor ECCLES. With that amount of money, with 26 billion, we had a national income of 82 billion, 300 million; or we had there what is termed an income velocity of 3.12. In other words, the total volume of our currency and checking account went into the total national income that year 3.12 times.

Now, we come down to 1933, when the national income was 46 billion, 800 million, and our money had diminished from 26 billion, 400 million to 19 billion, 900 million.

Mr. GOLDSBOROUGH. When was that, 1933?

Governor ECCLES. Yes.

Mr. GOLDSBOROUGH. The other year was 1928?

Governor ECCLES. The other year was 1929. There was very little difference between the 1928 and 1929 figures. And with the income of 46 billions, 800 millions and the deposits and currency in existence during that year of 19 billion 900 million, the income velocity was 2.35. We have not the figures for 1934, but that is expected to show a decrease. We know that the volume of deposit currency has been very substantially increased as the result of three factors—the budgetary deficit, gold imports, and the reduction of currency in circulation as the result of the dehoarding.

Mr. CROSS. Your gold is all stabilized, is it not?

Governor ECCLES. That is right. But the gold comes in from abroad to take care of the unfavorable trade balances of Europe and the rest of the world. The only way they have been able to take care of their unfavorable trade balances is to pay us in gold. There has been about 1 billion 300 million of gold coming into the country in 1934. Those three factors increase your deposits. There would have been a greater increase than that had there not been a shrinkage of loans and investments of banks, outside of Government bonds. As I recall the figure, it was around 6 or 7 hundred million dollars. The result was an increase in deposits and currency by about $4,000,000,000, as I recall the figures.

Mr. CROSS. You say an increase in currency?

Governor ECCLES. In deposits. I do not think there was any increase in currency.

Mr. CROSS. As to this billion dollars of gold that comes in here, do you mean to say that would make an increase of a billion dollars of back-bone or pocket money?

Governor ECCLES. An increase in bank deposits in that amount; yes, sir.

Mr. GOLDSBOROUGH. You said the amount in 1933 was forty-six billion, eight hundred million. Have you the amount in 1934?

Governor ECCLES. No; I have not. It is estimated as over fifty billion, but the ratio of the national income to deposit money will show up considerably less than it was in 1933, showing that with the increase in the volume of money there has been a decrease in the velocity of money; that the increased volume has not increased the national income in proportion.

Mr. CROSS. What is the increase for 1934 over 1933?

Governor ECCLES. I have not the exact figures.

Mr. CROSS. In the volume of money?

Governor ECCLES. It would just be an estimate. But I think it is around four billions. That is the increase of 1934 over 1933.

Mr. CROSS. What is the difference between the check money of 1929 and the check money of 1933?

Governor ECCLES. I do not know just what you mean. You mean in amount, the actual amount of check money in 1929 as compared with the check money in 1933?

Mr. CROSS. Yes.

Governor ECCLES. There was a difference of 7½ billion between 1929 and 1933.

The CHAIRMAN. Let me ask you a question right there, to make sure I understand it. Do you mean to give the total figures for the entire country? Are your figures predicated on calculations that embrace all of our banks?

Governor ECCLES. Oh, yes.

The CHAIRMAN. That is what I understood, but I wanted to make it clear.

Governor ECCLES. Yes; the member and nonmember banks.

Mr. CROSS. You do admit that the dollar as it is today, untied to any price level, is no measure of value, do you not? In other words, its purchasing power is constantly expanding and contracting?

Governor ECCLES. That has always been true.

Mr. CROSS. You have an exact measure of length, for instance, in the linear foot; and you have an exact measure of weight in the pound. You also have an exact measure of volume in a cubic foot.

But you cannot measure volume by weight. You might have two cubes of exactly the same dimensions, one made of cork and one of lead, but if you attempt to measure them by weight you would not get any idea about it at all, would you? That is a simple question, it seems to me. I am talking about the simple question of measure. You could not get any idea as to the size of those two cubes by using the measure of weight, per pound, could you?

Governor ECCLES. No.

Mr. CROSS. One would probably weigh a hundred or a thousand pounds more than the other.

Now, you attempt to measure the value by the pure unit of weight, do you not, with so many grains of gold, for instance?

Governor ECCLES. I do not think that a fixed gold content results in stable prices.

Mr. CROSS. I do not think it does either.

Governor ECCLES. It never has in the past.

Mr. CROSS. I do not think so, but we put the price at $35 an ounce, whereas it used to be $20.67.

Governor ECCLES. That is right.

Mr. CROSS. So it is no measure of value, is it?

Governor ECCLES. I do not think so.

Mr. CROSS. Now, the only way to get a measure of value is by a price level; do you not think so? Do you have any other suggestion as to a measure of value outside of a price level?

Governor ECCLES. Do you mean by some index figure?

Mr. CROSS. Yes; or some wholesale commodity price level.

Governor ECCLES. That gives you a measure of value, but it is not what you want.

Mr. CROSS. It does give a measure of value, does it not?

Governor ECCLES. Yes; it does give a measure of value.

Mr. CROSS. Now, if you would tie your monetary unit of the dollar, as we call it in this country, to the price level, you would get a measure of value, would you not?

Governor ECCLES. I do not know just how you would tie a monetary unit to the price level.

Mr. CROSS. I say, if you do do it.

Governor ECCLES. Yes; if you can.

Mr. CROSS. I am saying, if you can you would get a measure of value. As it is, you have not any measure of value. Do you know of any other method by which you could approach a measure of value?

Governor ECCLES. I think that a stable price level is a desirable objective.

Mr. CROSS. I know; we are talking about the price level. What other way is there?

Governor ECCLES. I should not say that I know of a way to get a stable price level, and at the same time get a stable business condition, which is a condition of full employment and prosperity.

Mr. CROSS. Of course, that is what we all want to do, if we can. Let me ask you this question: As the result of this instability, fluctuation, expanding, and contracting in the purchasing power of the dollar, and consequently affecting the earning power of a dollar, credit, or credit money, or check money is very sensitive, timid, and easily affected by any economic disturbance, is it not?

Governor ECCLES. I do not think that check money is more sensitive than any other money.

Mr. CROSS. All right. Any kind of money is sensitive, is it not; any other money, like legal tender?

Governor ECCLES. Yes; that is right.

Mr. CROSS. If you can stabilize it on a price level, it will become a dependable measure of value and relieve credit from the instability and constant fear to which it is now subject, will it not?

That is, if a man knows that he will know that he will have a dollar to spend in the aggregate, and would take into consideration the figures you use in determining the wholesale commodity price level, and he knows it will hold up the purchasing power and the value, would not that tend to stabilize and give confidence?

Governor ECCLES. I think it would.

Mr. CROSS. The only method by which we know how to do that are the levers you have in this bill, rediscount and open-market operations.

Governor ECCLES. Open-market operations, yes; that is right.

Mr. CROSS. Now, with those three levers, do you not think you could approximate holding the purchasing power of the dollar stable with the price level?

Governor ECCLES. Insofar as that can be done through monetary action, I think you could accomplish that.

Mr. CROSS. We know of no other action——

Governor ECCLES. In that connection let me read a short statement I have here which seems to me to cover this question.

Professor Olin, a Swedish authority—and they have possibly had more experience in this question of managed currency——

Mr. CROSS. He has not had a long experience because this just started recently.

Governor ECCLES. That is true of the entire world. As a matter of fact, as to the problem of central banking and money management, there is plenty to learn about it. There is no country which has had any experience for any great length of time.

Mr. GOLDSBOROUGH. There is plenty to unlearn about it, is there not?

Governor ECCLES. About the question of managed money?

Mr. GOLDSBOROUGH. About the way to handle central banks. Can you answer that?

Governor ECCLES. I do not know enough about the history of central bank operations. Of course an automatic gold standard has been a guide in the operation of the world's banking system in the past, up to the time of the war.

Mr. Cross. Controlled banking, was it not?

Governor Eccles. Very largely.

Mr. Cross. I wish you would read that book written by an Englishman.

Governor Eccles. This man says, after surveying the Swedish experiment in an article in index, volume 8, that—

> A business cycle policy that aims at as full and regular a utilization of the productive forces as possible, that is a maximization of the real national income per head of the population over a long period, is bound to take many other factors into account besides the development of prices; that is to say, it can not be based on the idea of stabilizing any particular price level, especially if the latter has been brought by an immediately preceding depression, but of equilibrium with the other parts of the price system.

Mr. Goldsborough. Which means that there are two factors: One is the factor of a scientific monetary system and the other is the factor of distribution of production. That is what he is talking about, is it not?

Governor Eccles. That is right; I agree with that.

Mr. Cross. My idea is that this bill is all right, except that there are two amendments we ought to have.

I think it is up to Congress to provide for the regulation of the value of money, through our agent, which is the Federal Reserve Board.

And since, as I think I showed here yesterday, the member banks are in the business of making money, and the 12 Federal Reserve banks have that idea, too, and as Governor Harrison, of the New York Federal Reserve Bank, said, the very time the Federal Reserve Board wants to hold down inflation or credit, the banks insist on expanding it, and the very time the Federal Reserve Board wants to boost credit, the banks tend to shrink and contract it. As long as they own the stock of the Federal Reserve banks, with their class A and class B directors, with all those influences working, I am afraid there will be cross-purposes, and I think they should be in a position, without any outside influence, to act for the whole people all the time. That is why I believe that the stock should be taken over and owned by the Government in those Federal Reserve banks.

Another amendment which I think should be adopted is this: I think we ought to give them a goal to work to. It is the best we have got; it might not be a perfect compass, and no doubt is not by any means; yet I think we ought to have some kind of a price level, whether you take 50 or 100 commodities, or 784, or use the economists' index, we ought to have some goal set for them to anchor on. We can try it, and if it does not work we can change it.

I notice that England has let the pound slide down, no doubt with the idea of getting constantly under our dollar, giving her the advantage. I think we ought to take 20 percent above the wholesale commodity price level of 1926. If we take that and go very little below that, I think we should do it, because if England or any other country is constantly trying to slide under us and cheapen their money to give them an advantage in the export trade, I think we should be in a position where we can follow along with them.

But I am sold on the question of tying the dollar to the price level within a certain latitude.

Then I will tell you another thing I think about this bill, at least in connection with the psychological effect. You have 40 cents on the dollar back of the Federal Reserve note, and I think if you would make it, say, 35, and provide, say, for 10 cents in silver certificates, you would be taking a wise step.

I realize if you can have stabilized and controlled currency you do not need any metal at all, except as a matter of foreign traffic. But as long as the balance of trade is in our favor we do not even need that because they have to be constantly buying money to pay for our goods.

Of course, if we become an importing nation and the balance of trade is against us, we would have to use a different currency.

Governor ECCLES. As to this question of fixing the price level in the bill, I personally would not like to see that. I would suggest that, in lieu of a fixed price level, something of this sort might be put in the bill, as indicating the direction or objective to which the Federal Reserve Board would be required to reach:

It shall be the duty of the Federal Reserve Board to exercise such powers as it possesses to promote conditions making for business stability and to mitigate by its influence unstabilizing fluctuations in the general level of production, trade, prices, and employment, so far as may be possible within the scope of monetary action.

Mr. CROSS. That is a lot better than what we have in there now.

Mr. GOLDSBOROUGH. Would you feel like including in that a statement indicating that the Board should also direct its attention toward using its power in such a manner as to absorb the unemployment? You have done that in a way, but it is not quite clear.

You know there are experts who I think are worthy of attention who claim that you can use monetary powers in such a way as to absorb unemployment to a certain point, and that when you do that you then have notice that you have raised your price level to the proper position.

I am wondering if you could put some sort of legislative direction as that in what you have said. I think myself you have done very, very well in what you just pointed out as a possible amendment.

Governor ECCLES. I am trying to avoid a rigid requirement in the law that may be impossible of accomplishment, and hence may cause embarassment. I would like to see enough flexibility in the law; because I do not believe that we can deal with our money, economic and social problems, and they are all interrelated, as an exact science. You have too many emotional factors to contend with, and when you talk about the problems of business stability, stable prices, full employment, and so forth, you have to take into account factors other than purely the mathematical or mechanical factors of money.

Mr. GOLDSBOROUGH. Will you read that proposed provision again?

Governor ECCLES. It says:

It shall be the duty of the Federal Reserve Board to exercise such powers as it possesses to promote conditions making for business stability and to mitigate by its influence unstabilizing fluctuations in the general level of production, trade, prices, and employment, so far as may be possible within the scope of monetary action.

Mr. GOLDSBOROUGH. You are stating the objectives.

Governor ECCLES. That is right.

The CHAIRMAN. The present law was designed, of course, to promote sound business conditions and laid down a guiding rule of policy somewhat along the line of your suggestion, although not so comprehensive.

Under the present law the language is:

The board of directors shall administer the affairs impartially—

And so forth—

and extend accommodations such as may be safely and reasonably made, with due regard to the claims and demands of other banks, and to the requirements of industry, commerce, and agriculture.

It is not so comprehensive, but it is in the law, and to a certain extent it is a recognition of the ends to be desired.

Personally, my view is that you have expressed the true policy, and that is to take the general results that would be desired as the guide and standard of activities.

In connection with Mr. Cross' inquiries, what is the relation between actual currency, or Government currency, or Government money, and check money and its velocity?

Governor ECCLES. So far as their functioning and purchasing power are concerned, there is no difference. They serve the same purposes as a means of payment. Currency is used largely as a matter of convenience in meeting pay rolls, in retail buying by the man with a small income, where the checking account is too expensive, or is not wanted. Even in cases where checking accounts are used, particularly is it true now with service charges and the check tax, people will cash checks for a larger amount and pay bills with currency rather than pay all bills with small checks. The use of the check has been greatly diminished.

The CHAIRMAN. What I am undertaking to develop is the necessary part that must be played by actual money in the present scheme.

Governor ECCLES. I do not know that I quite understand you, Mr. Steagall.

The CHAIRMAN. We cannot get away entirely from the use of actual money, even though we do 90 percent of our business by the use of bank checks.

Governor ECCLES. That is right. We possibly use the bank check more than any other country.

The CHAIRMAN. As we cannot rest our banking structure entirely on air, we have to have a basis for that. What I am directing your attention to and asking you to discuss is the proper basis, and the necessity for it; how far the development of a sound bank-check currency must rest upon the use of actual currency and the opportunity to redeem the bank check in actual currency.

Governor ECCLES. Of course, a bank has to be in a position to pay its deposits in currency. At one time it was required to pay it in gold, and of course we know what trouble that got us into. The bank is required to pay the deposit in currency. We found that, while banks were closing and the great deflation was going on, that a great many people and corporations wanted their deposits in currency, to such an extent that the amount of currency outstanding passed the all-time record of the use of currency, even when business was very active. It exceeded over seven billions of dollars, at a time when our business activity was about 50 percent of what it normally is, showing that a very substantial amount of that currency was not drawn out for current or immediate use but was drawn out for fear of loss through bank failures, to be held in safekeeping. We must prevent bank failures so far as is humanly possible. When people found they could get their money if they wanted it, confidence was reestablished in the banking system, and the amount of currency outstanding greatly diminished.

The CHAIRMAN. You say we got into trouble under the system under which we had to redeem everything in gold. Just what do you mean by that?

Governor ECCLES. I mean that when people demanded payment in gold, since gold was used as a reserve for our money system, it did not take the withdrawal of very much gold to force a suspension of gold payments and to put an embargo on gold.

The CHAIRMAN. Let me ask you this question, "Were we forced to suspend gold payments?"

Governor ECCLES. Yes; I think we were, not only because of withdrawals but also because of our price and debt structure and the measures that were absolutely necessary to correct it.

Mr. CROSS. Gold was leaving the country very rapidly, was it not?

Governor ECCLES. Yes; it was leaving the country very rapidly; not only that, but it was being drawn out by corporations and individuals at a rapid rate.

The CHAIRMAN. When we suspended payment we had an unprecedented amount of gold on hand, did we not?

Governor ECCLES. At the time we suspended we had lost a great deal of gold.

The CHAIRMAN. We had lost a great deal of gold, but we still had more than half of the world's gold, did we not?

Governor ECCLES. No; we had about 40 percent of it.

The CHAIRMAN. But we had certainly something like a third—an undue proportion of the world supply.

Governor ECCLES. But at the rate at which it was being drawn out it was evident that we might soon reach a position where it would be necessary to dispense with gold payments and put an embargo on, and therefore, why permit a preference to those people and corporations who demanded payment in gold?

The CHAIRMAN. Had we not always been able, by the use of Government credit, to get our hands on all the gold we needed to redeem the outstanding gold obligations? I do not mean it was a desirable thing to do; far from it; that is not my view of it. I am simply stating the facts.

Governor ECCLES. We had panics in the past where we could not even pay in currency, up until the time we got the Federal Reserve System set-up. I remember the panic of 1907, when they suspended payment in currency and used clearing-house certificates.

The CHAIRMAN. There was not any difficulty in redeeming the currency in gold, was there? Of course, we have always had occasion when quite a number of banks could not pay out any kind of money because they could not get it. But there never was any time in those situations when there was any difficulty about exchanging currency for gold, if you wanted it?

Mr. GOLDSBOROUGH. In the panic of 1873 the gold reserve was depleted.

Mr. CROSS. And there is always a vast difference between dollars and commodities. The whole world was trying to get back, and the whole world was scrambling for it.

The CHAIRMAN. I am speaking about what did happen when Mr. Cleveland was unable to get gold.

Governor ECCLES. I think he negotiated a loan with Mr. Morgan.

The CHAIRMAN. As a matter of fact, we maintained our gold standard with $150,000,000, did we not? That leads to this question: I am not one of those who think that our gold-standard system was ideal; that is one of the things I think it might be said we had to unlearn. Whether we have learned anything or not, I will not attempt to say.

But I think it will be agreed that is one of the things we have unlearned.

But I was going to ask you this question: Why was it we could not redeem in gold? Why could we not go along with that system? Why was it not safe to continue it? That is what I am talking about.

Governor ECCLES. For the reason that——

The CHAIRMAN. Is not this the fact, Governor, that the trouble was there was not enough gold?

Governor ECCLES. Of course, there was not a fraction of enough gold in this country or in the world to meet the gold obligations.

The CHAIRMAN. We did not have enough gold.

Governor ECCLES. Not a fraction of enough to meet the obligations, but that is always the condition. It works all right so long as no questions are raised about redemption but in case of panic there is not enough gold and payments have to be suspended.

The CHAIRMAN. Let me ask you another question. Was not that the chief difficulty with the banks when they found themselves in the situation where they could not meet their obligations in currency, that the currency was too scarce?

Governor ECCLES. No; the currency was not scarce, because the banks had assets with which they could go to the Federal Reserve System and get credit, and they could have drawn down currency. There was no shortage in the amount of currency available to a bank, if the bank had assets acceptable to the Federal Reserve bank.

The CHAIRMAN. That is the point. The fact was they had deposits, as you have said, I think, amounting to 26 billion, or say 25 billion in round figures, that were in the nature of demand obligations. But they had only a trivial amount in comparison to their deposit obligations of assets upon which they could apply for and obtain actual currency; is not that right?

Governor ECCLES. That is right.

The CHAIRMAN. And the fact was, as against 25 billion dollars of demand-deposit obligations for which the banks were responsible, they had only in the country something like 5 billion dollars in which to meet that responsibility. And for all their cash obligations in the Nation they had only such a portion of actual cash that they could have paid, plus their discountable or rediscountable paper, and the amount of rediscountable paper had gotten to the point where it was trivial as compared with the amount of obligations they had.

Governor ECCLES. Oh, yes; and the amount of rediscountable paper, even in 1928 or 1929, was only a fraction of the total deposit liability.

The CHAIRMAN. As a matter of fact, the banks now owe deposit obligations that I believe you say amount to about 25 billion.

Governor ECCLES. That is, demand obligations.

The CHAIRMAN. The amount has increased from 19 billion to 25 billion of demand obligations outstanding against the banks?

Governor ECCLES. That is right.

The CHAIRMAN. And they have available today to meet those demands something like three-quarters of a billion dollars of actual money; is not that about right?

Dr. GOLDENWEISER. You mean cash in vaults?

The CHAIRMAN. Yes.

Dr. GOLDENWEISER. That is about right.

The CHAIRMAN. That is what I am talking about. That is a fair way to state that position, is it not?

Dr. GOLDENWEISER. No.

The CHAIRMAN. Of course, they have in addition to the cash available to them their privilege of obtaining currency on their assets, which is still limited to a certain quality of assets.

Governor ECCLES. Besides the cash value which they have in their vaults, they have their balances in the Reserve banks, which are the equivalent of cash, the reason being that they can draw down currency against those balances with the reserve banks, and those balances today are over 4 billion dollars.

The CHAIRMAN. Then they would be entitled to have Federal Reserve notes issued.

Governor ECCLES. That is right; against those balances.

The CHAIRMAN. That is, their excess balances?

Governor ECCLES. They are required, of course, to carry a minimum balance.

The CHAIRMAN. But they could not utilize that.

Governor ECCLES. They could draw down their currency against their excess balances, but they would be penalized if their balances were below the legal requirements.

The CHAIRMAN. Which, of course, means that the legal requirements could not be utilized, as a practical proposition.

Governor ECCLES. Yes. It could be utilized subject to the payment of a penalty for any deficiency in reserves.

The CHAIRMAN. So they would be limited to their excess balances and their cash on hand, and such paper as they would have upon which they might obtain currency.

Governor ECCLES. That is right.

The CHAIRMAN. Does it not follow that the banks found themselves in difficulties in undertaking to meet their demand obligations growing out of the scant supply of actual currency, as compared with the demand upon that supply, not alone by the banks but demands from various sources in the Nation?

Governor ECCLES. The banks found that they were unable to meet their deposit liabilities in currency because of the lack of assets which the Reserve banks would accept. That reduced the amount of currency that they were able to pay out, and the very fact that many of them were unable to meet that demand caused the whole Nation to want to convert their deposits into currency.

As soon as the people found that they could get their deposits in currency, as the result of the emergency banking act of 1933 permitting the banks, not only the member but also the nonmember banks, to get credit, and hence currency from the Reserve banks upon all of their sound assets, the people of the country did not want their deposits in currency. The reverse action developed and the currency which they had wanted when they thought they could not get it began to come back into the banks and increased the deposits of the banks by an amount of from a billion and a half to two billion dollars.

So that it seems to me that the lesson that that experience should have taught is that the Federal Reserve Board should have some discretionary power in the making of rules and regulations that will permit the Federal Reserve banks to accept the sound assets of banks and thus stop what otherwise would be a repetition of what we have had in the way of a credit contraction and the reduction of our deposit money.

The CHAIRMAN. Governor, it is unquestionably true that we have, to a large extent, restored confidence in the banks, and money in hoarding, and no doubt considerable sums that have been withdrawn for legitimate uses, because of the distrust of the banks, has been returned to the banks.

But does not that result mainly from the insurance of bank deposits?

Governor ECCLES. I think that is a very important fact.

The CHAIRMAN. Let me ask you another question.

Governor ECCLES. I think that is particularly——

The CHAIRMAN. We will not have accomplished much, no matter how fully we accomplish that, if we only succeed in restoring confidence in banks so that the public will leave its funds in banks for safekeeping.

That would be a thing to be desired, and it seems to me a thing which the public has a right to expect, but that would be a long way from accomplishing what we need in this country, to bring about a revival and recovery of normal business conditions; is not that right?

Governor ECCLES. Yes; that is right.

The CHAIRMAN. It is a fact, is it not, that we did find the banks in a condition where their demand obligations were so great that they had no way on earth, with the limited amount of cash or currency available to them, to meet their demand obligations. Even though a bank might be solvent, the practical situation was that there was no way for the bank to get enough currency to meet its demand obligations. That was the situation that existed in many cases, was it not?

Governor ECCLES. That is right.

The CHAIRMAN. That is the situation that confronts us and for which we must find a remedy if we are going to make it possible to bring about business recovery and the normal use of banking credit to support business in the United States; is not that right?

Governor ECCLES. That is right.

The CHAIRMAN. And this is also true, is it not, that the emergency plans embodied in the emergency legislation which we passed in

1932 have certainly failed to accomplish those desirable results, have they not?

Governor ECCLES. I think that is the only conclusion one could reach, from the present evidence.

The CHAIRMAN. Those provisions are so hedged about, even though under the law, under the act of 1933, as it was finally written by an amendment that extended to nonmember banks the privilege of having their sound assets treated as eligible for advances by the Federal Reserve banks, and as a basis for the issuance of currency, the rules and regulations were so hedged about, the law being a temporary measure, and being tried out as an emergency measure, was not enough to reassure the banks that they were free to go ahead and use their credit facilities freely for the support of business and to promote recovery.

Governor ECCLES. An abundance of excess credit is available in the banking system. Excess reserves are sufficient at the present time for the banking system, as a whole, to extend credit to an amount in excess of 20 billion dollars, without the banking system as a whole having to use its rediscount facilities with the Reserve System. Interest rates are at possibly an all-time low level. The discount rates of the Reserve banks have been steadily reduced until at the present time none of the banks have a rate in excess of 2 or 2½ percent.

The amount of the excess reserves held by the banks, the low discount rate, and hence the low rates that are prevailing for commercial paper, for high-grade bonds, industrial and municipal, and for Government securities, are indicative of the excess supply of money and credit in relation to the demand for it, on a basis largely of short-term credit.

In order to expand the use of money which is necessary for recovery, either those holding deposits in banks must be willing to spend their funds, which would increase the velocity of the total existing deposits, or borrowers who can command bank credit must be willing to go to the banks and borrow funds which they will spend, or a combination of both is necessary.

If, in the first instance, owners of funds spend their funds, you would get an improvement in business through an increase in the velocity of the existing deposits. If new loans are made you would then get an increase in the volume of money as well as an increase in the velocity of money. In the absence of an increase in the velocity of the funds held by the banks, or an increase in the volume of private credit extended by the banks, the Government has been required to inject into our system through using its credit an increased flow of funds. Government spending has the same effect as private spending. It is somebody's income. Every one's spending is somebody else's income.

The CHAIRMAN. Let me ask you a question right there. Do you think Government spending has the same effect as private spending? Do you think you want to adhere to that statement upon reflection?

Governor ECCLES. From the purely monetary standpoint——

The CHAIRMAN. As far as the actual transaction is concerned; but as far as the psychological effect is concerned, and the effect upon a lot of men who want the money spread into their business, it would be a different matter would it not?

Governor ECCLES. It may be. It is, of course, desirable to have private spending instead of having Government deficits.

The CHAIRMAN. In that connection, let me ask you this question: In reference to the matter of farm-land values, we have put a certain amount of support under farm-land values by the assistance that has been extended by the Government. But the average citizen who might have some idle cash and might want to invest it for his children does not know how long that policy will continue, or when that support will be withdrawn, and in such an event, what effect it would have on bank values. But if this support was given in a normal way so a citizen would expect it to be maintained and to endure, he would have a different mental attitude toward the situation, it seems to me.

Mr. CROSS. The difference, as I see it, is that money put up by the Government in enterprises that would not come in conflict with the activities of private business would cause those who receive wages from that activity with the Government to spend money with the merchants and others, but it does not affect the feeling or help the condition. Everybody feels like the Government has to quit sometime somewhere, and therefore they remain nervous.

If private enterprise should take up this unemployment people will feel as if that is natural and normal. If you could get prices to where private enterprise could make a profit, I do not see how the credit you are talking about will be used, because neither the fellow will borrow, nor would the bank be foolish enough to loan; but you have to get prices to where a man can get a loan and can sell his products and make a profit and pay it back. Of course, that means the employment of labor, and that means spending power.

I know we are in a jam, and it is hard to get out. Of course, we can dig and dig, and get right back to where we find ourselves in the mud. But I do believe if we could get prices back we will be going ahead.

Governor ECCLES. The only way you could get prices back is through increasing the means of payment in the hands of the people who will spend faster than you increase production. To get them back any other way means to get them back through an artificial restriction of production or the fixation of prices, which are not desirable ways to get prices up. In other words, to raise prices and reduce production does not add anything to the national wealth.

Mr. CROSS. We are in this situation. You have a fixed indebtedness on the people. You say that Tom, Dick, and Harry own these buildings in this city. They do not. In the courthouse you will see a paper title in their names. But there is a mortgage against it, and under present prices, with the taxes they have to pay, they do not own anything. They are mere interest-paying tenants. That is all they are, struggling like the dickens to pay their rent to the fellow who owns the mortgage.

The dollar has so increased in its purchasing power that it takes twice as much for him to get the necessities and comforts that he has than he had to pay before, and with the taxes he has to pay now he is up against it. Unless we can get it to where he can pay back with the same kind of dollar that he borrowed, I do not see anything ahead but a general liquidation, and possibly a revolution.

Governor ECCLES. Of course, there are two ways out of depressions, it seems to me. One is through the process of liquidation and bankruptcy.

Mr. CROSS. Then there may be a revolution.

Governor ECCLES. The other is through an inflationary process. We went through a period of liquidation and bankruptcy as a result of allowing nature to take its course until we had extinguished a third of our deposit-money supply and until we had 15 or 16 million people out of employment, and until the quoted values of the resources of America were less than the debt. In other words, we liquidated down to a point where we had created a condition of general insolvency as measured by the ability of the people through the national income to support the debt structure.

The deflation was finally stopped because of the unrest and because of the suffering caused thereby and because it not only was affecting the debtor but the creditor was equally affected. The corner of completing the job of deflation was so hot that it could not be turned, and there was only one other course open. In order to save the system of capitalism and to maintain order, the Government was forced to step in, even under Mr. Hoover.

The first effort was made through the organization of the Reconstruction Finance Corporation, not for the purpose of directly relieving unemployment but for the purpose of using Government credit to support, through further debt, the railroad system, the banking system and the insurance structure, all of which was very necessary to support.

That action did not meet the problem of unemployment. It was an effort to support the private credit structure through the use of Government credit.

That action, plus similar actions by the Government through other credit agencies which have been set up and have not been inflationary—I mean the Home Owners' Loan Corporation, the Farm Credit organization, and the Reconstruction Finance Corporation—stopped deflation. The greatest portion of Government credit which has been used during the depression is not of an inflationary nature, because it is simply a question of transferring the debt from where it is to a Government agency.

The CHAIRMAN. And by that process it did stop deflation?

Governor ECCLES. Yes; that process stopped, or at least checked deflation. The condition of inflation has to come about through the increase in the volume and velocity of money either by Government spending or by private spending, or by a combination of both.

Mr. FORD. Would not "reflation" be a better term?

Governor ECCLES. Yes. The difficulty is that so many people, when you say "inflation", think it is something unsound; they think of worthless money. What I mean is that a rise in the general price level, in employment, and improvement in the business situation, from wherever it is, would be inflation, no matter how small the extent.

The CHAIRMAN. Let me suggest that you just use the word politely and call it "expansion."

Mr. CROSS. They deflated until they got into this condition. Now, if you go back to where we were, would we not simply be reflating, or expanding?

Governor ECCLES. "Expanding" or "reflating"—I do not care what the term is. I think it is a question of what is meant.

Mr. CROSS. It ought to be controlled?

Governor ECCLES. Absolutely; it is very important, of course, that it be controlled, and with the private banking system, with the excess reserves now available, if the credit expansion should commence and continue with the use of the present existing reserves, you could get a business activity and a price level substantially higher, I think, than we had in 1926, 1927, 1928 or 1929. You would have an increase in your total deposit money; or, in other words, your total deposit money would be increased beyond any amount that we ever had before.

Mr. CROSS. We know that, Governor; but do you not think that by these levers that have been put in this bill, as you have it, by your control over the reserves, the rediscount rate, and so forth, you could take the situation in hand any time so that you could control it?

Then, too, is it not much easier to control inflation, to stop things from going up, than to stop deflation after it has once started? As one of the Governors who testified here before told us, whenever you attempt to stop deflation, it is the hardest problem with which you have to deal.

Governor ECCLES. I think that the control of inflation is a far less difficult problem than the control of deflation. We have had a good deal of talk for a year or two about the fear of inflation. If there was any real fear of inflation, it would be evidenced by an increase in equities. Stocks would be going up instead of down, high-grade bonds would be going down instead of up, and the interest that would be paid on long-term municipal, Government, and other securities would be increasing rather than decreasing. Likewise, real-estate values would be rapidly increasing, and rents would be going up.

In other words, if there were a fear of inflation that we hear so much talk about, money would be shifting from deposits into things, and there would soon come a demand for increased credit, because it would be profitable, with things going up, to use credit to buy things.

Mr. CROSS. Every time a statement is given out, purporting to come from the White House, that there is or will be no inflation, down drops the stock market and everything else.

If you have any influence over there, I wish you would stop them from doing that. [Laughter.]

Mr. FORD. Is not the situation that you are describing there one of fear on the one hand and cupidity on the other? In a deflationary period, everybody is shivering; and in a boom period, everybody is overconfident and wants to get more. As I said, you have cupidity on the one side and fear on the other. You step from one stage to the other, do you not?

I am not criticizing that cupidity; that is human nature; but that is what it amounts to.

Governor ECCLES. You have, of course, a lack of confidence on the part of a good many people, and a timidity; but on the other hand, if they feel sure of inflation, that these things are going up, the natural result is that they would buy things in order to make a profit.

The CHAIRMAN. It is 12:30, and I think that this would be a good time to recess.

Governor ECCLES. I would be glad to have the Federal Reserve furnish to the members of the committee mimeographed copies of the first 3 days' hearings.

The CHAIRMAN. That will be very helpful. We will appreciate it.

Governor ECCLES. And also, when I have finished here, or the hearings have been finished, I will be glad to furnish the members of the committee with a complete brief, just as I have it here, of every phase of this legislation.

The CHAIRMAN. All right.

We will meet at 10:30 tomorrow morning.

(Thereupon, at 12:30 p. m., a recess was taken until Thursday morning, Mar. 14, 1935, at 10:30 a. m.)

BANKING ACT OF 1935

THURSDAY, MARCH 14, 1935

HOUSE OF REPRESENTATIVES,
COMMITTEE ON BANKING AND CURRENCY,
Washington, D. C.

The committee met at 10:30 a. m., Hon. Henry B. Steagall (chairman) presiding.

The CHAIRMAN. The committee will come to order. Mr. Eccles, you may continue your statement. Mr. Cavicchia desires to ask you some questions.

STATEMENT OF MARRINER S. ECCLES, GOVERNOR FEDERAL RESERVE BOARD—Continued

Mr. CAVICCHIA. Governor, I think the other day I asked you to tell me the amount of mortgages held by member banks. I understand that amount has already been inserted in the record, namely, $2,270,000,000.

Governor ECCLES. Yes; that is right.

Mr. CAVICCHIA. The bill before us, as I understand it, authorizes the national banks to lend on amortized mortgages up to 75 percent of the appraised value; am I correct?

Governor ECCLES. That is the limitation put in the bill; but I made the recommendation that the Federal Reserve Board be given the power to make rules and regulations governing mortgages to be taken by member banks, in lieu of the 75 percent and 60 percent limitations in the bill.

Mr. CAVICCHIA. What do you mean by 75 percent and 60 percent?

Governor ECCLES. Seventy-five percent of the appraised value of the property and 60 percent of the amount of the time deposits.

Mr. CAVICCHIA. One of the reasons given for the banks' inability to meet the demands of the depositors, Governor, in this crisis we have been going through in the last 5 or 6 years, was the fact that they had so much of frozen assets on hand. Do you not think that if you give authority to the banks to lend on mortgages on a higher percentage than they have been loaning on heretofore that you will make it still harder for them to meet the demands for payments in case we should have another crisis?

Governor ECCLES. I feel that the liberalization of the mortgage provision should be considered in connection with the modification of the eligibility changes in the legislation. It seems to me that unless the eligibility provision be liberalized, permitting the Federal Reserve banks to loan on sound assets in order to meet conditions of deflation, then the banks should be prohibited from loaning on

5-year 50-percent mortgages. They should be prohibited from loaning on or purchasing any bonds the maturity of which runs beyond 6 months or a year.

Mr. CAVICCHIA. You think that it is the short-term mortgages that add to a feeling of fear?

Governor ECCLES. No; what I think is this, that the banks, having only 12 percent of their loans and investments eligible in 1929, and those eligible assets not equally distributed throughout the banking system were not able to meet a substantial contraction of credit without many of them being forced to the wall and without forcing the payment of loans as they fell due.

There should be no more objection to the long-term amortized mortgage as proposed in the bill than to the 5-year straight 50-percent mortgage, which has been permitted for a period of 20 years, or to the investment in securities of all kinds without regard to maturity.

It is interesting to note as to the banks which closed throughout the country, and I understand that it has been shown by investigation, that the greater number of bank failures was in the area—and this is according to Federal Reserve districts—where the smallest amount of real-estate mortgages were held by the banks. The area where the larger percentage of real-estate mortgages was held by the banks was where the percentage of bank failures was the smallest.

It is found that the investment in securities—in bonds—has a very close relationship to bank failures.

Mr. CAVICCHIA. That leads me to ask you this question: I think you will agree with me that the decline in the value of real estate has amounted to perhaps 25 percent or more during this crisis as compared with what it was in 1923, 1924, and 1926. Do you agree with me on that?

Governor ECCLES. Yes; I think there is an average deflation of real estate of at least 25 percent.

Mr. CAVICCHIA. So that if a bank loans up to 75 percent of the appraised value on a mortgage, and then there should be a depression, that 25 percent equity would be wiped out overnight, would it not?

Governor ECCLES. It would be wiped out over the period that it took to bring about a deflation of that amount.

Mr. CAVACCHIA. It will not be as good a security as a mortgage based on 50 percent, because if there is that difference there will still be a leeway there.

Governor ECCLES. I think that is correct, with this exception: That in the case of the 50-percent straight mortgage, which is now permitted, the owner——

Mr. CAVICCHIA. What do you mean when you say "which is now permitted"?

Governor ECCLES. The law now permits a mortgage of 50 percent of the appraised value—up to 50 percent of the time funds.

Mr. CAVICCHIA. Is that in the law now?

Governor ECCLES. That is in the law now, and it has been there for 20 years.

Mr. CAVICCHIA. You say "time funds"?

Governor ECCLES. That is right.

Mr. GOLDSBOROUGH. I think you are mistaken about the 20 years. I know that Mr. Steagall and I fought the inclusion of a more liberal provision in the banking act for years and years, and I have only been on the Banking and Currency Committee for 15 years.

The CHAIRMAN. We liberalized the provision in the McFadden Act of 1927.

Governor ECCLES. You might have liberalized it, but they have been making real-estate mortgages for 20 years. I was incorrect in stating that the present provision has been there for 20 years.

Mr. GOLDSBOROUGH. They were not allowed to carry real-estate mortgages before 1926.

Governor ECCLES. There is a provision in the original Federal Reserve Act.

Here is the provision of the original Federal Reserve Act:

SEC. 24. Any national banking association not situated in a central reserve city may make loans secured by improved and unencumbered farm land, situated within its Federal Reserve district, but no such loan shall be made for a longer time than five years, nor for an amount exceeding fifty per centum of the actual value of the property offered as security. Any such bank may make such loans in an aggregate sum equal to twenty-five per centum of its capital and surplus or to one-third of its time deposits and such banks may continue hereafter as heretofore to receive time deposits and to pay interest on the same.

The Federal Reserve Board shall have power from time to time to add to the list of cities in which national banks shall not be permitted to make loans secured upon real estate in the manner described in this section.

Mr. CAVICCHIA. That was confined to farm lands, as you read it.

Governor ECCLES. Yes.

The CHAIRMAN. Just a moment. This seems to be chasing niceties rather than principles. Dr. Goldenweiser, can you give us off-hand the history of this legislation?

Dr. GOLDENWEISER. I think Mr. Wyatt can answer that question.

Mr. WYATT. I cannot give you the details off-hand, but that section has been amended a number of times and all the amendments were in the direction of greater liberality. The last extension of it was in the McFadden Act of February 25, 1927.

Mr. GOLDSBOROUGH. My memory is that Mr. Steagall and I fought that for years and years and years, and finally we were steamrollered in 1927. I also know that this Congress has spent a large part of its time in the last 2 years bailing out the banks that accumulated these real-estate mortgages over our protest.

Mr. WYATT. That section was amended twice: Once by the act of September 7, 1916, which was in the direction of greater liberality, and authorized loans on city real estate as well as farm land. It was amended again by the McFadden Act of February 25, 1927 which authorized loans on city real estate for 5 years, instead of 1 year, removed the prohibition against banks in certain reserve cities making any real-estate loans, and increased the aggregate amount of real-estate loans which might be made by any national bank from one-half of its time deposits to one-third of the savings deposits.

Mr. CAVICCHIA. When we talk of 1-year mortgages, it does not mean that they will be called in at the end of 1 year. If the people will pay their interest and the property is kept up, the mortgage is permitted to run along; am I correct or not?

Governor ECCLES. I think that is true.

Mr. CAVICCHIA. That is the general practice, is it not?

Governor ECCLES. That is the general practice, in connection with most loans, whether real estate or otherwise.

Mr. CAVICCHIA. I am only cognizant of what takes place in my own State. I know of savings institutions——

Governor ECCLES. The borrower usually pays a commission, however, each time the loan is renewed, and he is always in the position of never knowing——

Mr. CAVICCHIA. That is not true in New Jersey. The savings institutions make their mortgages for 1 year. They never pay a bonus for getting the money. The mortgage is never renewed. Under our law it may continue, even though it is for a 1-year period. You will find mortgages that have been on some pieces of property for 15, 20, or 25 years. As long as the people pay their interest, they run on. They do not have to be renewed.

It does not cost them a nickle, except in the case of some mortgage companies, where some 5 or 6 years ago they got into the habit of writing short-term mortgages for 3, 4, or 5 years. When those mortgages expired, they did have to be renewed, which caused extra cost to the borrower, and sometimes a great deal of trouble in having them refinanced.

Let me ask you one more question in connection with the mortgages.

I take it that the reason you are liberalizing the mortgage clause in this banking bill is that you are hoping to be able to provide mortgage money, which has been very scarce during the last 6 years. Am I correct about that?

Governor ECCLES. That is partly true. We had this in mind.

The commercial banking system has over 10 billion of time funds. Those time funds, or savings funds, in the commercial banking system are the equivalent, so far as the people are concerned, of funds held by the mutual savings banks in the New England and New York areas.

Either the banks are going to use those time funds in the long-term lending field, either long-term bonds of various kinds, or long-term mortgages, or long-term Government financing, or they are going to have to stop paying interest and give up those time funds.

If a bank is confined to its loans to eligible paper, in order to be liquid, then the only other avenue for investment of its funds would be Government bonds. That would mean at the present time that 8 percent of the total loans and investments of the banks would be commercial paper, and the 92 percent would be Government securities. This would mean that the Government, through its agencies, would be doing the lending business, furnishing long-term credit, which it is largely doing today, and the banks which hold the funds of the people would be furnishing the Government the funds by purchasing Government bonds or bonds guaranteed by the Government. That is the trend today.

As a matter of fact, 44 percent of the assets of the banks are now Government bonds, or bonds guaranteed by the Government, and I see no——

Mr. CROSS. Long-term deposits?

Governor ECCLES. Forty-four percent of the loans and discounts; that is, the investments of the banks represent Government bonds.

What I am trying to do is to put the banking sytem in a position where it can furnish long-term credit to the communities, just as the mutual savings banks and savings and loan associations do with the time-funds which they have.

If banks are not to be in a position to compete in that field for loans and investments of that sort, then it seems to me that they are put up against the problem of the use of these funds, which they hold and which are greatly needed to bring about an improvement in business conditions.

As I indicated yesterday, the income velocity of our existing funds was about two, whereas in 1926, 1927, 1928, and 1929 it was over three. Of if we had the same velocity of our deposit money that we had during that period, our national income would be at least from 20 to 25 billions more than it is.

But it is the stagnation of credit, the stagnation of funds, that continues, it seems to me, to retard business recovery. As to the extent to which an easing of credit by the use of long-term mortgages or on the amortized basis, and the liberalizing of eligibility requirements would bring about the use of that credit, nobody, I think, is in a position to say.

Mr. CAVICCHIA. I think you will agree with me when I say that whether they be national banks or State banks, or mutual savings banks, they have a lot of money on hand at the present time and are not loaning it; am I correct?

Governor ECCLES. That is right; they have excess reserves.

Mr. CAVICCHIA. The savings banks or the mutual banks which are now permitted under State laws to loan money on mortgages up to 50 percent of the appraised value are not loaning any, or very little, money at the present time.

Do you think, if this act were passed, that the national banks would do what the mutual banks are not doing now—lend money on mortgages?

Governor ECCLES. The mutual banks are lending money on mortgages in certain sections. The insurance companies are lending on mortgages, and one of the first things this act would do would be to enable the banks which now hold over 2 billion of mortgages, many of which are in excess of 50 percent of the appraised value——

Mr. CAVICCHIA. That is because of the drop in the market?

Governor ECCLES. That is right. Therefore, they are forced to collect on the mortgages, and Congress is appropriating money for the Home Owners' Loan Corporation, the Federal Farm Mortgage Corporation, and the R. F. C., to take up these mortgages.

The banks are not in a position to hold many of the mortgages that they may have for the reason that their mortgages are in excess of 50 percent, and they are due.

I would like to see the banks required to hold the mortgages they have and refund them on a long-term basis, requiring amortized payments with reduced interest. Instead of going through the process of changing the form of the obligations they hold, they have to substitute for their own loans obligations guaranteed by the Government.

Not only that, there are many State nonmember banks which, if they should come into the Federal Reserve System, would have more than 50 or 60 percent of their time funds in mortgages. In many sections the banks are permitted to loan in excess of 50 percent; and, if there is a liberalization of the mortgage feature, the bill will make it less difficult for the nonmember banks to come into the Reserve System.

If we are going to proceed on the assumption that we are going to have great cyclical booms and depressions, depressions that can extinguish 30 percent of our deposit currency and can reduce the national income by one-half, then I say that there is no way you can set up a banking system that will serve the money needs of the country and at the same time be prepared to meet that kind of a catastrophe. Liquidity in deflation can only be provided by the Federal Reserve System.

Mr. GOLDSBOROUGH. You mean as long as we are on this fractional reserve basis of 10 percent? Is that what you mean?

Governor ECCLES. Yes.

Mr. GOLDSBOROUGH. Of course, when you have an accordion and just blow the air in and out, you are right, but you do not have to have that system.

Governor ECCLES. Of course, it seems to me we do not have any alternative at this particular time without a very revolutionary change in the whole banking set-up. The 100-percent reserve idea would, of course, eliminate the 10 to 1 ratio. But that is another story.

Mr. CAVICCHIA. Governor, am I right in saying that one of the main reasons why this provision is in the law is to encourage the banks to hold onto the mortgages that they have now, because otherwise they would have to resort to foreclosure, because their mortgages are no longer on a 50-percent basis on account of the big drop in values?

Governor ECCLES. I would say that is true in some cases, and I would say that is one of the constructive effects. The other constructive effect would be that the banks are put in a position to do what the R. F. C. and other Government agencies are now doing.

There apparently is no demand for short-term commercial credit. The business of this country is largely done by concerns with an adequate working capital. But there does seem to be some demand for longer-term credit, and there is no prospect of getting any building activity without providing long-term credit at low interest.

The English have provided 30-year credit for home construction on 80 percent of the value of the property at 4½-percent interest, and that is done by the private savings institutions.

The most unsound type of mortgage credit is the straight loan that we have had in this country. It means that the borrower, the builder, will get a straight 50-percent loan from the banks and insurance companies, and then a second-mortgage loan will be financed elsewhere at ruinous rates, until the cost of the mortgage money, considering the first-mortgage cost and the second-mortgage cost, has made the financing cost of the property ruinous to the home builder and the home owner. The amortizing payments were to be made over a period of time on the second mortgage. The first mortgage became due and it was expected, of course, that the full amount would be renewed.

Mr. CAVICCHIA. Governor Eccles, I appreciate the fact that there are many definitions as to what constitutes centralized banking. One of the charges made about the bill that is before us now is that it tends to centralize banking.

Is this so, or is it merely regulatory in the sense that this bill tends to do away with the great disparity heretofore prevailing between the national and State banks?

Governor ECCLES. Which part of the bill are you referring to? Title II does not deal, it seems to me, with the problems of national and State banks, except by giving the Board the right to waive the present legal requirements for membership of nonmember State banks.

Mr. CAVICCHIA. I mean in the strict sense that centralized banking is used. This is not a bill aimed to centralize authority in the Federal Reserve Board, is it?

Governor ECCLES. It centralizes some authority in the Federal Reserve Board. The authority that is being centralized through this in the Federal Reserve Board is the authority over open-market operations.

The Board at the present time has authority over the discount rate, and subject to the approval of the President, under the emergency act, has the authority to change reserve requirements by declaring an emergency.

This bill is proposed to place in the Board, with the advice of the governors, the third function of monetary control, that of open-market operations, which, at the present time, is in the committee of governors, subject to the approval of the Board, and then subject, finally, to the decision of the twelve Federal Reserve banks as to whether or not they will participate in the program recommended by the governors and approved by the Board.

Mr. CAVICCHIA. Does that leave the different Federal Reserve banks in different districts to operate independently, if they wish?

Governor ECCLES. It leaves them to operate independently; and that is not changed. The question of extending credit to member banks is left with the credit division of each Federal Reserve bank.

It has been stated that the changing of eligibility requirements would cause the Federal Reserve banks to be loaded up with long-term mortgages. It seems to be assumed that the Reserve banks would discount these mortgages or any slow assets that they may choose to take, during the life of such assets.

In the first place, whether or not credit will be extended to a member bank, and upon what basis, will be determined by the regional Federal Reserve banks, which are responsible for the credits extended to member banks. The Board will only make the rules and regulations governing the basis upon which credit can be extended, and it is proposed here to give the Board power to liberalize the basis upon which the Reserve banks can extend credit to the member banks. The occasion for the extension of credit arises when the reserves of the banks get below the legal requirement, and they find it necessary to borrow to build up the reserves.

Mr. CAVICCHIA. The other day you showed the members of this committee a chart, showing the conditions in England. This chart seems to show that there is no relation between the price level and the increase or decrease in employment; am I correct about that?

Governor ECCLES. That is correct.

Mr. CAVICCHIA. Although we have been proceeding on the theory in this country that if the price level goes up wages will increase and unemployment will decrease; am I correct in that?

Governor ECCLES. You say we have been proceeding on that theory? I do not know what you mean by "we."

Mr. CAVICCHIA. There are certain economists; everything that this Administration has done in the past 2 years—and I am not criticizing the Administration; I do not intend to be partisan; but it has proceeded on the theory that if the price levels went up wages would go up and unemployment would decrease. But the chart showing conditions in England seems to negative that assumption.

Governor ECCLES. That is correct.

Mr. CAVICCHIA. Governor Eccles, the Canadian banks, I am told, are not permitted to make mortgage loans, and in depression times they are not met with the problem of frozen assets. Is this one of the reasons why they have had no bank failures in Canada during this depression?

Governor ECCLES. I do not accept the assumption that a mortgage is any more of a frozen asset during deflation than nearly any other asset of the bank. The assets become frozen when every banking institution wants to dispose of its assets to meet the demands of its customers for money. The only liquidity that can be provided for a banking system is through the central bank.

The Canadian banking system is a very different structure than the American banking system. In the first place, they have very few very large banks, and the creditor area—the eastern section of Canada supplies the credit to the debtors of the interior provinces of Canada. I have been told that the interior sections of Canada, had they not been tied into the creditor or eastern section of Canada, would have had the same kind of bank trouble that we have had in this country; that it was the eastern section which was really furnishing the funds to develop the interior areas that enabled the system to carry through.

The Canadian system had only a fraction of the credit contraction that we had in this country. Had our credit contraction been 13 percent, as it was in Canada, we would not have had the banking collapse that we had.

The credit contraction in the British banks during the depression was practically negligible. The total amount of deposit money and currency outstanding all during the period of the depression in Great Britain remained almost uniform. Things might have been different here also, had our Federal Reserve System been in a position to loan against sound assets. The demand for money would have ceased—that is, the demand for currency—because we know that when people were able to get their currency after the bank holiday they did not want it, and currency came back into the banks instead of continuing to go out of the banks.

Mr. HOLLISTER. You said Canada had very, very few very large banks. You mean she only has a few very large ones.

Governor ECCLES. That is right.

Mr. HOLLISTER. It sounded as if you meant there were a lot of little ones.

Governor ECCLES. I mean that they have few very large banks, but they have a large number of branch banks.

Mr. HOLLISTER. I thought you might want to clear that up.

Governor ECCLES. Yes; I thank you.

Mr. Cross. You say that in England they did not have trouble with currency to take care of their deposits. Are the assets upon which those banks loaned money broader than ours? Can they loan upon any sound paper, where we are limited in that respect?

Governor Eccles. Are you referring to central banks—that is, the new Canadian Bank and the Bank of England—or are you referring to the commercial banks?

Mr. Cross. I am just referring to your statement that they could loan on sound security, and that if we had been in their position we would not have had the crash that we had. The question I am trying to get at is, Could they loan upon different assets than we loaned upon, because it is sound paper and ours is sound, but we are not under our law permitted to loan on that paper or discount that paper?

Governor Eccles. In the first place, the Canadian banks, as I understand it—and I am not an authority by any means on that subject; it is just what I have been told and hear—that the Canadian banks and the British banks do not loan on real estate. The banking structure, as I said, is entirely different; it is differently constituted.

The savings funds in Britain are largely built up, as I understand it, in the savings and loan associations, the mutual savings and loan associations, which carry the real-estate credit.

If our banking system was a large branch banking system such as the Canadian system or the British system, it would be a much easier problem to segregate investments or savings funds from the commercial banking system. But so long as we have unit banks operated under the laws of 48 different States and the National Bank Act, these unit banks have two functions: The function of providing the check money through their deposits, and the function of investing the community's savings or investment funds.

Demand deposits representing our deposit currency should be invested in short-term paper, so far as possible, and in Government securities. But when it comes to investment funds, interest-bearing funds, it seems to me that we have another problem, and it is entirely different from the problem in Canada or the problem in Britain, or in any other country.

If we are going to avoid a banking collapse and the extinguishing of a large part of our money supply in the future, it is going to be necessary to make it possible, when contraction starts, for our Federal Reserve System, which is our central bank and bears the same relation to our banking structure as the Bank of England does to the English banks, to loan on sound assets to prevent a continuation of credit contraction and bank failures.

Mr. Cavicchia. You need not answer this next question if you feel that you ought not to, Governor. This is the question: In your opinion, should we have a metallic base for our money, such as gold, or is that an exploded theory?

Governor Eccles. A "yes-or-no" answer could be misunderstood. That is a question which, in order to answer it, would need considerable explaining.

Mr. Cavicchia. The reason I asked it is this: Some people still hold to the theory that we should have a metallic base, and that that should be gold. Others say it has been tried and it as failed. That is why I asked the question.

It is a problem upon which many opinions are expressed; but I do not think it has been answered. The fact that the important countries of the world have been wedded to gold by experience and habit for so long a time makes it a very difficult matter to divorce money from gold.

Mr. CAVICCHIA. Governor, it is a moot question whether or not the United States is still on a gold basis just now. What do you say about this?

Governor ECCLES. Our currency and our deposits in the Federal Reserve still require the same gold reserve that they always have, of 40 and 35 percent. To the extent that gold is not being paid out, we might say that we are not on gold. To the extent that we are requiring the same gold reserves, we can say we are on gold. We permit the export of gold under license, so that internationally we are on gold.

Mr. CAVICCHIA. So far as our imports are concerned, we are on gold, are we not?

Governor ECCLES. The dollar has been fixed at a certain price at the present time in relation to gold.

Mr. HANCOCK. It has been stated that we are today on a discretionary international limping gold-reserve standard. What do you think about that?

Governor ECCLES. I would prefer not to discuss that question. I do not believe that has very much relation to title II of the banking bill.

Mr. HANCOCK. Well, it is not irrelevant.

Mr. CAVICCHIA. Under our present system, fear and confidence have a lot to do with the banking question, have they not; and is that not also true in relation to business in general?

Governor ECCLES. Not as much as I think is sometimes claimed. What is confidence with one group would be lack of confidence with another.

An effort to balance the Budget would give confidence to a group of people who feel that, if it is not balanced, their taxes are going to be higher; but it would put fear and consternation in the minds of the group of people who are dependent upon what the Government appropriates for relief.

Therefore, when we speak of confidence, it does not have an equal application to all our citizens.

Mr. GIFFORD. Governor, I question the necessity of title II. Mr. Hancock questioned you and you answered that that is really the primary feature of the bill, while the secondary feature is in reference to the reserve of banks. I want to ask you a few questions leading up to the necessity of it.

What is the total debt of the Nation, having in mind the present expenditures and authorized expenditures? In the President's message, was it 31 billion of authorized expenditure that faced us up to that moment?

Governor ECCLES. I would not be certain. As I recall, I know it is over 30 billion, but I do not remember the exact figures.

Mr. GIFFORD. It is 31 billion and some fraction, I think.

Governor ECCLES. I think that is approximately correct.

Mr. GIFFORD. Having in mind what has been done, we passed the H. O. L. C. bill, carrying one and seven-tenths billion?

Governor ECCLES. That is right.

Mr. GIFFORD. And if we pass the bonus bill that will be two and three-tenths billions additional, will it not?

Governor ECCLES. It depends on which bill passes.

Mr. GIFFORD. It is two billion three hundred million, is it not?

Governor ECCLES. It will depend on which bill passes.

Mr. GIFFORD. You are following these probable expenditures with the idea in mind of the necessity for this law?

Governor ECCLES. No; that is not correct. This law has no relationship to that. If the Government were to balance its Budget, we would propose the same law.

Mr. GIFFORD. I think my vote, so far as the necessity of this is concerned, would be guided by the actual necessity presented.

Governor ECCLES. I think there has been——

Mr. GIFFORD. If the Public Works bill now pending in the Senate, carrying $4,800,000,000 passes, and we provide for 1 billion to take care of social problems, as suggested, and if another billion should be required for farm-credit loans, we would get into the realm of a national indebtedness of 42 billion dollars, should these things transpire. You may subtract from your total, 3 billion, if you want to, and take into consideration the $1,800,000,000 profit from gold, but you would still have a debt of some 36 billion dollars. How much did you say there were in deposits in the banks?

Governor ECCLES. About 25 billion, eliminating interbank deposits. That represents the demand deposits.

Mr. GIFFORD. There are 38 billion in currency and deposits in the banks of the country. Do you recall the President's warning about the danger of the banks having to absorb the deficiencies in 1932, causing a very dangerous situation—that is, the deficiency caused by the operations of the R. F. C.?

Governor ECCLES. I do not recall that statement, but, of course, I would not feel there was any danger in that.

Mr. GIFFORD. The President spoke very strongly, and I wish you would read what he said, of the great danger of the banks having to absorb that deficiency caused before March 4, 1933, and since then we have added this large amount.

The purpose of this legislation is to control the privately owned banks, which would still be privately owned, by a Government board in Washington, so far as open-market operations are concerned?

Governor ECCLES. You mean control the investments that are made by the Reserve banks?

Mr. GIFFORD. To control open-market operations.

Governor ECCLES. Yes; to control open-market operations by the Reserve Board in Washington rather than by the banks themselves.

Mr. GIFFORD. They will still be privately owned, but they will be Government controlled.

Governor ECCLES. That is right.

Mr. GIFFORD. You mean the Government as constituted at the moment.

Governor ECCLES. I would say they are publicly controlled, rather than governmentally controlled. The control of open-market operations is proposed to be placed in the Federal Reserve Board.

Mr. GIFFORD. Exactly; and that policy will be dictated by this new board.

Governor ECCLES. It will be carried out by the Federal Reserve Board.

Mr. GIFFORD. So far as the Government as at present constituted is concerned, that means just that, does it not, inasmuch as a provision for refusal to reappoint was included in your bill?

Governor ECCLES. I do not think that has anything to do with the political relationship.

Mr. GIFFORD. Oh, no; there is nothing political in this bill.

Governor ECCLES. The fact is that the Governor has always been appointed by the President, at his pleasure.

Mr. GIFFORD. This bill specifically indicates the method by which the Governor might not be reappointed.

Governor ECCLES. That is entirely incorrect. The bill provides that the Governor shall be—that his term as a member shall expire when he no longer——

Mr. GIFFORD. I am talking about the members of this new Board.

Governor ECCLES. It is not a new Board; there is no difference——

Mr. GIFFORD. The present Federal Reserve Board——

Governor ECCLES. There is no change whatever proposed in that Board.

Mr. GIFFORD. But they retire at 70, under a pension, after a term of years, and there are many changes.

Governor ECCLES. Rertirement at 70 will be compulsory only for future appointive members.

Mr. GIFFORD. My point is, should another government come in, otherwise constituted, could they get control of this Board?

Governor ECCLES. In what way could they get control?

Mr. GIFFORD. I am asking you.

Governor ECCLES. No; they cannot, not unless their terms expire, and the President chooses to appoint some one other than a member whose term expires.

Mr. GIFFORD. By that method could not the new President get control?

Governor ECCLES. By what method?

Mr. GIFFORD. By the refusal to reappoint.

Governor ECCLES. He could, if the terms expired. But a member is appointed for a 12-year term.

Mr. GIFFORD. There is no way of getting rid of them?

Governor ECCLES. There is no way of getting rid of them except for cause. That has always been in the bill. There is no proposal to put in the bill any change in the method of appointing members of the Board, or as to their terms.

Mr. GIFFORD. That reminds me of the lady who insured her home. There was a fire, and when the agent came to the house he said he would look into the cause of the fire. Then she said, "I thought there would be a catch in it."

Governor ECCLES. That has always been in the law; we are not presenting any change.

Mr. GIFFORD. Then the banker who wrote this letter to me was misinformed when he said that nothing short of a revolution could ever change the condition that will be brought about by the enactment of this bill; is that correct?

Governor ECCLES. When the Federal Reserve Act was passed in the beginning, what did the bankers say?

Mr. GIFFORD. Getting back to the necessity of it, it is not quite as tight as the United States Supreme Court, is it? It is not quite as tight, is it, so far as the appointments are concerned? Would you be willing to provide for the appointments in that way, to have these men appointed in the same way that members of the Supreme Court are appointed?

Governor ECCLES. They are appointed in the same way, by the President of the United States, with the advice and consent of the Senate.

Mr. GIFFORD. I think that has been challenged. But you claim it is exactly the same?

Governor ECCLES. It is the same, so far as the appointment and confirmation is concerned. The term of the members is 12 years, in the case of the Federal Reserve Board, whereas the term of a Justice of the Supreme Court is for life. I believe he may be removed for cause.

Mr. GIFFORD. For what cause may a Justice be removed? What would be the cause in this case?

Governor ECCLES. I suppose for dishonesty or improper conduct.

Mr. GIFFORD. Or unwillingness to cooperate with the Government; would that be a cause?

Governor ECCLES. I am not in a position to say what the cause would be. All I know is that during the life of the Federal Reserve Board of over 20 years no member of the Board has ever been removed for cause. Their terms have expired or they have resigned voluntarily.

Mr. GIFFORD. I think if they made it hot enough for them they would get out, if they did not cooperate.

Now, coming back to the necessity for this bill: Faced with a debt of 38 billion or 42 billion, do you want to make the assets of the member banks sound assets, available for the issuing of currency; is that it?

Governor ECCLES. No; that is not the purpose of it. The law is not being drawn with that idea, of assisting in the financing of the Government.

The Government is having no difficulty with its financing. Its interest rate has been going down steadily. The desire of the banks to purchase Government bonds is so great that whereas at the end of Mr. Hoover's term the interest rate was nearly 4 percent, it is now less than 2¾ percent.

Mr. GIFFORD. Of the present indebtedness of the Nation, how much of it is in short-term loans?

Governor ECCLES. Do you remember, Dr. Goldenwesier, what the exact amount is?

Dr. GOLDENWESIER. I can look that up and let you know presently.

Mr. GIFFORD. You have not been offering many loans to the public on long-time paper, have you?

Governor ECCLES. They have been doing a good deal of refunding. They have just called one billion eight hundred million of the fourth 4½-percent Liberty loan, and they offered in exchange a 25-year bond at 2¾ percent.

Mr. GIFFORD. They did that in other countries, based partly on the ground of patriotism.

Governor ECCLES. As a matter of fact, the bonds held by the banks of this country are less in proportion than the Government bonds held by the English banks. Thirty-nine percent of the assets of the member banks are invested in Government obligations, whereas 41 percent of the assets of English banks are so held.

Mr. GIFFORD. You said this morning it was 44 percent.

Governor ECCLES. Forty-four percent of the total outstanding bonds; 44 percent of the amount of Government bonds outstanding are in the member and Reserve banks and 39 percent of the assets of the member banks are invested in Government bonds; whereas 15 percent of the total bonds outstanding in Britain are held by the London clearing banks and the Bank of England, but that represents 41 percent of the resources of the British commercial banks.

It takes 5½ percent of the national income of Great Britain to pay the interest on the British national debt.

Mr. GIFFORD. Suppose we had to have an indebtedness of $40,000,000,000, and $9,000,000,000 was to be absorbed in the next year and a half, what proportion would the banks probably hold?

Governor ECCLES. What proportion of their resources in bonds?

Mr. GIFFORD. Yes.

Governor ECCLES. Of course, if the banks took 9 billion of bonds, the banks would increase their deposits by 9 billion.

Mr. GIFFORD. The term " deposits " is a rather tricky term. I suppose if I owed you $100,000, and you should be able to discount that, you would get some more currency and loan me another $100,000, and then take my second note and discount that, and still loan me still another 100 thousand, and that process could go on indefinitely, could it not?

Governor ECCLES. As a matter of fact, the banks could extend $20,000,000,000 of credit without rediscounting anything. The trouble today is not the need of the banks to rediscount; the trouble is the banks are unable to loan the funds that they now hold.

Mr. GIFFORD. We know that is a temporary situation. Idle money is glad to get something to invest in. There have not been many long-term offerings made in these times. They are all anxious to get something. You do not consider that that condition will be regular, do you?

Governor ECCLES. I think—and this, of course, is my opinion only—that for a long time to come there are not going to be in this country short-term loans of sufficient quantity to create the money that is required to carry our business structure.

Mr. GIFFORD. Why has not the Government—knowing that this indebtedness cannot be paid off for many years—why has not the Treasury offered long-term paper or bonds?

Governor ECCLES. Why have they not?

Mr. GIFFORD. Yes.

Governor ECCLES. That is a question I would prefer you ask the Treasury. I would not want to answer that question for them.

Mr. GIFFORD. You have said money was plentiful.

Governor ECCLES. Money is extremely plentiful. But if the Treasury had offered long-term bonds a year ago or 2 years ago, they would have paid a rate of maybe a half or three-quarters of a percent more than they are paying now. So long as the Treasury can borrow at a fraction of 1 percent, and the interest rate on long-term financing is going down, would it not appear advisable to finance on the cheapest basis of short-term credit, so long as the long-term market is going down? It has been profitable up to date to defer long-term financing.

Mr. GIFFORD. If they could sell these long-term securities at 2¾ percent they would sell them, would they not?

Governor ECCLES. If they could, you say?

Mr. GIFFORD. Yes; they would offer them if they could be sold, would they not?

Governor ECCLES. I do not know whether they would or not. Personally, I think you will see less than a 2¾ percent rate on long-term financing.

Mr. GIFFORD. Then you think there will continue to be plenty of idle money and that business will not get busy and need this money?

Governor ECCLES. I cannot conceive of business using 20 billion dollars of commercial credit, when in 1929 they only used 4 billion.

Mr. GIFFORD. You do not care to answer as to why the Treasury does not now, when money is plentiful and rates are low, offer long-term paper, that must, necessarily, be refinanced, a lot of it, with short-term paper?

Governor ECCLES. If they can borrow later at 2 or 2½ percent, would it seem advisable now to borrow at 2¾ percent?

Mr. GIFFORD. Let us put it the other way. If business recovers and needs money, and money is at a higher rate, has not that been the fear, that when these short-term securities are forced to be refinanced by long-term securities that the rate will be very high?

Governor ECCLES. That has been the fear, but it has been unjustifiable, and the reverse has been true.

Mr. GIFFORD. I hope you will prove to be a prophet, and a correct prophet, so far as the next 5 years are concerned.

You have no fear, so far as the Government using the method of issuing currency to banks with sound assets is concerned, that they will not always have plenty of money to buy the issues put out by the Government, and that this Government, under this plan of banking, could go into that practically to any amount?

Governor ECCLES. The amount of the Government debt that can be supported depends upon the national income, and a 40-billion-dollar debt here with an 80-billion income, is 6 months of the national income.

Mr. GIFFORD. We had a 90-billion-dollar income once, but what is it now?

Governor ECCLES. I think when Mr. Roosevelt came into office it was around about 38 or 40 billion. It is now some 50 billion.

Mr. GIFFORD. Our capital structure was 38 billion, that being the amount on deposit, available money and credits in the banks?

Governor ECCLES. No; it was 26 billion 400 million in 1929. That was the amount of demand deposits plus currency.

Mr. GIFFORD. There are two other questions I want to ask you, which you may be willing to answer.

You have no particular fear of a 40-billion-dollar national debt in this country?

Governor ECCLES. I have no fear of a 40-billion-dollar national debt.

Mr. GIFFORD. Your answer staggers me. I have.

Governor ECCLES. I can give you my reasons for not having it.

Mr. GIFFORD. Personally, I wish you would. With the present national income you have no dread or fear of the consequences of a 40-billion-dollar debt?

Governor ECCLES. I am concerned about the present national income, but you do not increase the present national income by diminishing Government expenditures. It is the total expenditures of the Nation that create the national income, and when the community, as individuals and corporations, do not spend, then the Government must.

Mr. GIFFORD. I am looking at it from the standpoint of my corporate interest. If I owed a hundred thousand dollars to you and you discounted my note and loaned me another hundred thousand, you could then go to the bank and discount my second note and loan me still another hundred thousand, and keep that up indefinitely. But then what happens to me, finally? How long do you think that a person, an individual, or corporation, can keep that up, and how long can the Government keep that kind of thing up? The application is the same.

Governor ECCLES. That is just where the mistake is usually made. Government credit is considered in the same way as we consider individual or corporate credit, whereas when the Nation borrows it is a question of the Nation borrowing from itself, so long as it is a creditor Nation. Therefore, when it borrows from itself, that is the——

Mr. GIFFORD. If the citizen owed enough taxes, that is sound. But the whole revenue is based on taxation, is it not?

Governor ECCLES. Taxes are the basis of the Government's income. If by Government spending you increase the national income, you increase the ability to pay taxes.

Mr. GIFFORD. Exactly. Then you have answered the question, that a 40-billion-dollar debt can only be paid by taxes.

Governor ECCLES. But the taxes will not be paid out of the present national income. I believe in the Government spending to a point that could prime the pump. If you increase that spending, in that way you increase the demands for goods.

Mr. GIFFORD. Did you ever try to prime a pump and you did not get quite enough water?

Governor ECCLES. That has just been the case.

Mr. GIFFORD. That being the case——

Governor ECCLES. It is the case today.

Mr. GIFFORD. Does anybody know the exact measure of water to be poured in before you catch?

Governor ECCLES. The measure would be when you get your unemployment problem rapidly diminishing and with private business being required to employ those who are unemployed to meet the demand for goods, by reason of increasing purchasing power and spending.

Mr. GIFFORD. Your statement about the 40-billion-dollar debt will probably be of great comfort to those who vote for the soldiers' bonus; it will probably be of great comfort to those who want social legislation, that is, your statement that you have no fear of a 40-billion-dollar debt. Do you realize the importance of that statement?

Governor ECCLES. Forty billion dollars in relation to the debt of Australia and in relation to the debt of Great Britain and other countries that we look upon as having met all the problems of the depression possibly as successfully as anybody else——

Mr. GIFFORD. So far as a comparison of our banking system is concerned it is no comparison to compare that with the system of other countries, if you can prove that our indebtedness is nothing to be worried about, in comparison with other countries.

Governor ECCLES. When we speak of a future debt of 40 billion. it seems to me it is only fair to deduct from the 40 billion the assets which the Government has taken in lieu of the debt. We cannot say that the loans which the R. F. C. has made are entirely uncollectible, and we should also take into account the balance in the Treasury in considering the net debt.

Mr. GIFFORD. And the gold profit?

Governor ECCLES. I think any other country would take the gold profit into account. It is there.

So that the debt is less than 23 billion today when you consider the Treasury balance, and without considering the gold profit, but when you consider the assets that you can use to offset the debt. That is less than 4 months of the normal national income of this country.

The indebtedness of Great Britain is 35 billion, and it takes 5½ percent of the national income to support the British debt. That is, what is considered the present national income, which is between 19 and 20 billion.

Mr. GIFFORD. You do not want us to fall into their company, do you?

Governor ECCLES. Our situation would require less than 1 percent of the normal national income to support the Federal debt.

Mr. CAVICCHIA. What percent?

Governor ECCLES. Less than 1 percent of the normal national income to support the present Federal debt.

Mr. GIFFORD. The national income?

Governor ECCLES. I said the normal national income.

Mr. GIFFORD. What is that?

Governor ECCLES. Eighty-two billion was the national income in 1929.

I am as anxious as anyone to see the Budget balanced. The Budget can only be balanced, however, out of the national income. The national income can only be increased by employment.

Mr. GIFFORD. May I say, before I go any further, Governor Eccles, I may appear to be almost brutally frank in my questions, but that is my mannerism. I am the most harmless man on the committee.

I have letters from 25 commercial bankers in my district, all fine bankers and upright men, who are opposed to this legislation, and I want to find out about their opposition.

Governor ECCLES. I appreciate the opportunity for giving my answers. I have met with the bankers, with the representatives of the American Bankers' Association, and with many other bankers, and I find that their opposition to the bill has been largely the result of a misunderstanding. They do not understand what is in the present law, and the opposition they raise to this bill is the same opposition which might be raised to the present law, in a great many instances.

Mr. GIFFORD. I am a new member of the committee, and know little about the problems.

Governor ECCLES. I have now the figures of the Government debt as of January 31, 1935, the total interest-bearing debt being $27,952,000,000; due within a year, $5,606,000,000; from 1 to 5 years, $8,792,000,000; and over 5 years, $13,554,000,000.

The CHAIRMAN. Let me suggest that in your statement you incorporate the figures showing the holdings of the Government against those obligations, in order to make the story complete.

Governor ECCLES. Yes; I will do that.

Mr. HANCOCK. You mean the credit balances in the general fund of the Treasury?

Governor ECCLES. The general fund balance is somewhere between a billion and a half and two billion. We will have to insert in the record the exact figures.

The CHAIRMAN. That is what I said, that you should do that to complete the statement, showing the holdings in the R. F. C. and other organizations inuring to the benefit of the Government.

Public debt and net assets of the United States, Jan. 31, 1935

[In millions of dollars]

Gross public debt	28,476
Net balance in general fund (excluding balance of increment resulting from reduction in weight of the gold dollar)	1,519
Net debt	26,955
Proprietary interest of the United States in governmental corporations and credit agencies:	
I. Financed wholly from Government funds:	
Reconstruction Finance Corporation	2,321
Commercial Credit Corporation	41
Export-Import Bank	14
Public Works Administration	269
Regional Agricultural Credit Corporation	90
Products-Credit Corporation	113
All other	506
Total	3,354
II. Financed partly from Government funds	1,120
Total	4,474
Increment from reduction in weight of the gold dollar	2,812

Mr. GIFFORD. We have your Treasury statement every day on our desks. I am speaking this morning of the probable billions to be added. We have that fact staring us in the face every day.

I want to bring out the fact that with this continual financing by the Government of Federal indebtedness we need this sort of protection.

Governor ECCLES. The budget of any government must be balanced over a period of time; there is not any question about that.

Mr. GIFFORD. Would you suggest a time—possibly 5 years?

Governor ECCLES. I would say it might be desirable over a 5-year period, but I do not think it necessarily need be fatal if it is only balanced over a 10-year period. A war condition could create an unbalanced budget for a considerable period of time, if sufficient taxes were not imposed to pay as it was carried on.

Mr. GIFFORD. Would you advise my creditors to carry me along for 5 years? If so, I wish you would send me a letter.

Governor ECCLES. It has been my philosophy that the amount and the rapidity with which the Government spends will reduce—that is, if the amount and the rapidity are sufficiently great—they will reduce the total amount that the Government may be required to spend. To do that we have had a 40-billion-dollar deficiency in national income and a 3-billion priming process last year; that is about what it was.

I do not consider the transfer of the existing debt from where it is to the Government as a priming process. It stops deflation, but the actual amount of the budgetary deficit as a result of the Government spending and the Government lending for new structures that increases the buying power of our people has not been sufficient to stop the process of deflation and to give the momentum necessary when you consider the size of the pump.

By that I mean that with 10 or 12 million unemployed the buying power cannot be sufficiently increased by a 3-billion-dollar spending to utilize our existing productive capacity.

Mr. GIFFORD. That is a fine statement you are making, but I am sure that the priming process must reach down far enough to give constructive money that not only feeds and clothes people, but begins to construct something out of which people can get an income.

If the Government had spent this money and it was being used by people who were constructing something which was employing labor, that would be different than simply feeding and clothing people and building beautiful roads or race tracks, and ornamental things in the country which, in the end, does not keep very many people at work bringing in an income. That does not keep many people at work for any length of time bringing in an income, does it?

Governor ECCLES. I think so. I think to spend money, or increase productive capacity when you already have an excess of productive capacity, is just the place where you do not want to spend it.

Mr. GIFFORD. In my section, they want to spend money on public works, or on race tracks and beautiful roads through the woods, and after they spend that money how much of an income will that produce?

Governor ECCLES. After all, income has to come from spending.

Mr. GIFFORD. But if that spending is simply for feeding and clothing people and putting up ornamental unnecessary things, that will not help them any in the future, so far as any income in the future is concerned.

Governor ECCLES. Of course, I do not believe that Government spending should be in a field of competition with private enterprise, where Government spending will be expected to return an income.

Mr. GIFFORD. You do not believe in the Government loaning to help private business, do you?

Governor ECCLES. I would prefer that the lending should be done by the private-credit system, but when you reach an emergency such as we had in 1932, and set up the R. F. C., it became necessary to save the credit structure and lend money.

Mr. GIFFORD. Would you prefer that the $4,800,000,000 in the bill pending in the Senate be loaned to private industry, the whole of it, rather than have it expended in the method suggested?

Governor ECCLES. I would prefer that no part of it be loaned; that every part of it be used as a grant, as leverage, so as to induce private borrowing and spending.

Mr. GIFFORD. Would it be possible to make such a grant to private industry by any such process without favoritism?

Governor ECCLES. It is possible to make grants to cities, counties, and States for noncompetitive public works, and induce leverage through that process.

It is possible, through a subsidy to home owners, to induce the construction of new homes, and the subsidy will be the difference between the cost and rents.

Mr. GIFFORD. Do you prefer non-Federal projects?

Governor ECCLES. When it is a pure Federal project there is no multiplying. If the funds are used as a leverage, as a subsidy, we will say, to cities, counties, and States, you get an increased spending or a leverage added to the spending by the home owner. We have a differential between costs and rents today which is retarding private construction.

Mr. GIFFORD. You mean, do you not, if you grant 30 percent to municipalities and the municipalities are putting up 70 percent, therefore you get three times as much work done?

Governor ECCLES. Yes.

Mr. GIFFORD. Exactly.

Governor ECCLES. But instead of the Government loaning 70 percent, let the municipalities arrange their own credit. I think 30 is possibly not sufficient.

Mr. HANCOCK. I am very much interested in the statement you made with respect to subsidizing the private home owner to induce him to build a new home. If such a program as that were carried out by the Federal Government, would it not have a tendency to stagnate every private lending institution in this country?

Governor ECCLES. It would stimulate them greatly if the subsidy represented the difference between costs and rents.

Mr. HANCOCK. Are you explaining the proposal that the newspapers carried not long ago, to the effect that you advocated or suggested a plan whereby the Government would make a grant or a gift to a prospective home owner up to, say, 20 percent of the cost of construction?

Governor ECCLES. I am not sponsoring any plan. The question was with reference to the spending of the $4,800,000,000, whether I would prefer that to be spent by the Government or used as a loan.

In answer to that I am simply making some observations here, or some suggestions as to what would be my own personal view, in order to get the most out of the proposed appropriation.

Mr. GIFFORD. I think you have answered my question sufficiently.

Mr. CROSS. It seems to me we are going far afield from this bill, and that we have taken in all of the theories of loaning, most of which have nothing whatever to do with this bill, and if we continue along that line we will never get through with this hearing.

Mr. GIFFORD. Mr. Cross went very far afield.

Mr. HANCOCK. I think the gentleman's questions have been interesting and pertinent.

Mr. GIFFORD. I will be through in 2 minutes, if you will give me 2 minutes longer. I want to make two remarks.

I believe thoroughly in non-Federal grants, where the Government itself pays only 30 percent and the municipality puts up 70.

I want to say simply in connection with this matter of priming the pump, the answer seems to be suggested to me that we have poured in the water, but the well is frozen. Lack of confidence has frozen the well, and it does not amount to very much.

(Thereupon, the committee took a recess until 3 p. m. this day.)

AFTERNOON SESSION

The CHAIRMAN. All right, gentlemen. I believe we finished with Mr. Cavicchia. Now, does anybody on this side want to interrogate Governor Eccles?

Mr. SPENCE. I want to ask him some questions.

Mr. DIRKSEN. I would like to ask some questions.

The CHAIRMAN. All right, proceed. Let us get along.

Mr. DIRKSEN. Governor, I shall try to be brief. Perhaps I ought to restate the question Mr. Gifford had in mind this morning, I think, namely, that the President has authority to designate one man to the Board as Governor of the Federal Reserve Board; is that a Presidential designation?

Governor ECCLES. That is right.

Mr. DIRKSEN. And when a man ceases to be designated by the President, he is no longer a member of the Board?

Governor ECCLES. No; he is no longer Governor, but he is a member of the Board.

Mr. DIRKSEN. He remains a member of the Board?

Governor ECCLES. Yes; unless he resigns, which is usually the case if he is no longer designated as Governor.

Mr. DIRKSEN. I got the impression from reading your observations on the bill that, when the President ceased to designate him as Governor, he automatically divorces his membership as a member of the Federal Reserve Board.

Governor ECCLES. The present Federal Reserve Act requires that the President designate a member of the Board to serve as Governor at his pleasure.

Mr. DIRKSEN. I think I see, and it will not take very long to state the question. Now, with respect to the government of the Federal Reserve bank, I think the residence requirement has been taken out of the old act, has it not? In the new provision there is a statement to the effect that the Governor no longer has to be a resident of the Federal Reserve district or Board on which he should serve.

Governor ECCLES. That is right.

Mr. DIRKSEN. I am wondering whether it would be possible, under this provision, to take a man from New York, for instance, and by virtue of the fact that the power of approval is vested in the Federal Reserve Board, insofar as the class C directors are concerned—if it would be possible to transplant such a man to the seventh Federal Reserve in Chicago, and by either the giving or withholding of the power of approval, you could make him a member of the Board? Do you think that is possible, if not probable?

Governor ECCLES. Yes; it is possible to transfer a man from any other reserve districts, and the proposal simply applies the same and class C director. At present the Governor may be chosen from other reserve districts, and the proposal simply applies the same principle to the chairman and class C director, which is necessary in combining the offices of governor, chairman, and class C director.

Mr. DIRKSEN. It would be possible then, to take somebody from another section of the country and transport him to some other place?

Governor ECCLES. Yes. The idea of that was to promote able men in the Reserve System by moving them from one bank to another bank, creating a career system. The selection of the Governor, however, must be made by the local board of the reserve bank.

Mr. DIRKSEN. However, you have the power to approve?

Governor ECCLES. That is right.

Mr. DIRKSEN. And you could approve, or you could disapprove anybody that you desired to disapprove? In other words, you could prevent a man from becoming a combination governor, chairman, and Federal Reserve agent by simply giving your disapproval to his selection?

Governor ECCLES. They would have to submit some other name.

Mr. DIRKSEN. So really you would have the power to control?

Governor ECCLES. Well, whether the power of approval is the power to control may be open to debate. It would become necessary for the board of the Reserve bank and the Board here—at least a majority of the board of the Reserve bank and the majority of the Board here to agree upon a man that would be the executive head of the bank.

Mr. DIRKSEN. I think the matter is important, for this reason, and this is not very familiar to me and may not be familiar to you, but in 1927, I think, the rediscount rate was reduced for the purpose of stimulating the investment interests and also stop the flow of gold toward Europe, and the directorate of the Chicago Federal Reserve Bank was rather opposed to it, because they saw a possibility of the flow of capital from every agricultural bank. They resisted the idea, but it was done anyway; and I am not so sure but what, in the light of hindsight, that was right, after all. So if it depends on somebody out there who is absolutely sympathetic with all of the things that are done, that might prejudice the interests of the particular area. That brings up, of course, this question: I was interested in your observations that it was seeking to make them responsive to the national interest. That was the idea I think that you enlarged upon in the course of your remarks some days ago.

Governor ECCLES. Make who responsive?

Mr. DIRKSEN. Well, your Federal Reserve Board, and I suppose your open-market committee; they would be responsive to the large public interest, rather than to the sectional or local interest.

Governor ECCLES. Yes; that is right.

Mr. DIRKSEN. That would, of course, eliminate the checks and balances that did exist between the open-market committee and the Federal Reserve Board and the directors of the respective Federal Reserve banks. In the light of that experience back in 1927 I am just wondering whether it would be wise to eliminate that check, because, in that instance it would have had a most salutary effect upon the country, if the directors of a particular Federal Reserve bank had prevailed, and that probably had been able to carry out their own policies with respect to that Reserve bank district.

Governor ECCLES. Well, of course, if each of the 12 Reserve banks is going to be permitted to operate independently of the interests of the country as a whole, with reference to their monetary policies, it seems to me you would be sure to have great confusion.

Mr. DIRKSEN. If carried to the extreme?

Governor ECCLES. So long as you have 12 banks without a Federal Reserve board, without coordination and the power to deal with the problems of national interest, I cannot imagine how you could have a monetary policy that would be effective in meeting a situation that the Nation might be confronted with. No other country, so far as I know, has a divided responsibility with reference to the monetary policy that would be comparable to a policy made by the 12 different Federal Reserve banks.

Mr. DIRKSEN. You know, section 205 of this bill, in speaking, for instance, of the open-market committee, contains this language: It says that you are to deal, instead of through the Federal Reserve Board, with the Federal Reserve banks, and then the language is, "and the Federal Reserve banks shall conform their open-market operations to the provisions hereof." So, you are going to establish, after all, complete control at a time that might be disadvantageous to the interests of a particular geographical section. For instance, I suppose in Atlanta and Dallas you have certain cotton interests, in Minneapolis you have the grain interests, in Chicago you have not only grain but industrial interests; and that very question came up in 1927, and I am not so sure that, if it had prevailed, we might not have been infinitely better off. Of course, that is a speculative thing, I admit, but that was one instance where it proved out.

Governor ECCLES. I feel that monetary policies must be dealt with on a national basis, and that for each Reserve bank to act independently with reference to open-market policy or discount rates would cause great confusion. Money is like water—it seeks a level; and to raise rates in one section would cause the funds to flow to the section where the rates were raised from the section where the rates were low, which would act to increase the excess reserves in one area substantially and, therefore, make for expansion of credit and cheap money, and have the opposite effect in another area.

Mr. DIRKSEN. But I think you will admit that was practiced in one Federal Reserve district, and we might have had a 2 percent rediscount, and in another place $2\frac{1}{2}$ percent, and another place possibly 3 percent, because that seemed to fit the conditions of that Federal Reserve district at that particular time.

Governor ECCLES. I do not believe it is necessary to have a uniform discount rate at all the Reserve banks and, as a matter of fact, there has rarely been uniformity in the discount rates. The discount rate is proposed by the Reserve banks and approved by the Federal Reserve Board, as a general rule.

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Mr. DIRKSEN. But, examining the maximum possibilities of the bill with respect to the open-market committee, it is quite possible that the Federal Reserve directorate in any particular district would not have anything to say about it, the System insisting that they conform to whatever regulation is laid down about it?

Governor ECCLES. That is correct. If the committee felt it was in the national interest to raise rates to prevent undue expansion and speculation, they would do so; and, if they felt on the other hand that there was an unnecessary contraction, they would want to reduce the rates and the reserve requirements in an effort to stop the deflationary process, so far as they could. It seems to me that must be done in the interests of the Nation, because we have found that every part of the country is very interdependent with every other part of the country, and that money has a very rapid flow and is movable and transferable almost instantaneously.

Mr. DIRKSEN. When Mr. Crowley was before the committee, I asked him about the section entitled I, which provides that mutual savings banks and other banks may become member banks, or insured banks, after July 1, 1937. In other word, you would have to become a member of the Federal Reserve or otherwise have no Federal Deposit Insurance. I presume you are familiar with that?

Governor ECCLES. Yes; I am.

Mr. DIRKSEN. That, in the light of section 202 entitled "II" of the bill, which provides that the Federal Reserve, in order to facilitate their entry into the System, can waive the capital requirements. You enlarged on that somewhat in your observations and said, "and any other requirements that may be necessary." Now, you are familiar with the facts, also, that in organizing many of these State banks, you had to give deferred certificates in lieu of deposits, and I think you have answered that that is a contingent liability charged against the capital and, therefore, you cannot take those banks into the System.

What would you do about those banks, particularly in cases where most of the deposit liability was made up by deferred certificates, and there may be in small banks, as much as $30,000 or $40,000 outstanding of those certificates, and it may take 10 years to earn enough money to pay them off?

Governor ECCLES. I am familiar with that rule and I do not know that I, personally, agree with it.

Mr. DIRKSEN. The rule does exist, however?

Governor ECCLES. Yes; it was the opinion of counsel at the time the question came up, that in the light of the present banking legislation, by reason of those deferred certificates which the banks had issued, although they were secondary to the depositors' claims, still the bank was unable to qualify for membership. Now, one of the reasons for this provision which you just read is, to permit the membership of the banks of the class that you referred to.

Mr. DIRKSEN. Well, now, the corollary of that is this: What will the present members of the Federal Reserve System say if by wholesale, you should take in these banks? They might object to the fact that you are cutting corners in order to get them into the System, might they not?

Governor ECCLES. I cannot see that the other members of the Reserve System could be, in any way, affected by that, except favorably. It would be to the interest of all of the member banks of the System to have all of the nonmember banks members of the System, for the purpose of uniformity in carrying out the banking practices and procedure, and so forth. Admitting those banks into the System does not, in any way, place any liability upon the present member banks.

Mr. DIRKSEN. Well, if this is a fair question, would you care to say, categorically, whether you favor all banks coming into the Federal Reserve System at this time?

Governor ECCLES. I think that it is in the interest of the banking situation as a whole, nonmember banks as well as member banks, to have all banking institutions, which have the power to create money, members of the Federal Reserve System.

I think that the period of 1937 is helpful, in that it gives to the banks an element of time in adjusting their affairs to any extent that they may desire to, before applying for membership; and I think that, if this proposed legislation is passed, permitting the Board to waive the requirements that the nonmember banks are unable to meet, and providing the eligibility features that this bill carries, it will be a great source of strength to the Federal Deposit Insurance Corporation and to the banking system as a whole, through all banks being members of the Federal Reserve System.

Mr. DIRKSEN. Well, now, Governor, if I remember the figures, I think 41 percent of all of the banks in the United States are in towns of 1,000 in population. I am just wondering what distinct advantage will accrue to a bank in a small town which is simply subserving the money and borrowing interests of that community to buy 6 percent of the stock of the Federal Reserve, on which they will get no interest and discount benefits and privileges, which they probably would not use.

Governor ECCLES. They get 6 percent on the stock which they buy, which is a very profitable investment right now. Six percent is what they get on the Federal Reserve bank stock which they buy at the present time. Furthermore, the opportunity of rediscounting or borrowing from the Reserve bank for seasonal requirements or for emergency requirements should be a great source of help to the local community and would tend to prevent bank failures which otherwise might develop.

Mr. DIRKSEN. Well, now, if all of these banks come into the Federal Reserve System, manifestly, you are first destroying the banking authority of your State, and that would be possibly, or would possibly have the effect of superseding the laws of the State with reference to branch banking, and you might have an extension and development of branch banking; is that possible?

Governor ECCLES. I have not said very much about branch banking——

Mr. DIRKSEN. Will you allow me to interpose and tell you that my interest is aroused in the matter because of Senate bill 1926, which was introduced recently by Senator Fletcher, a very short bill, and the last phrase provides that—

Any national banking association may, with the approval of the Federal Reserve Board, consolidate with or purchase the assets of, and thereafter operate as a branch or branches thereof, and national or State banks, or banks, located in the same State, with which such national bank association was on

January 1, 1935, and still is affiliated, or shares or majority of shares of which were, on January 1, 1935, and still are owned by an affiliate of such national banking institution.

Mr. GOLDSBOROUGH. I am putting the committee on notice of the fact that the bill is before us now, and there seems to be a trend toward unification of the banking system. The extent of the branch banking would be easier than it is at the present time, when you still have checks and safeguards of some State law.

Governor ECCLES. Of course, there has been a rapid development of branch banking in the last few years.

The CHAIRMAN. Since the passage of the act that was to restrict branch banking.

Governor ECCLES. The National Banking Act or the Federal Reserve Act permits State-wide branch banking in those States where branch banking is permitted by State law.

Mr. GOLDSBOROUGH. Just to give the historical fact, we let the branch-banking features slip by with the express assurance on the part of those who wanted it that they would stand by the permanent insurance plan, and as soon as the law passed they began to fight the permanent insurance plan; we have had that fight on our hands ever since. Our theory was that it would be impossible to make any branch-banking law effective, because the independent banks would be so strong under the permanent insurance plan that they could preserve themselves. That is the history of that legislation. The branch-banking features would not have passed had we not had the assurance that the permanent insurance plan would be allowed to stand.

The CHAIRMAN. Governor, in connection with what Mr. Goldsborough said, the remark I made a moment ago had reference to the McFadden bill, which dealt with the matter of branch banking.

Governor ECCLES. The development of branch banking has been brought about by the action of the various State legislatures, and I understand that at the present time about one-half of the States permit branch banking, either on a State-wide basis or in some form; and, of course, the national banks are permitted to carry on the branch-banking business to the extent that is permitted in the States in which they operate.

Now, there is nothing in this proposed legislation that in any way changes the present laws with reference to branch banking, and there is nothing that interferes, or encroaches upon, the State banking organizations. The provision that requires insured nonmember banks to become members in 1937 is not in this legislation, but in the legislation that was passed last year. So there is nothing in this legislation that is being considered now that in any way changes the relationship of the State banking authority with reference to the banking structure.

Mr. DIRKSEN. I quite agree. What I was getting at, of course, is that, if a little later, it was all set up it would be made infinitely easier to extend the branch banks.

Now, getting over to section 206, there is a section there that provides that any sound assets may be discounted, that any Federal Reserve bank may discount any commercial, agricultural, or industrial paper and may make advances to any certain member bank on its promissory notes secured by any sound assets of such member bank. I presume an asset may be sound and still be "ill-liquid" rather than liquid, can it not? In other words, it might be good security behind it, but still not liquid?

Governor ECCLES. Yes. Many of the assets which are considered to be eligible and held to be liquid were less sound than many of the assets held by banks which could not qualify for rediscount or security for borrowing from the Reserve banks.

The CHAIRMAN. Mr. Dirksen, let me ask him a question right there, please.

If you have not already stated it, what percentage of the investments of the banks, exclusive of Government securities, is eligible for rediscount with the Federal Reserve bank?

Governor ECCLES. Well, at the present time, I do not know the exact percentage, but I understand it is less than 8 percent of the total loans and investments of the banks that are eligible; and that is according to the classifications made by the banks themselves and not according to the classification made by the Reserve banks. I think, upon experience, the banks would find, if it were necessary to use all the paper which they considered eligible, that some of it would not be so considered by the Reserve banks. So that the figure given, which is as I say, less than 8 percent, is the maximum.

Mr. DIRKSEN. I see section 207 provides that guaranteed obligations of the United States may be bought and sold without regard to maturity. Those are such bonds as Home Owners' Loan Corporation——

Governor ECCLES. And Federal farm mortgages, and so on.

Mr. DIRKSEN. Well, now, I suppose that has to be considered in the light of the provision in the bill which calls for the repeal of the collateral requirements. Is there any notion of policy that something else should be substituted for 50 percent of the eligible paper and collateral in addition to the 40-percent gold reserve?

Governor ECCLES. No. You see, this is providing for the elimination of the collateral requirements against the Federal Reserve notes. The reason for the provision that you have just read is that it is felt that there should not be discrimination between Government bonds and bonds guaranteed by the Government. The fact that the Reserve banks may buy direct obligations of the Government, and the fact that they may not buy long-term guaranteed obligations of the Government is an unjustifiable discrimination between the guaranteed bonds and direct obligations.

Of course, at the time the law providing for the purchase of direct obligations was originally passed, there were no guaranteed obligations; and I feel that, had there been guaranteed obligations at that time the law would very likely have included both direct and guaranteed obligations.

Mr. DIRKSEN. Well, now, heretofore, of course, the note-issuing power was used largely commensurate with the rise and fall of business in that area; and if there had to be a 40 percent gold reserve and 60 percent of eligible paper, there had to be commercial transactions behind all of that paper. And so as there was a fixed volume of business, the chances of any demand on the Federal Reserve agent for more Federal Reserve notes, or less, depended on whether the tide of business was high or low.

Now, that collateral requirement is to be repealed and you are authorized to buy and sell in the market, and these guaranteed obligations of the Government—that is what is called elasticity, which does not mean a great deal to me—however, it is taken away, and from then on the amount of notes that will be issued will bear no definite relationship to the amount of business in the 12 Reserve districts, or it may be a very arbitrary amount.

Governor ECCLES. That was the theory upon which the collateral requirements for note issue were based, but that is proving to be inapplicable to the facts in the case. The greatest requirements for notes in any year in this country happened when the business volume was at its lowest, showing that the demand for currency does not necessarily follow the fluctuations of business. The fluctuation of bank lending on short-term eligible paper reflects to some extent the activity of business. The call for Federal Reserve notes in the United States, a country where 90 percent of the business of the country is done by check, has very little relationship to the volume of business.

As I stated a few days ago in discussing this question, the Reserve banks have two classes of liabilities: One is the deposits to the member banks and the other is the notes outstanding.

The CHAIRMAN. Will you not add to that, the capital held by the other banks?

Governor ECCLES. That is a liability to the stockholders, of course; and the surplus is a liability to the Government. In liquidation, the assets of the Reserve bank consist of the gold certificates, and the investments that the Reserve banks make in governments, and loans and discounts which they make to member banks.

I see no reason for putting up 40 percent gold certificates back of notes and then putting up eligible paper to the extent of 60 percent. As a matter of fact, it would be perfectly impossible to cover the note requirements of the banks by 60 percent of commercial paper; because the banks do not have the paper to cover that proportion of the note requirements. Therefore there would not be sufficient Federal Reserve notes to meet the requirements, if the Reserve banks were required to secure notes, as originally contemplated in the act, by 60 percent of the commercial paper.

There is no difference between note liability and deposit liability. They are both liabilities of the bank and there would seem no more occasion for the securing of notes than it would for the securing of deposits. All of the assets of the Reserve banks are back of all of the liabilities of the Reserve banks. The type of assets that the Reserve banks hold—outside of the Government bonds which they buy and the gold certificates which they hold—is determined by each Reserve bank, when that Reserve bank extends credit to member banks.

Mr. DIRKSEN. Well, Governor, if you have more than 40 percent gold reserves, that means that the Federal Reserve bank has got to issue $2.50 for every gold certificate dollar that it has; is that correct?

Governor ECCLES. What is that?

Mr. DIRKSEN. If you have that 40-percent gold reserve behind every dollar of Federal Reserve notes issued, you will have issued

$2\frac{1}{2}$ times for every gold certificate that the Federal Reserve banks may have?

Governor ECCLES. That would be right.

Mr. DIRKSEN. Then in the light of the fact that you could buy and sell without limit, virtually, all of the outstanding contingent obligations of the Government, or those that are guaranteed, you could retire most of them today if you so chose, and if that was going to be the policy, by rather copious note issue; that would be entirely possible under the bill, would it not?

Governor ECCLES. As I understand it, the bill would not change that situation, at all.

Mr. DIRKSEN. But I would think that would be possible, would it not?

Governor ECCLES. The present law permits notes to be secured by Government bonds and gold certificates. That is not in the present law, it was in the Emergency Banking Act of 1932.

Mr. DIRKSEN. You could, instead of just securing them, retire them altogether?

Governor ECCLES. What is that?

Mr. DIRKSEN. I say, instead of securing them, you could retire them altogether?

Governor ECCLES. Retire what?

Mr. DIRKSEN. Retire these bonds that had been guaranteed as to principal and interest, being nothing more than a note issue——

Governor ECCLES. You mean that the Reserve Bank, through open-market operations, could purchase all of the outstanding, or as many of the outstanding Government bonds and guaranteed bonds as they chose to do?

Mr. DIRKSEN. Yes; as far as there were gold certificates available that would be possible, would it not?

Governor ECCLES. Yes; but, of course, that would increase the reserves of the members by the amount of bonds which were purchased, and the excess reserves of the members today are something over $2,000,000,000. To extend that reserve, banks purchase additional Government bonds or bonds guaranteed by the Government—they would increase the reserves of the member banks.

Mr. DIRKSEN. I think this morning, or yesterday, you made the observation that the relationship of income to the deposit currency was as 3 to 1, or substantially so?

Governor ECCLES. In 1928, and 1929 it was 3.12. That was about the average, as I recall, of the deposits and currency to the national income. In 1933 the relationship, or what is spoken of as the income velocity, was about $2\frac{1}{3}$. At the present time, it would be substantially less than that. That increase of money, deposits plus currency, has been much more rapid than the increase in income, and hence, the velocity has been reduced.

Mr. DIRKSEN. Has that relationship of 3-to-1 between the income and deposit currency existed for a longer period than since 1929?

Governor ECCLES. No; it has been steadily going down.

Mr. DIRKSEN. It has been going down since that time, but I mean anterior to that period. I do not know where I got that figure, but——

Mr. GOLDSBOROUGH. Does income mean the same as production?

Governor ECCLES. Yes; it is spoken of as the national income. Dr. Currie says the figure was very stable from 1923 to 1929.

Mr. DIRKSEN. At 3-to-1?

Governor ECCLES. Yes.

Mr. DIRKSEN. And before that time, what was it?

Governor ECCLES. I do not have the figure on it. Of course, during the war period and during the period of depression in 1920 and 1921, I imagine there would be some changes in ratio.

Mr. HANCOCK. May I ask a question?

Mr. DIRKSEN. Yes.

Mr. HANCOCK. Governor, what do you mean by "national income?"

Governor ECCLES. What I understand to be the basis for figuring the national income is the price of all goods, whether consumer's goods or capital goods, that are produced in any one year.

Mr. HOLLISTER. For ultimate sale?

Governor ECCLES. Would that be sale?

Dr. CURRIE. It is the wages, profits, dividends, of all the money actually received by the income receivers.

Governor ECCLES. It is supposed to represent all the goods bought and sold.

Mr. HOLLISTER. That is, the ultimate sales?

Governor ECCLES. The ultimate sales, yes; otherwise you get duplication. That is right, the ultimate sales.

Mr. HOLLISTER. Dr. Townsend refers to $1,200,000,000,000, and I wanted to be sure about it.

Governor ECCLES. No, you have $900,000,000,000 to $1,000,000,000,000 of bank debits, which, based upon the amount of demand deposits would possibly give a velocity of deposit currency turn-over of over 50 times in the period of 1928 and 1929.

Mr. HANCOCK. At what rate is the national income running today?

Governor ECCLES. Well, I do not know. I do not know that there are any figures at all on it.

Mr. HANCOCK. What was the national income in 1934, as defined by you?

Governor ECCLES. Do you have the figures of the Department of Commerce?

Dr. CURRIE. No; not for 1934.

Governor ECCLES. I have heard it variously estimated from $50,000,000,000 to $50,000,000,000, but you would really have to have the complete figures for 1934.

Mr. DIRKSEN. At any event, that ratio is invariable and goes back to 1923?

Governor ECCLES. It was relatively constant.

Mr. DIRKSEN. And for any increase of $1,000,000,000 in deposit currency, you would get an increase of $3,000,000,000 in national income?

Governor ECCLES. Well, theoretically, but that has not been the case from 1929 to 1934.

Mr. DIRKSEN. But if it were invariable, there would be a great incentive then to increase the amount of deposit currency, in the hope of increasing the national income by just exactly three times that amount and all the good that we could do with that amount of money?

Governor ECCLES. It would be fine—there is no question about that—if we could do that by an increase of our volume of money, without regard to who owns the money, and thus regulate our national income. I do not believe that is possible. I do feel, as I have said before, that of course the volume of money is an important factor; and, certainly, with high interest rates and shortage of reserves today, you could expect no credit expansion, and such a situation would be very deflationary. Excess reserves, such as we have today, which bring down the rate of interest, should ultimately lead toward creating credit expansion—whether we can do that and recover time alone can tell. That is one of the factors and one of the elements that will help make for recovery, if private credit expansion can induce recovery.

Mr. Driscoll. Governor, I am not entirely clear in my mind as to the expression "national income"; does that mean the price of every taxable article that is produced in the United States per year?

Governor Eccles. It is the income received from the production of all goods.

Mr. Driscoll. We will say all of the hay, tobacco, textiles, wool that is sold?

Governor Eccles. No; you would get duplication then.

Mr. Driscoll. Not if you sell it only once?

Governor Eccles. That is right. For instance, you would sell wheat to the miller, and the miller would sell the flour to the wholesaler and so on, and you would get, of course, a duplication, because that would be the flour sold to the consumer——

Mr. Driscoll. And not the wheat sold by the farmer?

Governor Eccles. No.

Mr. Sisson. In other words, there is a great distinction between the national income and the total turnover of business.

Governor Eccles. A very great distinction.

Mr. Sisson. Many times?

Governor Eccles. A very great distinction, but the national income determines the actual wealth produced, which determines the well-being of the people if it is properly distributed.

Mr. Ford. Might I suggest that my interpretation of "national income", is all wages, interest, dividends, ultimate sale prices of goods. Does not that fairly well cover it?

Governor Eccles. I think that is the rule.

Mr. Sisson. That would not include the lawyers' income, who are not productive members of society, as a part of the national income?

Governor Eccles. Yes; it includes a lawyers' income.

Mr. Williams. How about wages?

Governor Eccles. The same thing applies.

Mr. Hollister. Would not the real test be not the national income in dollars, but the units of articles sold in respect to these other particular years? If your prices are quite different, your national income may look different, but it is the units of things that happen to be sold in a particular year, with reference to the other year?

Governor Eccles. Yes, the production; that is right.

Mr. Driscoll. Governor, I see that section 209 of this bill confers upon the Reserve Board the authority by regulation to change the requirement as to the reserves to be maintained against demand or time deposits. As I understand the percentage on demand is now 13 for Chicago and New York, and 10 for other eastern cities, and 7 for the country banks, and 3 percent on time deposits?

Governor Eccles. That is right.

Mr. DIRKSEN. Now, at one time, I think when the Federal Reserve was raising prices, it was up to 25, 18, and 15, was it not? Was it not much higher, and mounting higher when the Federal Reserve was first enacted?

Governor ECCLES. It was higher than it was in 1925; it was 18 and down below 18.

Mr. DIRKSEN. It has been reduced?

Governor ECCLES. Yes. Dr. Goldenweiser, I wonder if you know the reason for the drop in the Reserve requirements, from those higher percentages to the percentage that applies at the present time?

Dr. GOLDENWEISER. The reason requirements were reduced at the time was that it was the theory that the cash held in the bank vaults amounted to about that much. When this cash in the vaults held by the banks was excluded from the legal reserve, there was an allowance made for it.

Mr. DIRKSEN. You do not require any cash in vault now, do you?

Dr. GOLDENWEISER. No. When they would not let it count as reserves any longer they reduced the requirement.

Mr. DIRKSEN. No; actually, there is no cash in the vault at the present time, only of course these reserves against the deposits that are deposited with the Federal Reserve bank?

Governor ECCLES. There is cash in the vault, and these reserve requirements of 7, 10, and 13, as I understand Dr. Goldenweiser, were reduced because previously the cash held was considered as a part of the reserve requirements, and the cash now held by the banks is not considered a part of the reserve. There is no legal cash requirement, but banks have to hold sufficient cash to be able to meet the cash requirements of their customers, and those requirements fluctuate from day to day.

They have to ship money, from the Reserve bank to their bank and the amount of cash required by a bank that is not in a Reserve center, that is, in centers where there is no Reserve bank or branch of a Reserve bank, is relatively higher than the percentage of cash that is carried in a bank where there is a Federal Reserve branch bank or Reserve bank.

Mr. DIRKSEN. What reserves do the Bank of England and the Bank of France require, as compared to these requirements here?

Governor ECCLES. I am unable to say.

Mr. DIRKSEN. Dr. Goldenweiser, what can you say about that?

Dr. GOLDENWEISER. There are no legal requirements about the reserves of commercial banks.

Mr. DIRKSEN. In practice, what do they maintain?

Governor ECCLES. Well, in England, somewhere around 10 percent, as a rule.

Mr. DIRKSEN. Yes; both the demand and time deposits?

Dr. GOLDENWEISER. Yes; against their deposits.

Mr. DIRKSEN. Against all deposits?

Dr. GOLDENWEISER. Yes; and in France I do not know, because in France they hold so much of it in actual notes and the ratio varies, but it is not very greatly different from the English system.

Mr. DIRKSEN. Well, now Governor, section 209, of course, would confer upon the Federal Reserve Board the power to raise or lower those reserve requirements; in other words, instead of 13, 10, and 7, you could reduce them to 10, 7, and 3, and you might reduce the reserve against the time deposits to 2 percent or even 1 percent. In practice, how much of that reserve deposit do the Reserve banks, as a general thing, carry?

Governor ECCLES. You mean the member banks?

Mr. DIRKSEN. No; of the deposits that are carried by member banks in the Federal Reserve bank, do they keep all of the 13 percent or 10 percent or 7 percent on hand, or do they use it?

Governor. ECCLES. The Reserve banks.

Mr. DIRKSEN. Yes.

Governor ECCLES. The Reserve banks do not invest their money—that is, their deposit money—from the standpoint of keeping their money operating at a profit. It is their business to invest their money in open-market purchases as a regulatory measure of the monetary system.

Mr. DIRKSEN. Well, the purpose, apparently, of that section is to give greater flexibility and give the Federal Reserve Board the authority to raise or lower their reserve requirements, and——

Governor ECCLES. That provision with reference to the reserve requirement is now in the law. The Thomas amendment to the act of May 12, 1933, added to the Federal Reserve Act a provision giving the Federal Reserve Board the power, by declaring an emergency, to raise the reserve requirements, with the consent of the President. That was put in there as a supplemental monetary control to open-market operations. It is a control against inflation.

Mr. DIRKSEN. Against inflation?

Governor ECCLES. Yes; that would be the purpose of that—a control against inflation. For instance, assuming that the excess reserves of member banks greatly exceeded the amount of Government bonds which the Reserve banks held and the bills which they held, there would be no way of controlling through open-market operations an inflationary credit expansion on the part of member banks. There would be no way of reducing or wiping out their excess reserves upon which credit inflation is built. For instance, if the authority now granted to issue $3,000,000,000 of greenback currency was exercised, and if the $2,000,000,000 of gold profit now in the stabilization fund were used, $5,000,000,000 additional bank deposits would be created.

Mr. GOLDSBOROUGH. Right there, if that money were used to retire Government bonds, the deposits would not be increased but the reserves would be increased?

Governor ECCLES. That is right. In that case it would increase the reserves by that amount, but it would increase deposits to the extent that it retired Government bonds not held by the banks. If the money was used to retire Government bonds held by individuals, it would increase deposits and increase reserves; to the extent that it was used to buy Government bonds held only by the bankers, to that extent it would increase the reserves alone without increasing deposits.

It is possible with the use, we will say, of the $5,000,000,000 referred to, to increase the reserves by that amount. Additional gold may continue to come into the country, which would also tend to increase the reserves. So that the banking system could build up excess reserves from the $2,300,000,000, approximately, that they hold now to $7,300,-000,000 plus any increased gold that comes in. You would have a potential agency for bank-credit inflation that would simply be terrific and no open-market operation could control it. An increase of reserve requirements would have the same effect in extinguishing the excess reserves as a sale of securities, and that is why this proposal is made.

Mr. DIRKSEN. That is the sense of the 20 percent in this bill?

Governor ECCLES. Yes.

Mr. DIRKSEN. Ultimately to extinguish the reserve requirements, if necessary?

Governor ECCLES. Yes.

Mr. DIRKSEN. I think I have only one more question, and that is with reference to section 210, dealing with real-estate loans. I was much interested in the discussion this morning, and I wondered whether, after all, we could not keep the banks on a commercial basis and keep them liquid by letting the building and loan associations handle the amortized real-estate mortgages up to 20 years, and pursue the policy of greater leniency with respect to bank loans, to such thrift agencies that now operate. I say that for this reason—the building and loan associations are equipped to handle the amortized loans, and if the banks were going to handle them in any quantity, they would have to set up separate establishments and take on additional personnel to do that.

Mr. CAVICCHIA. May I say this, Mr. Dirksen?

Mr. DIRKSEN. Yes.

Mr. CAVICCHIA. The great trouble was that many building and loan associations were running businesses in opposition to the banks. They got in the habit of going to the banks to borrow money on notes and pay, say, 5 percent on the money that they borrowed from the national bank or trust company; and they would proceed to lend it to me, or the man who wanted to buy himself a home; and they would get 3 percent or 4 percent or 5 percent bonus; and if they started to sell preferred shares to depositors and some of these companies borrowed—they did not borrow, but they took on deposit money on which they guaranteed as much as 7 percent per annum, which no bank could afford to pay. If the building and loans had not gone to that field, they would not have suffered as much as they did when the crash came in 1929.

Mr. DIRKSEN. Well, let me say there are probably 700 or 800 Federal savings and loan associations that have been established now; and, of course, their sole mission is to deal in amortized loans.

Governor ECCLES. Well, I may answer that by stating that the Federal savings and loan associations are members of the home-loan banks.

Mr. DIRKSEN. And those are rediscount institutions?

Governor ECCLES. Yes; and those institutions can borrow money from the home-loan banks at 3 percent. Therefore I do not know how commercial banks owning substantial savings funds upon which they pay 2½ percent could compete with the home-loan banks in providing funds to savings and loan associations.

Mr. DIRKSEN. It could, but for one thing, and do you know what it is? It is the bank examiners. There are lots of buildings and loans that would go to the banks and make their notes signed by all of the directors, get the money, and pour it into the development of building and construction in their communities; but I doubt very much whether the examiners would permit that at the present time.

Governor ECCLES. The only thing is that a bank, in order to pay 2½-percent interest on time funds, which it will likely have to pay to hold the funds against the competition of the 3- and 3½-percent rates paid by savings and loan associations, must lend those time funds on a basis to yield them not less than 5 percent.

A building and loan association, as a member of the home-loan bank, would not be willing and could not afford to pay the banks 5 percent for funds which they in turn would have to loan out at 8 percent; and in borrowing from the banks, they would borrow on a short-term basis and would be loaning in the community on homes on a long-term basis. Therefore I do not think it is practicable to expect the building and loan companies to borrow from the savings or time funds of commercial banks.

Mr. DIRKSEN. There is one statement in here, one proviso in the section dealing with real-estate loans, section 210, that says:

> Nothing contained in this section shall prevent any national banking association from acquiring, as additional security for loans, previously made in good faith, second or subsequent liens on real estate or shares or participations in such liens.

Those are junior liens, or they would not be second mortgages?

Governor ECCLES. That is right.

Mr. DIRKSEN. There would not be anything to prevent a bank from taking a $2,000 first mortgage on a $10,000 property, and then stepping in a little bit later and taking another junior mortgage for $1,000, and making a junior lien against the first mortgage against the property, if they so desired. I believe you stated this morning you thought that was rather poor financing to even indulge in junior liens, if it could be avoided.

Mr. ECCLES. A bank should be prohibited, in the first instance, from taking a junior lien—from making a loan secured by a junior lien; but if a bank has a loan, and even though it may be an unsecured commercial loan or a collateral secured loan, the bank is justified in taking a second lien, for additional security, if conditions develop where the loan, which was adequately and properly secured, or a loan which was made to a concern which had ample resources, gets into a position where it becomes a doubtful loan. In such cases the bank may take a second mortgage or take any other security that it can get; and banks have always done that, in fact. They have always been doing that.

Mr. DIRKSEN. The only requirement, however, in that language, is the faith of the bank, "previously made in good faith."

Governor ECCLES. I think possibly the only reason for that language there is this: The banks, we know, have always taken, and there has been no prohibition upon banks taking, for debts previously contracted, second mortgages or any other collateral.

Mr. DIRKSEN. Have they that authority now?

Governor ECCLES. Yes.

Mr. DIRKSEN. To take second mortgages?

Governor ECCLES. Yes; they have always done that.

Mr. CAVICCHIA. Is there not some confusion here, Mr. Dirksen? I think you mentioned about a bank lending their $10,000, and subsequently he wants to borrow another $1,000 on the same piece of real estate. That is perfectly legitimate, because it is considered practically one mortgage loan—is it not—whether it is made in one loan or two loans; am I correct, Governor?

Governor ECCLES. It would seem to me that it would be considered a first and second mortgage, because the first mortgage might be sold without recourse, and certainly the $1,000 mortgage would then be a second mortgage. So long as both pieces of paper are held by the same institution, they would be, for all practical purposes, the equivalent of a first mortgage.

Mr. CAVICCHIA. I had in mind the building and loan practice, where a man has $5,000 mortgage, and a year or two later wants another $1,000; in all respects, that is considered as one mortgage. Now, a second mortgage is never taken by a building and loan—by a member bank unless it wants to secure some loan that it had already made; is that correct?

Governor ECCLES. That is right.

Mr. HANCOCK. Mr. Dirksen, may I ask one question?

Mr. DIRKSEN. Yes.

Mr. HANCOCK. In addition to the fact that there is such a small amount of eligible commercial paper available for rediscount, did I understand you to say the other day that one of the reasons why you were suggesting that 20-year amortized real-estate mortgages should be made eligible for borrowing was the fact that unless the banks did handle this type of paper, these loans would continue to gravitate to the home-building and thrift institutions?

Governor ECCLES. We are not proposing that 20-year mortgages, as such, be eligible for rediscount. The proposal is that the banks be permitted to make amortized real-estate loans on improved property up to the maximum period of 20 years, up to a certain percentage of their time funds.

Mr. HANCOCK. Sixty percent, is it not?

Governor ECCLES. Yes. Now, with reference to the question of eligibility, there is nothing said at all about the right to rediscount those mortgages. The wording of the eligibility provision is to the effect that the Federal Reserve Act would be amended to authorize the Federal Reserve banks, subject to regulations of the Board, to discount for member banks any commercial, agricultural, or industrial paper, and to make advances to member banks on promissory notes, secured by any sound asset.

Mr. HANCOCK. I understand. This is something that was recognized in the Emergency Banking Act, that the member banks be permitted, on their bills payable or promissory notes, secured by sound assets, to borrow from a Reserve bank, and the credit department of each Reserve bank would determine the terms upon which the member bank could borrow.

Let us see if we understand each other right there for a minute. Under that provision, would the member bank be able to endorse, without recourse, a first-mortgage note to a Federal Reserve bank?

Governor ECCLES. A member bank now cannot endorse without recourse any paper to a Reserve bank. All borrowing from the Federal Reserve bank is done on eligible paper, on the discount basis, with recourse, and all the bill does is to broaden the borrowing privilege so as to give to the Reserve banks the power to lend to member banks on the member bank's note for a period of 3, 6, or 9 months, according to the regulations that the Board may make, those notes to be secured by bonds, mortgages, or loans secured by collateral, with such margin as the Reserve banks may consider adequate to make the loans safe and sound to the Reserve bank.

Mr. HANCOCK. I think I understand that now; you see if I do. In other words, the member banks, under this provision, would not be able to rediscount a 20-year amortized mortgage with the Federal Reserve System, but use the mortgage as collateral for a loan.

Governor ECCLES. That's correct.

Mr. HANCOCK. But it could give its own note, secured by the 20-year amortized mortgage, and secure a loan from the Federal Reserve bank, if that was a sound asset?

Governor ECCLES. The Reserve bank would determine what margin might be required, and would also determine whether the loan would be made for 3 months or 6 months, or a longer period.

Mr. HANCOCK. But that would enable the member bank to be in a position, in time of emergency, to take that paper and use it for the purpose of liquidity?

Governor ECCLES. The same as it could with eligible paper; that is right.

Mr. HANCOCK. In other words, you mean put real-estate mortgages on parity, as they should always have been, so far as eligibility is concerned, with bonds?

Governor ECCLES. Government bonds, you mean?

Mr. HANCOCK. Yes; Government bonds?

Governor ECCLES. Yes; so far as being able to borrow money from the Reserve bank is concerned.

Mr. CAVICCHIA. Is this inflation, Governor?

Governor ECCLES. This is not inflation, because no member bank is going to borrow from the Reserve bank as long as it has excess reserves. Now, when the borrowings of member banks reach the point where you can get credit inflation, just as we have had in this country in the past, it was said to be the duty of the Reserve Board and the Reserve banks to raise the discount rates and to discourage future credit expansion.

Inflation can only be brought about by the willingness of the people and corporations to borrow money, and that is one thing we are trying to get; we are trying to induce the borrowing and lending of money upon which recovery is based. We are talking about the fear of inflation or reflation, when, as a matter of fact, that is what we want.

Mr. DIRKSEN. Governor, I have one more question, and that is predicated on the question asked by the chairman of the committee last week, when, off the record, he observed something about the condition of one of the Federal Reserve banks. Was that early in 1933?

The CHAIRMAN. I am not sure that I remember the remark you refer to.

Mr. DIRKSEN. Well, I got the impression at that time that it was the Federal Reserve banks that had lost their liquidity; is that possible?

Governor ECCLES. The Reserve bank lose its liquidity?

Mr. DIRKSEN. Yes.

Governor ECCLES. I never heard of that.

Mr. DIRKSEN. I got that impression at the time, but that is neither here nor there. I am just wondering if, carried to its logical conclusion, there is plenty of demand for this money; and, as you say, the assets can still be sound and still not be liquid, but if those were infiltrated to the Federal Reserve banks, you may have another flurry similar to the one we went through.

Governor ECCLES. An asset that may be considered sound and liquid with business activity and a high rate of employment and national income becomes frozen and unsound when the national income diminishes. Soundness is not determined only by the substance of a loan or asset at the time the asset is purchased or the loan is made; it depends upon the state of trade and business which follows, and it is up to the banking system to maintain a state of trade and business that will preserve soundness, if soundness existed when the credit was created, in so far as it is possible.

When certain foreign bonds were purchased, German bonds, prior to the war, we considered those the best in the world, and they were sound assets. When wheat was selling at $2 a bushel, it would have been considered perfectly sound, and the paper would have been eligible to have been loaned upon, and it would have been proper to have loaned upon that wheat with a 25-percent margin, on the warehouse-receipt basis. The same thing is true in any other commodity.

I remember when sugar was selling at around $21 a bag, and within a 6-month period it fell below $5 a bag. I am not arguing that a loan of 80 percent of the value of $21 sugar would have been sound.

I remember when sheep were selling at $16 a head, when within a 6-month period you could not sell them at $4 a head, yet a loan made on sheep at $16 for 9 months—that is, on the basis of 50 percent of $16—say, $8 a head for 6 months was eligible; whereas before that loan came due that security was not selling for one-half of the amount of the loan.

The point I am trying to make is that the question of liquidity and the question of soundness depends upon the state of trade and the state of business; and to the extent that forced deflation through forced credit contraction is obviated through making available the rediscount facilities of the Reserve banks—to that extent you provide liquidity. The only liquidity that really exists in a serious depression is the liquidity that is provided through the money-issuing agency, the Reserve System. Even Government bonds cease to have liquidity at the price at which corporations can sell them without going bankrupt.

The price of Government bonds in 1932 was down, the 3's, I think, to $83. A bank holding any substantial amount of those bonds—to have sold them at that market—and if any substantial amount had been sold, the market possibly would have gone to $50, and the bank would have been ruined. The banks, however, could go to the Federal Reserve banks and borrow on those Government bonds, and that was a protection to the market, and also a protection to the banks, which would not have existed if the banks had been forced to sell those bonds to get money to meet the demands, instead of going to the Reserve bank and getting the money.

Mr. HANCOCK. Mr. Dirksen, may I ask one other question?

Mr. DIRKSEN. Yes.

Mr. HANCOCK. Now, deposits you have already written off.

Mr. DIRKSEN. I think if the Governor wanted to, in the light of the fact that it was related to the bonus, he might make a further observation.

Governor ECCLES. I do not care to express an opinion on matters of that kind, because I feel it is entirely outside of my official position. I have my personal opinion, but I think it is outside of my official position.

Mr. DIRKSEN. I have just one observation to make with reference to this last section of title II, and it is this: Whether or not the time deposits will be drained off in the form of real estate amortized loans to any appreciable extent, will depend entirely upon the public demand?

Governor ECCLES. Entirely.

Mr. DIRKSEN. The public demand must necessarily be occasioned upon the purchasing power?

Governor ECCLES. There is no question about that.

Mr. DIRKSEN. If you have not got the purchasing power, they might demand until they are blue in the face, and it would not do any good; and that, in turn, is conditioned upon the state of employment in the country?

Governor ECCLES. That is correct.

Mr. DIRKSEN. The question that comes up to us is: Which is the first, the hen or the egg? And I question whether it is going to do any good.

Governor ECCLES. If you get demand for long-term credit for home construction or for other construction, and the facilities for providing it do not exist, that would be most unfortunate.

Now, I feel that, with low interest, and abundance of excess funds, that the need and desire of institutions with those funds should be to put them to work, and that may tend to create some construction. I do not believe that the demand, today, throughout the country as a whole, for long-term, amortized loans is entirely being met. What you say about the hen and the egg is true, and I am not claiming for the eligibility feature of this legislation and the real-estate feature, one of which is the corollary to the other, that it will bring about recovery; but it would create the machinery upon which recovery can be brought about.

I might say this: That the increase in private expenditures for equipment and construction await upon the increased demands for products of industry. The increased demand depends upon the increased incomes, as a whole. Increased incomes await upon increased expenditures in construction. There is your circle.

Now, the impasse can be broken in the first instance, I believe, only by the various Government activities, and if the impasse is broken, then you have created here the machinery with which to help carry forward, just as you are creating in the case of the Home Owners' Loan Act and providing funds for your home-loan banks to loan to the members of the home-loan banks. That is the agency that will help in the mortgage field as well.

Mr. HANCOCK. That is what you said in 1933, is it not?

Governor ECCLES. Something like that.

Mr. DIRKSEN. That is all I have to ask, Mr. Chairman.

The CHAIRMAN. All right. Mr. Wolcott, have you any questions?

Mr. HANCOCK. Let us adjourn now until in the morning, Mr. Chairman.

Mr. FORD. May I make one observation before we adjourn?

The CHAIRMAN. Pardon me just a minute. Let this be off the record.

(Here follows discussion off the record.)

Mr. SISSON. As I understand it, this bill makes no change in the law with respect to the liability of the banks that are members of the permanent insurance fund for assessment; that is, in other words, the assessment is still based upon the total amount of the deposits; that is correct, is it not, whether insured or not?

The CHAIRMAN. That will be the situation under the new law, but it is not the basis on which the assessments are made under the law as is stands now.

Mr. SISSON. I know, but it was contemplated as a permanent fund?

The CHAIRMAN. Well, under the permanent plan, there would be an assessment of one-fourth of 1 percent, to be repeated in case of necessity. The necessity depends upon whether or not the total fund on hand equals one-fourth of 1 percent of the amount of the total deposits of insured banks.

Mr. SISSON. Well, what I am getting at, Mr. Chairman, is this: You all know that was one of the points at issue last year, and that is going to be one of the points in controversy this year. We are getting some letters from certain banks to the effect that that is inequitable; that is, when the total amount of the deposits that are insured are a relatively small percentage of their total deposits, as compared with their uninsured deposits, they are making the claim that there should be a change made.

I am not taking any position. In fact, if I were to take any position now, I would be opposed to that contention.

The CHAIRMAN. I think you will find, Mr. Sisson, in Mr. Crowley's testimony, and in Mr. O'Connors' testimony that that phase of the legislation is fully covered, not only as to the changes made and the systems being employed, but all fields that enter into the calculation are covered.

Mr. HANCOCK. Mr. Chairman, may I respond to my good friend from New York?

I had occasion, today, Mr. Sisson, to go into a case affecting an institution in my own State. I received a letter recently criticizing the method proposed under title I of the new bill, whereby the proposed assessment of not more than one-twelfth of 1 percent would be levied against the total deposits in any one institution, annually. This institution that I have in mind, under the present law, insured $20,700,000 of its total deposit liability of $58,000,000, and the present cost to that institution is approximately $51,000 a year. Under the provisions of the new act, whereby the assessments apply to the total deposits of $58,000,000—on the basis of not in excess of one-twelfth of 1 percent, the cost of insurance to this institution is actually reduced $3,000, to $48,000 a year; and 13,000 institutions that are insured today would carry this insurance at a lesser amount under the new act than they do under the temporary plan at the present time.

Mr. WILLIAMS. The fact is, there is no insuring under the permanent system and——

Mr. HANCOCK. No; I say, under the temporary plan.

The CHAIRMAN. Well, gentlemen, have we decided to adjourn for the afternoon? We will meet at 10:30 in the morning, and I hope we shall finish with Governor Eccles tomorrow.

(Thereupon, a recess was taken in the hearing until 10:30 a. m., Friday, Mar. 15, 1935.)

BANKING ACT OF 1935

FRIDAY, MARCH 15, 1935

HOUSE OF REPRESENTATIVES,
COMMITTEE ON BANKING AND CURRENCY,
Washington, D. C.

The committte met at 10:30 a. m., Hon. Henry C. Steagall (chairman) presiding.

The CHAIRMAN. All right, gentlemen, there is nothing in the House to interfere with our meeting today.

We will resume with Governor Eccles. Mr. Ford, have you something?

Mr. FORD. Mr. Spence is next.

The CHAIRMAN. That is all right. Mr. Spence, if you have any questions, you may proceed.

Mr. SPENCE. Governor Eccles, what will be the practical effect of waiving the collateral requirements for the issuing of Federal Reserve notes? In other words, is there any limitation, or will there be any limitation on the issuance of notes?

Governor ECCLES. There is no limitation now, for all practical purposes. What determines the use of currency is not the Federal Reserve banks, nor the member banks, but the people of the country who have claims on the deposits in the banks. They have the right to request a bank to pay them in currency. The bank, in order to be able to pay them such currency as they request, goes to the Federal Reserve bank to get the currency. The bank, in order to get the currency from the Federal Reserve, must have a balance with the Federal Reserve, just as an individual depositor with a bank must have a balance with the bank. Therefore, the only limitation upon the issuance of currency is the demand for currency by the people of the country that have bank deposits, and the collateral requirements in no way affect or change the amount of the currency.

Mr. SPENCE. What was the philosophy of the original act which so meticulously made the requirements for collateral?

Governor ECCLES. I do not know that I can say. I could only surmise what was in the minds of the framers of the act at that time. The theory apparently was that the demand for currency would fluctuate directly with the volume of activity of business, and as business increased in activity, it would increase its borrowings on eligible paper, which, together with the gold, would supply the necessary collateral for the Federal Reserve notes; and, as business activity slackened or decreased, the volume of eligible paper held by the banks would be reduced, and hence the volume of currency would be reduced.

It has been found, however, that there is nothing in the history of the Federal Reserve System to warrant such a conclusion. This is the only country where there is a central banking system, outside of Great Britain, which requires collateral to be held back of the note issue of the central bank. All of the new central banks which have been established in recent years recognize that, in essentially a check-using country, there is no necessary relationship between the use of currency and the volume of business.

We heard a great deal of talk about issuing currency with the idea that, if that currency is issued in greater quantity than is now outstanding, it would improve or help business. The direct spending by the Government of currency, from the standpoint of the actual money in circulation, and the business activity created thereby, would be no different than the same amount of money spent by the Government as the result of its present method of financing; because you cannot keep out in circulation more currency than is required by the country to meet its convenience in doing business. The currency comes right back to the banks and from the banks goes to the Federal Reserve banks and is destroyed. We have noticed that, from the time of the bank holiday up until the present time, the amount of currency in circulation has been reduced by about $2,000,000,000.

Mr. SPENCE. What is the total amount of gold held by the Federal Reserve, Governor?

Governor ECCLES. I do not recall the figures. Do you have that, Dr. Goldenweiser?

Dr. GOLDENWEISER. Gold certificates held by the Reserve banks amount to $5,400,000,000.

Mr. FORD. $7,866,000,000 in 1934.

Governor ECCLES. That would probably include the gold held by the Treasury as well. The Federal Reserve would not have that.

Mr. SPENCE. The amount of gold reserves upon which the circulation is based; what would that be?

Governor ECCLES. The law requires a 40-percent reserve against Federal Reserve notes in circulation. Those gold certificates, plus the Government bonds or commercial paper, or both, are held by the Federal Reserve agent as collateral. In the absence of commercial paper, it was necessary to accept Government bonds to make up the 60-percent difference between the 40-percent gold and the total of notes outstanding.

Mr. SPENCE. And this act is that 40 percent of the gold reserve is the sole basis of the circulation?

Governor ECCLES. Yes; 40-percent gold reserve is the only limitation. There is also a reserve required against the deposits of the Reserve banks, which is 35 percent in gold or lawful money.

Mr. SPENCE. And the circulation, based upon the gold now held, would be two and one-half times that?

Governor ECCLES. So far as gold is concerned——

Mr. SPENCE. So far as gold is concerned?

Governor ECCLES. Yes; there is almost sufficient gold now to back up the outstanding currency 100 percent.

Mr. SPENCE. As I understand, the Federal agent was the agent of the Federal Reserve Board in its dealings with the Federal Reserve banks?

Governor ECCLES. The Federal Reserve agent is the chairman of the board of directors, and is appointed by the Federal Reserve Board and not by the banks, and he is the person at the bank through whom the Federal Reserve Board deals.

Mr. SPENCE. He, in a sense, represents the Federal Reserve Board in dealings with the Federal Reserve bank; is not that the philosophy of it?

Governor ECCLES. That is right.

Mr. SPENCE. And he saw that the Federal Reserve banks complied with the requirements of the Federal Reserve Board. How will those functions be performed now?

Governor ECCLES. Through the Governor and the chairman, who will be one and the same. Instead of having a dual organization, which creates cleavage and which is bad administration, it is proposed to combine the two offices. That is one proposal in the bill to which there has been practically no opposition from any source. The bill will save, in the operation of the Federal Reserve System, about $400,000 a year.

Mr. SPENCE. But the functions that were performed by the Federal Reserve agent are still being performed, but the Board will select the person to perform them?

Governor ECCLES. One of the principal functions of the agent was to hold the collateral as a sort of trustee against the notes which were issued. He was responsible at all times to see to it that these gold certificates and these Government bonds or commercial paper were deposited with him in sufficient amount to meet the legal requirements for the issue of notes.

Mr. SPENCE. Under the law, one Federal Reserve bank may rediscount—it says under the orders of the Board and regulations prescribed by the Board, may rediscount its paper in other Federal Reserve banks. To what extent has that been taken advantage of?

Mr. ECCLES. I could not tell you just to what extent. I understand, however, that in 1920 and 1921 there was some of that done, when the reserves of the Reserve banks got down to practically the legal limit and they were unable to extend further accommodations and, at the same time, have sufficient gold to meet the legal requirements for deposit and note-coverage. Do you remember to what extent that was, Dr. Goldenweiser?

Dr. GOLDENWEISER. In 1920, from memory, about $250,000,000.

Mr. ECCLES. How many banks were involved in the rediscount?

Dr. GOLDENWEISER. There were 11.

Mr. SPENCE. That provision, really, in effect, makes the Federal Reserve bank a central bank, does it not?

Governor ECCLES. It does so only to the extent of making the resources of the system available for the benefit of all the member banks, and that is all.

Mr. SPENCE. There is one other thing: I believe you said that you thought that some policy ought to be prescribed with reference to the administration of the bill, and you made a suggestion, or you suggested an amendment. Will you tell us what that amendment was, again?

Governor ECCLES. I suggested that I thought that fixing the price level as an objective would not be desirable, and as an alternative

I suggested that something like this might be better as a definition of objective:

It shall be the duty of the Federal Reserve Board to exercise such powers as it possesses to promote conditions making for business stability and to mitigate, by its influence, unstabilizing fluctuations in the general level of production, trade, prices, and employment, so far as may be possible within the scope of monetary action.

That is better, I feel.

Mr. WILLIAMS. That would be their duty even if you did not put it in there, would it not?

Governor ECCLES. The present law does not give them such a duty, at all. The present law only provides for——

Mr. WILLIAMS. Ought it not to be their duty?

Governor ECCLES. I do not know. The law has looked upon the Federal Reserve banks as agencies to provide credit for agriculture, commerce, and industry. The original act never contemplated the Federal Reserve bank as a monetary factor, as I understand it.

Mr. CROSS. May I interject right there, that the testimony of the members of the Reserve Board and some of the governors—they testified that it was not their duty and they did not consider they had anything to do with it.

Governor ECCLES. I think it was thought that, if credit was provided for commerce, agriculture, and industry, that is all that could be done toward creating business stability.

Mr. WILLIAMS. You think they made no effort along that line, at all?

Governor ECCLES. What is that?

Mr. WILLIAMS. You think they have paid no attention to the objective that you set out there, heretofore?

Governor ECCLES. I would not say that. Of course, the powers of the Board have been limited, their authority and their duties——

Mr. WILLIAMS. And they made no effort, at all, to stabilize business conditions and mitigate the evil effect of fluctuating prices and unemployment, and things of that kind?

Governor ECCLES. I have only been on the Board, as you know, for a very short time, and what the Board may have done is a matter of record, and it would appear in the record, from the condition of unemployment, the fluctuations of business activity, that whatever may have been done was a long way from creating stable conditions. Whether a condition of business stability can be brought about by monetary policy, only time can determine; and, as I stated the other day, monetary action has its limitations and has to be considered in connection with the tax program and Government expenditures.

Mr. WILLIAMS. I do not mean to be understood to be opposed to the suggestion you made here. I had had the impression that was their duty all right, and I still think, if it has not been their duty, we ought to make it their duty.

Governor ECCLES. I do not believe that under the existing law they are required to carry out or to perform that function.

The CHAIRMAN. Well, the fact is, is it not, Governor Eccles, that there was an attempt to incorporate specific directions of that type in the original Federal Reserve Act, and finally, it was left out of the bill.

Mr. FARLEY. Mr. Chairman, may I have an opportunity——

The CHAIRMAN. Mr. Spence, will you yield to Mr. Farley?

Mr. SPENCE. I just want to ask a question. Governor Eccles, do you consider that this bill, if passed, will be an attempt by the Congress to exercise its constitutional legislative function to regulate the value of money?

Mr. ECCLES. I should say that it would be a case of Congress delegating to a body that power and that responsibility, as defined in this statement that I just read. We often think of regulating the value of money as having reference to gold.

Mr. SPENCE. Well, as a corollary to that, that would be regulating the price levels, too, would it not?

Governor ECCLES. It would be an attempt to regulate the price level. If these instructions or requirements are prescribed for the Federal Reserve Board the price level will be one of the objectives, but not the only objective. Others will be stable production and employment.

Mr. SPENCE. Well, how far do you think you could go in obtaining some definite objective as to the regulation of price levels?

Governor ECCLES. The controlling of production and the fixation of prices can tend to create whatever price level is desired.

By the operation of the National Recovery Act and the Agricultural Adjustment Administration you can restrict production and bring about a rise in prices; but it seems to me that the thing that we are most interested in is to get a maximum of production in the country as a whole and a maximum of consumption. That is far more important than the price level.

In order to be able to get a maximum of production, it is necessary to get a proper distribution, and the question of price naturally has to enter into the problem. I do not know that I could add anything to what I said when Mr. Cross was examining me with reference to the problem of prices.

Mr. CROSS. May I ask a question?

Mr. SPENCE. Go right ahead.

Mr. CROSS. Governor, you said that three factors come in there: The question of price and production and employment. If you check the price level when the country was prosperous and when its indebtedness was created, much of it fixed by bonds and taxes, and the cheap dollar compared to the present dollar that existed—if you get a price level that is comparable to the price level then in that period, is not that the very thing upon which depends both production and employment? In other words, to get employment you have got to get the price to where the producer makes a profit—a probable profit, because not everybody makes a profit, of course, but under good management, he can make a profit, and when he can do that, he employs labor and in turn labor is given a purchasing power and the country can function as a result of that, and you get rid of your unemployment and you keep a stable product and you keep a stable price level on the standard you take of some prosperous year.

Governor ECCLES. You know, from 1923 up to about 1929, we had a fairly stable price level. Now, why was it that that stable price level became an unstable price level and we got into the depression we did?

Mr. CROSS. If you will let me answer that, if you put that as a question——

Governor ECCLES. I think maybe asking a question is the best way for me to answer it.

Mr. CROSS. I would say the Federal Reserve Board fell down in its duty, or fell down under the law as it existed—I could not say it was a duty. But in addition to that, we did not have then the securities act to control the wild speculative gambling that took place throughout the country on the stock exchanges. Now, we have controlled it largely through the laws enacted in the Seventy-second Congress.

Governor ECCLES. You assume that, if the volume of money in relation to total production is kept at a certain ratio, you would thereby maintain a uniform or fixed price.

Mr. CROSS. Not a fixed price of anything?

Governor ECCLES. No, I know; I mean a fixed index, uniform prices according to some index. And you overlook, it seems to me, the income velocity, which is an element as important in our economy as is the quantity of money. As I indicated the other day in reading the quotations from the Brookings Institution report on our capacity to consume, there must be a more equitable distribution of income than existed in 1928 and 1929, in order to keep up income velocity and to prevent production capacity getting all out of balance or relationship with consumer buying power.

Mr. FORD. In other words, Governor, if you have a national income of $100,000,000,000, but if it was confined to a small percentage of the people in the country, it would not accomplish the result of wide-spread purchasing power, would it?

Governor ECCLES. It would only so long as those receiving this income continued to spend or invest those funds, but you reach a point where——

Mr. FORD. A saturation point, in other words?

Governor ECCLES. They no longer invest.

Mr. FARLEY. Mr. Chairman, may I ask the Governor a few questions about the bill itself?

Mr. SPENCE. When I get through; yes.

The CHAIRMAN. When Mr. Spence gets through, I will recognize you immediately, Mr. Farley.

Mr. SPENCE. Governor, the maintenance of a stable dollar is something that is very greatly to be desired, is it not, because if the dollar would raise 10 percent in value and buying power, the wealth of the Nation would be raised that much. For instance, if there was $400,000,000,000 of wealth in the Nation and the dollar raised its buying power, or was increased 10 percent, that would reduce the money value of the wealth of the Nation $40,000,000,000, would it not?

Governor ECCLES. A stable price level is very desirable. If I knew of some way to maintain stable prices, and at the same time maximum production, naturally I would be very much in favor of pursuing that method. But prices are influenced by so many factors, crop failures, for instance, prices of imported goods as they are influenced by the variation in the exchanges—those are two factors that we may have very little or no control over, and they all enter into the price structure.

Mr. SPENCE. Now, in this bill we state a new policy, or new standards, or new criterions, or new objectives to be attained. The provision here in regard to the open-market committee says it shall set forth policies that, in the judgment of the committee, should be followed with respect to the open-market operation of the Federal Reserve bank. Now, if this is a delegation of constituted legislative power to regulate money, would it not be necessary for the Congress, in making that delegation to state some objective to be attained?

I have not gone into that, but I want to read a paragraph from a decision of the Supreme Court in *Panama Refining Company et al.* v. *Ryan et al.*—one of the "hot-oil" cases:

> The Constitution provides that "all legislative powers herein granted shall be vested in a Congress of the United States, which shall consist of a Senate and House of Representatives" (art. I, sec. 1). And the Congress is empowered "to make all laws which shall be necessary and proper to carry into execution" it general powers art. I, sec. 8, par. 18). The Congress manifestly is not permited to abdicate, or to transfer to others, the essential legislative functions with which it is thus vested. Undoubtedly legislation must often be adapted to complex conditions involving a host of details with which the national legislative cannot deal directly. The Constitution has never been regarded as denying to the Congress the necessary resources of flexibility and practicality, which will enable it to perform its function in laying down policies and establishing standards, while leaving to selected instrumentalities the making of subordinate rules within prescribed limits and the determination of facts to which the policy as declared by the legislature is to apply. Without capacity to give authorizations of that sort we should have the anomaly of a legislative power when in many circumstances calling for its exertion would be but a futility. But the constant recognition of the necessity and validity of such provisions, and the wide range of administrative authority which has been developed by means of them, cannot be allowed to obscure the limitations of the authority to delegate, if our constitutional system is to be maintained.

I have not gone into that question, but do you not think there ought to be some objective, definite objective placed in the law?

Governor ECCLES. You mean as to price?

Mr. SPENCE. As to price level, the purchasing power of the dollar?

Governor ECCLES. By purchasing power of the dollar you mean the price level?

Mr. SPENCE. The price level; yes.

Governor ECCLES. If the price level is placed in the law as an objective for the Board to reach as a result of monetary action, and the other factors are left out, we may get the result of having a stable price level and not getting any of the other factors which we want. I believe that the price level is less important than employment. I think the most important element, after all, is total production, because that is the real measure of wealth. I do not know what monetary policy could possibly be pursued to bring about a fixed price level and maintain it; I do not know how that would be possible.

Mr. SPENCE. Well, the price level does have a very great relation to the production, does it not?

Governor ECCLES. It may or may not. The thing that, after all, has relation to production is the buying power of the people of the country as a whole. When the national income is increasing faster than production, prices rise and production is stimulated thereby; and when the national income is diminishing, prices decline, and production is diminished thereby.

Therefore, it seems to me that the problem of the national income is a determining factor with reference to prices and production. So, rather than an arbitrary fixation of prices, if we could get an increase in the national income, we would get an increase in production and an increase in prices; and that is why in 1929, after we had had a period from 1923 to 1929 of stable prices—because we had had reasonably full employment during that period—and then our national income started to diminish and we got into a cyclical depression, prices went down and production went down.

Mr. SPENCE. Do you think the changing price level comes from conditions over which we have no control?

Governor ECCLES. Over which we do not have anything like complete control. We possibly can exercise some control through monetary action; but I do not think that we can exercise absolute control, unless we undertake to fix prices, by legislation, and attempt to regulate production accordingly. Even then, I doubt that we could maintain stability of the price structure as a whole.

Mr. SPENCE. The power given to the Congress, in the Constitution, to regulate the value of money is a power you do not think can be exercised?

Governor ECCLES. I do not think it can be exercised to the extent of maintaining a uniform price level, and at the same time keeping up maximum production.

Mr. SPENCE. Well, a good many of our ills have resulted from changing the value of the dollar and the fluctuating price level.

Governor ECCLES. Oh, yes; but the changing value, as I say, has been brought about primarily through the decrease in the national income, which was brought about through the inequitable distribution of income. That is where the trouble commenced very largely.

Mr. SPENCE. How far do you think legislation can go to stabilize the value of the dollar? Suppose we set the objective that we might not hit, but could we come anywhere near it?

Governor ECCLES. I do not know how. Certainly, interest rates could not be very much lower than they are now. The volume of money that is not in use is very great, and to increase it, it seems to me, would accomplish nothing toward either price raising or increasing business activity.

We have a potential increase of $20,000,000,000 in the supply of money. The excess reserves provide that. True, if Government spending were greatly increased, you would get an increase in the price level, because you would get an increase in the national income, and you would get an inflationary or reflationary effect as the result of that increased spending.

Mr. SPENCE. That would be an artificial condition?

Governor ECCLES. It would bring about the same result as an equal volume of spending by our people of their own funds, or their being willing to borrow and spend a like amount. That would inject into the circulation an increased amount of money and increase the velocity of money and raise the price level, and the buying power of the people would increase through that spending, and production would then have to increase to meet the increased buying power, and with the general increases, prices should tend upward.

Mr. CROSS. May I ask a question?

The CHAIRMAN. Mr. Farley is next.

Mr. SPENCE. There is one question more. I have gotten so many letters from State banks—there is a provision in the law that you can waive the capital requirements of the State banks and then give them such additional time to conform to the requirements as the Board may, by regulations, prescribe. A good many of them feel that they ought to know just how long they have to comply with these requirements, when they become members of the Federal Reserve System, with the ultimate purpose of remaining in.

Governor ECCLES. I suggested an amendment to that the other day that would give the Board the power not only to waive the capital requirements, but all other requirements, and also to permit banks to continue with less than $50,000 capital, if it is adequate in relation to their liabilities. So there would be no time limit if a bank with $25,000 capital did not need a greater capital in relation to its deposit liability.

Mr. SPENCE. Well, I suppose it works both ways.

Governor ECCLES. That was the suggested amendment to liberalize that section.

The CHAIRMAN. All right, Mr. Farley.

Mr. FARLEY. That is right in line, gentlemen, with what I had in mind. In section 202 you provide——

Governor ECCLES. Where?

Mr. FARLEY. Section 202, that the time in which this shall become effective is July 1, 1937. But why is there any objection to writing into the law 1940, for instance?

Governor ECCLES. That is not in the banking bill of 1935. As I understand it, that is in the banking act which was passed in 1933. Personally, I see no reason for an extension of time in lieu of the provisions that are being made, in order to make it possible to admit all the State nonmember banks which are insured. I believe that it would be in the interest of those banks and the System as a whole to be members of the Federal Reserve System, if this legislation broadening the eligibility features is passed.

Mr. FARLEY. I wanted to ask this, because in the State of Indiana we have, in round numbers, 420 banks, and only six now are in the Federal Reserve, and I have the fear that, if they are compelled to qualify by July 1, 1937, there will be many of them left out. Do you not think that, if the insurance feature is withdrawn from these banks, because they have not qualified, it is just the same as closing the banks?

Governor ECCLES. Why do you think they cannot qualify?

Mr. FARLEY. Well, they might be able to qualify in a little additional time, but if the rules governing the examination of these banks continue as rigid as they have been for some months past, they probably would not be able to qualify, because they have a lot of frozen assets yet.

Governor ECCLES. I am sure that, so far as the present Federal Reserve Board is concerned, they realize fully that situation, and it is their expectation to take into the System all, or practically all, banks which are insured. It is for that reason that we are proposing this amendment to the Federal Reserve Act.

It is true that, as a condition of admission to membership, the Federal Reserve Board has rather rigid regulations, which are not requirements of law. They require banks to charge off all paper that is classified as a loss, by the reserve examiners, and all depreciation on bonds except those in the four highest classifications. However, the Federal Reserve Board, under this provision, would be expected to give the same consideration to the bond accounts of these banks that is now given to the bond accounts of existing member banks both by the Reserve Board and by the Comptroller's office.

Mr. FARLEY. Well, the inference, then, is that you mean to undertake to liberalize them; and I do not mind saying that, from the impression I have of you and your public work, I should not be much afraid that would not be done.

Why object to writing it into the law and making it 1940? I have in mind a case where I tried, a year and a half ago, to get a bank into the Federal Reserve System, and they were declined, because they had something like $360,000 of what they counted doubtful paper. Now, even in these hard times, that bank has been able to reduce that now over $200,000, and collect——

Governor ECCLES. When was that, you say?

Mr. FARLEY. About a year and a half ago.

Governor ECCLES. With the guaranteeing of bank deposits by the Federal Deposit Insurance Corporation and with help from the Reconstruction Finance Corporation, with reference to capital structures, providing funds at 3½ percent for preferred stock, the banking problem is very different than it was. As a practical matter, it seems to me that the banks which are insured by the Deposit Insurance Corporation should be admitted to membership in the Reserve System. There would be no point in making requirements upon those banks which would exclude them from the Reserve System, and thus exclude them from the benefits of the Deposit Insurance Corporation, and possibly close them. That would be a foolhardy thing to do.

So long as the depositor is protected by the Federal Deposit Insurance, there should be an effort made to get all of the banks into the System, so as to have unification of the banking system and thus be able more effectively to carry out a monetary policy; and by that means, also, greatly to assist in dealing with deflation as well as inflation.

It is true that by far the greatest decline, both as to the percentages of deposits and as to total deposits, was in nonmember State banks, practically twice as great as it was in the member banks.

Mr. GOLDSBOROUGH. I did not catch that.

Governor ECCLES. I said the shrinkage in deposits of nonmember banks, the deflation in nonmembers banks from the peak of their highest deposits down to their lowest deposits—in other words, the deflation of nonmember State banks—was almost twice as great as the deflation in the deposits of member banks.

That was a very great hardship on the communities which those banks served, and the bank failures were far greater in the case of nonmember State banks than in the case of member banks, both State and national, and that of course——

Mr. GOLDSBOROUGH. I would like to inject that that was not the condition in the State of Maryland; it was the failure of the large member banks in the important cities which carried the reserves of the country banks which burst the nonmember country banks.

Governor ECCLES. I think there are exceptions all over the United States; but what I am speaking of is the United States as a whole. I am taking the entire country.

The CHAIRMAN. Somebody in the Senate, Governor Eccles, and I believe it was Senator Norbeck—I never ran it down like I should possibly have done—gave the figures, as I remember, for the year 1931, which show that the deposits, the casting up of accounts, showed that there were as many deposits tied up in the failed national banks as there were in the State banks; that I think the figures would show that, in 1931, there were more deposits tied up in failed national banks in the State of New York and in the State of Pennsylvania than there were in the State banks. I would not say that I could not be mistaken in those figures, because I am not an authority, but that is my recollection.

But let me ask you this question: What happened was that the failures first took place among the smaller banks; and of course that involved, at least in number, the State banks more than the national banks, and the nonmember banks probably more than the member banks; but when the fire spread from the back alleys and side streets to the mansion on the front and to the important centers, and began to involve the large banks, they were not helpless; they did not stand by and let the fire ruin them, but they came to Congress and had us open the Treasury of the United States to them.

So that it seems to me that an appraisal of that situation should be taken in the light of the fact that the processes were started by resort to the Federal Treasury, and never allowed to reach that end. So we do not know what the complete picture might have shown.

Mr. GOLDSBOROUGH. I think it ought to be stated here, as well as any other time, that another direct cause of the failure of the small banks was the fact that the large national member banks in the great centers, through the years immediately preceding 1929, unloaded securities on those banks, practically all of which securities afterward were shown to be sour.

Governor ECCLES. I have pointed out the effect of the bond acount when I was upholding the real-estate loan provision.

With reference to the chairman's remarks, I am not here making any odious comparisons between member and nonmember banks, for the purpose of putting the nonmember banks to any disadvantage. I am only trying to argue for the need of all banks to be members of the Reserve System and have available to them borrowing and rediscount facilities of that System, as well as of deposit insurance, so that we may avoid fires starting in the back alleys, et cetera; because, after all, the net result of the conflagration of the bank failures is finally to burn down the System, if it is not stopped; and in the process it is not only the bankers and the stockholders of the banks that we are directly or particularly interested in, but it seems to me we are interested in this problem as the duty of Congress and as the duty of officials who are responsible for our money situation.

Mr. GOLDSBOROUGH. Mr. Eccles, right there. Yesterday, I think, you stated that the stockholders in the Federal Reserve System receive 6 percent on their investments?

Governor ECCLES. That is right.

Mr. GOLDSBOROUGH. But the Federal Reserve System, in turn does not redeposit those funds in those little country banks; so that, in case of an investment which they make in the Federal Reserve System, they only get interest once; whereas on the ordinary investment, where they get a redeposit, they may lend the same money 10 times. Is not that the reason why they object to coming into the Federal Reserve System, because they do not get the benefit of the deposits which they can reloan?

Governor ECCLES. As I understand it, most State laws provide that State banks—whether members or nonmembers they are subject to State laws—are required to maintain reserves, either in money or in balances with other banks, or both, of a certain percentage of their deposits. Now, I know the requirement for State banks in two of the Western States that I am familiar with is 15 percent of demand deposits and 10 percent of time deposits, which must be carried in cash or with other banks.

Mr. GOLDSBOROUGH. Yes; but that does not answer my question. I do not know whether you want to direct your attention to my question, but what I asked was, whether or not, as a matter of fact, when one of these small country banks enters the Federal Reserve System and gets its 6 percent, that is all the interest it gets on that particular investment. The investment is not redeposited with them so they can loan it over again, as the ordinary investment is which they make.

For instance, if they loan me $5,000, they expect me to simply take a bank book from them, so they can reloan that same money.

Governor ECCLES. When you buy a Government bond, the proceeds are not reinvested, or when they buy other bonds that are marketable, we will say, or listed on the New York Exchange, or when they buy Canadian bonds or other bonds, those funds are not redeposited with them.

Mr. GOLDSBOROUGH. They are not redeposited with the country bank, but they are redeposited with some bank?

Governor ECCLES. That is correct.

Mr. GOLDSBOROUGH. But the small banks are not loaded up with Government bonds.

Governor ECCLES. Their percentage of Government bonds is pretty high; it is much higher than it was, because there was no other place——

Mr. GOLDSBOROUGH. When one of these national banks buys $100,000 worth of bonds, all the Government gets is an entry by some $25-a-week clerk to the effect that the Government has deposited or has a deposit in that bank of $100,000. That is what happens.

The CHAIRMAN. Just one moment, in connection with what has been said, I think it might be well to call attention to the situation: It means more to the small bank, the bank of small capital, to tie up 6 percent of its stock in the Federal Reserve bank than it does for the large institution to carry that burden, it would seem to me. The little banks, under the old order, were permitted to carry their reserves in a correspondent bank, upon which they were accustomed to draw interest, which was no little thing to small banks. That operated in this way: In the South, for instance, or in the West, the demand for credit is seasonal. When marketing time came and collections came in, the bank had a plan by which it could use its surplus funds, to put them to earning, by carrying them to the city bank; and that, in turn, gave them a large borrowing privilege during seasons when the demand for loans was accentuated. So that was an advantage that they enjoyed.

In addition to that, the small banks, members of the system, had to surrender their right to charge for the services rendered in remitting checks, and that is, of course, a big item to any small bank where the problem of overhead is great, and where the volume of business is small, and, of course, that requirement kept many banks from joining the Federal Reserve System. And those banks that were automatically taken into the Federal Reserve System—the national banks—conducted a war against the efforts of the Federal Reserve Board to take away such earnings, as long as they were able to carry on the fight. They finally lost through legislative action and processes that I will not take the time now to review, but which were not altogether justifiable, in my view of the matter.

You may resume, Mr. Spence.

Mr. SPENCE. I want to address——

Mr. FARLEY. There is one other question I want to ask, in connection with your statement of the wide difference between the assets of the nonmember banks and the member banks. Was that arrived at by the same committee's examination?

Governor ECCLES. I do not just understand your question.

Mr. FARLEY. You said, a few moments ago, that the nonmember banks had a much larger amount of worthless assets than the member banks. Did the same group examine the nonmember banks, or arrive at the same conclusion?

Governor ECCLES. You must have misunderstood me. I did not make a comparison between the assets of the member and nonmember banks.

Mr. FARLEY. Then I misunderstood you.

Mr. ECCLES. I made no comparison between the assets, because I am not familiar with the condition of the assets of the nonmember banks.

Mr. FARLEY. I thought you said that the losses were greater in the nonmember banks than in the member banks, or their portfolios were not so good.

Governor ECCLES. No; what I said was, that the shrinkage in deposits and the liquidation at nonmember banks was far greater than that at member banks; that the deposit deflation, as the result of bank closings and credit contraction in the nonmember banks——

Mr. FARLEY. I get the idea.

Governor ECCLES. Was about twice as great as that in the member banks, in proportion to the total deposits of each group of banks.

Mr. FARLEY. I have a letter in which the Indiana Bankers' Association makes this very emphatic statement:

> The Indiana Bankers' Association is unalterably opposed to central banking in any form, and especially to a central banking system in which credit granting and management will be vested in any political body.

That gets back to the question of control. You thought, the other day, there was no danger of anything of that kind happening.

Governor ECCLES. I see no reason to expect the Federal Reserve System, under this bill, to be any more subject to political control than has been the case in the past under existing legislation.

Mr. FARLEY. I remember your answer. There is another item I would like to get a little information on. I have read your speech at Columbus over several times, and it is a very excellent presentation of the subject.

I personally think you never can have a price level until you control all products of every kind and description, from the farmer to the market, or to the consumer. I do not ask you to say whether you do or not concur in that suggestion. But now, about this provision by which you are going out and loan on all types of real estate, making provision for the rediscount of those securities at the Federal Reserve bank, and then permit the Federal Reserve itself to issue currency against all securities. It seems to me that the wildest inflationist in the world could not have had a better term than that. When you take on anything and issue securities—and issue currency against those securities, it seems to me it is just like Germany did at the end of the war. Is there anything in that?

Governor ECCLES. I though I had answered that point. That question has been asked a number of times. I will try to answer it very briefly and cover the subject. Three phases of this legislation have a bearing on this matter: Changing eligibility requirements, permitting long-term real-estate loans, and eliminating collateral requirements for Federal Reserve notes.

In the first place, I think that you will probably agree that the amount of Federal Reserve notes that go into circulation has no relationship to the collateral requirements. I attempted this morning, and yesterday, and I think the day before yesterday, to explain why that is the case.

Mr. FARLEY. If that is already in the record, Governor, it is not necessary to repeat it.

Governor ECCLES. With reference to the question of eligibility, what we are proposing is to permit the banks, subject to rules and regulations by the Board, not only to discount eligible paper, but also to make advances to member banks on notes of the member banks, secured by any of their sound assets. That does not mean that the Reserve bank would have the power to discount a 20-year mortgage. What it does mean is this: That the Board could, by regulation, permit the Reserve banks to loan to member banks on bills payable of the member banks, for such——

Mr. GOLDSBOROUGH. A promissory note; that is what you mean?

Governor ECCLES. That is right, a promissory note, secured by bonds, mortgages, collateral loans, on a basis to be determined by each Reserve bank to be a sound basis for the loan.

Those loans would be made for periods of 90 days or 6 months, according to the regulations that the Reserve Board may make with reference to maturities. The member banks in the aggregate do not borrow for the purpose of reloaning. What is usually done is that the banks borrow to meet a shrinkage of deposits, the shifting of funds back and forth, which always happens seasonally under normal conditions, and it is usually seasonal borrowing.

If an emergency situation developed, the only way that the fire of deflation and bank closing can be stopped is by the banks being able to meet the demands of their depositors, and when they are able to do that, the depositors do not want their money. But when the depositors find banks are unable to meet the demands and banks start to close, it is a progressive condition of deflation that develops; and, therefore, this eligibility feature becomes effective.

By the way, I believe that the governors of the Federal Reserve banks and most of the member banks favor that requirement and recognize the advantage of it in protecting the banking system. The banking system, as a whole, would have to expand its credit by $20,000,000,000 before there would be any occasion to do any borrowing from the Reserve System, on the basis of present excess reserves.

The amount of real-estate loans to be made is not determined by the member bank's ability to borrow from the Federal Reserve bank, but by the percentage of time deposits, which, in itself, puts a limitation upon the expansion of real-estate loans.

I do not know that I answered your question——

Mr. FARLEY. Well, I have 2 or 3 other little questions I want to get a little light on. Does the practice still prevail of buying foreign bonds?

Governor ECCLES. I do not know to what extent. I would think, however, that if experience is any teacher, there would not be any great traffic today in foreign bonds. There are, however, certain foreign bonds, such as the Canadian issues, if that could be considered foreign, and Australian issues, and British bonds, and I think the bonds of Finland, and Poland, and Scandinavian bonds, which maintain their strength, their marketability, and have a very much better record than many domestic bonds of our cities, and counties, and States.

Generally speaking, foreign bond accounts of banks have been disastrous to them, particularly some of the South American issues and some of the European issues.

Mr. FARLEY. Would you care to state whether they need the Postal Savings System now, Governor?

Governor ECCLES. You mean is it a necessity?

Mr. FARLEY. Well, is it a good business proposition?

Governor ECCLES. For the Government?

Mr. FARLEY. Yes; for the Government?

Governor ECCLES. It is a good business proposition to the extent that they have been able to get money for 2 percent. I do not think that it is necessary for the Government for its own interests. I think the Postal Savings System has operated for the convenience and benefit and security of citizens who prefer to deposit up to $2,500 with the Government through the Postal System.

Mr. FARLEY. Well, would the guaranteed bank-deposit proposition——

Mr. ECCLES. It is less needed.

Mr. FARLEY. I think it is obsolete and ought to be put in the place where the interest that would be collected would be so low that nobody would even try it.

Governor ECCLES. I know that bankers, generally speaking, feel that there is a competitive relationship, and I think many of them would like to see the Postal Savings System eliminated, and feel that it is unnecessary in view of the Federal Deposit Insurance Corporation insuring $5,000 accounts. I do not believe it is very important, however, because the total funds in the Postal Savings System I think are somewhere around $1,000,000,000, and that is a comparatively small percentage of the total deposits of the banking system.

Mr. FARLEY. On page 69 of this act, in paragraph (g), we wrote into the law in 1933 that bank directors could not borrow from their own banks. Has any good purpose been served by that act? In other words, do you not think that it is time that we liberalized that?

Governor ECCLES. It is not bank directors, it is bank officers.

Mr. FARLEY. Well, bank officers.

Mr. ECCLES. Yes. I think it is a very constructive piece of legislation. There is not any question that, in principle, officers of a bank should not be in position to loan to themselves funds of the bank. It may be very difficult for an officer to be impartial in dealing with himself.

However, to the extent that officers of banks have loans in banks, which were made prior to the passage of the legislation, those loans should be treated, it seems to me, with due regard to the ability of the borrower to meet the obligations. There is a time limitation provided in the law, which I think is July 1935.

Mr. FARLEY. June 16, 1935.

Governor ECCLES. June 16, 1935, and, of course, there are many officers' loans in banks that it has been impossible, during this period of depression, shrinkage of values, and lack of market for securities to meet by June 16, and it is proposed in section 3 of this bill that that time be extended for 3 years.

Mr. FARLEY. Three years from June 16, 1935?

Governor ECCLES. Yes.

Mr. FARLEY. Now, would it not be infinitesimally better to prohibit bank officers from borrowing outside of their own bank, and thus compel an officer to do his borrowing from the bank with which he is connected, and if desirable and with the approval of the majority of the board, to the end that his board may be able at all times to know what he is doing, and also place some responsibility on the board. Is not there this danger, that to permit the executive officers to borrow outside of their own banks could prove very dangerous? There is nothing to prevent an officer from an inland bank to borrow excessively from a large and distant city bank, for which he may furnish proper security, but which might involve him beyond the point where his directors would consider it safe for him to go?

Governor ECCLES. There is in the law a provision that requires officers who borrow outside of their own banks to report those loans to the chairman of the board, or the president of the bank; and if it happens to be the president or chairman himself, he is required to report to the board of directors.

I feel that officers should be prohibited from borrowing from their own banks, and I feel that they should also be required, if they borrow outside, to report their borrowings, as now provided in the law.

Bank officers in the past have always been required to report their loans within their own bank to the board of directors, because it is the duty of the board of directors of a bank to approve all loans, and, therefore, officers' loans in their own banks have been reported to the boards of directors; but we have found that not only officers' loans but many loans to directors have, in instances, created real banking difficulties, and I cannot help but feel that, in view of the record of the past, the prohibition now imposed should be continued, with the extension of 3 years for those officers' loans which cannot be paid at the expiration of the period on June 16 of this year.

Mr. FARLEY. Have you already put in the record whether you think we have money enough in circulation or not?

Governor ECCLES. If I have not, I am willing to.

Mr. FARLEY. In your speech at Columbus, you stated there were $24,000,000,000 in circulation. Do you think it would be a good thing if we increased that circulation?

Governor ECCLES. How is it possible to increase it?

Mr. FARLEY. Why do we not use the authority we gave the executive department to issue $3,000,000,000, to take up some of these bonds bearing interest?

Governor ECCLES. How would that increase circulation?

Mr. FARLEY. Well, it would give these banks the actual cash instead of bonds.

Governor ECCLES. What would they do with the cash? They would immediately send it back to the Federal Reserve bank and it would be in the Reserve banks as their excess reserves, and actual circulation would not change. The banks would have, in lieu of Government bonds, $3,000,000,000 additional excess reserves.

Mr. FARLEY. I was in a bank not so long ago and the banker made this statement, and he said he wanted to sell $50,000 worth of bonds, and he could get immediate credit without any trouble if he called Chicago and New York, but he could not dispose of them. He wanted the money on the bonds he had in his safe——

Governor ECCLES. You mean Government bonds?

Mr. FARLEY. Yes.

Governor ECCLES. You mean he could not sell Government bonds?

Mr. FARLEY. That is the statement that he made—that is, without a little sacrifice at that time.

Governor ECCLES. He is misaken. He could have gone to the Federal Reserve bank and borrowed par on those bonds and possibly at a discount rate of 2 percent. If they were 3-percent bonds he would have gotton more than the interest on his loan. He could have borrowed the funds at par from the Reserve bank.

Mr. FARLEY. In your judgment, we do not need any more circulating medium right now?

Governor ECCLES. In my judgment, you cannot possibly force out and keep in circulation more currency than you have now. You may substitute——

Mr. CROSS. Right there, may I ask a question?

Governor, if that be true that this money would go right back—if that be true—and if you were to take the $3,000,000,000 that he refers to and buys bonds with it and you could not keep that money in circulation, it would go right back out of circulation?

Governor ECCLES. That is right.

Mr. CROSS. That is unquestionably true, is it?

Governor ECCLES. There is no question about it.

Mr. CROSS. Why not pay off all of the Government bonds and get rid of paying any interest—because that would be inflation itself?

Governor ECCLES. Here is what would happen: We have outstanding some twenty-odd billions of dollars and Mr. Cross asked the question, why do we not do that, and I think I should explain that such action would simply increase the reserves of the banking system by the amount of Government bonds which were purchased with currency. The currency would go out, if it was $10,000,000,000 or $20,000,000,000 or $3,000,000,000, whatever amount the Government paid out in currency to retire its bonds; but the currency would immediately go into the banks and from the banks into the Federal Reserve banks and be destroyed, and you would just have additional reserves, additional excess reserves.

The CHAIRMAN. Do you not think this bill rests upon the theory that it is necessary to control the excess reserves, because of the fact that it would have a bearing on the circulation?

Governor ECCLES. Yes. You get to the point of increasing the reserve requirements a sufficient amount to extinguish the excess reserves created by the amount of the Government bonds retired.

Mr. GOLDSBOROUGH. That is when the banks really begin to fight, is it not?

Governor ECCLES. Now, let me follow that point through and see what the situation would be. In the first place——

Mr. GOLDSBOROUGH. Can I just carry out the question so you can answer this too? Have we not actually given the banks over $13,000,000,000, and if we undertake to pay the bonds off in the way indicated by Mr. Cross we would simply be taking away from them what we have already given them?

Governor ECCLES. The thought is that you are giving the banks an interest payment that is unnecessary and is therefore a subsidy; and that, by the Government paying its bonds in currency and thus increasing the reserves of the banks by the amount of Government bonds retired, it would be necessary to increase the reserve requirements by that amount in order to extinguish the reserves; otherwise this operation could carry possibility of credit inflation to almost unknown heights.

The CHAIRMAN. You mean by that that the release of that currency would tend to bring about inflation, but there would be under this bill the power in the Board to control that tendency or defeat it?

Governor ECCLES. It would have to get started first. Of course, the $2,000,000,000 that we now have in the excess reserves should tend to do that, and it has not done it. But following out the extinguishing of these reserves, that would close thousands of banks for this reason: About 39 percent of the total loans and investments of banks is represented by Government bonds. Therefore, if the bonds, we will say, which are held by the banks are retired, it would mean that the reserve requirements would be increased by the amount of Government bonds that are retired. Some banks have only 10 percent, and that is particularly true of nonmember State banks; and, of course, if this only applied to the member banks, you would destroy the Reserve System, because they would all leave it and become nonmember State banks. That is one thing that it would do.

If all the banks were members of the Reserve System, and the principle of increasing the reserve requirements by the amount of total bonds that were retired through currency were put into effect, a bank that had 10 percent of its assets in Government bonds would be required to increase its reserve requirements, we will say, by 39 percent. That would mean that that bank would have to liquidate the difference between the 39 percent and its Government bonds, unless you simply would say to the bank that its reserve requirement increases only by the amount of the Government bonds taken up with currency; in that case the bank that had the largest amount of Government bonds would suffer the greatest loss of earning assets and would have the largest increase in reserve requirements. This would be thoroughly unworkable.

For the time being, it does not seem to me that is the alternative at all, because it would create a condition that would do anything but make for recovery. It would create a condition that would be terribly deflationary. It would put the banking system in the position that you do not want to put it in. After all, whether we like the system or not, we have it today; and to make a change of this sort would be so revolutionary that it would bring about, as I said, a condition of great deflation.

Mr. HOLLISTER. Would it not, incidentally, scare every sound business man to death?

Governor ECCLES. I say, without question, that it would bring about a condition that would be almost as bad as the bank holiday.

Mr. HOLLISTER. Which would be reflected immediately in decreasing employment, would it not?

Governor ECCLES. It would close up thousands of banks, because there is not any question that you cannot take away from the banking system 39 percent of its present investments, when we all know that they are not operating today very profitably——

Mr. CROSS. Governor, if that should happen——

Mr. HOLLISTER. Let him finish, please.

Governor ECCLES. We have not taken a most important feature into account, and that is the service which the bank renders. If a bank has to carry reserves equal to its demand deposits, why on earth would a bank take demand deposits and become the bookkeeper for the community funds, for every individual that carries an account, and act as a collection agency for the purpose of clearing and facilitating individual business transactions from all over the Nation, unless that institution made up by service charges, what it lost through having to carry increased reserves by the amount of Government bonds retired with currency? This would be anything but popular with the people of this country.

Mr. GOLDSBOROUGH. The service charge would be assumed by society, of course. The Government would assume the service charge?

Governor ECCLES. Of course, and that is exactly what is being done today through the Government paying this interest on its bonds. That means that the service charge is being assumed by society.

Mr. GOLDSBOROUGH. In other words, you agree that bonds—it is not necessary for the Government to issue bonds; in other words, to borrow money, it is just the same as the Government issuing a circulation medium, is it not?

Governor ECCLES. As a mechanical proposition, yes. But after all, we have established a method of financing, not only in this country, but in every other country—Russia is the only exception——

Mr. GOLDSBOROUGH. Well, we do not have to do things that are wrong simply because somebody else does it.

Governor Eccles. Whether it is wrong or not, is a question. I am pointing out what are the customs, what are the practices, and to make a change, as proposed, which is revolutionary, would destroy confidence and so delay and retard recovery that I do not think it is desirable, and I do not believe that there are any particular advantages or arguments for the retirement of Government bonds by the issuing of currency.

It may be interesting to see just what the Government is paying the banks. There have been some very exaggerated statements made with reference to this subject, and it has been claimed that the banks were getting as much as $1,000,000,000 a year subsidy in the form of bond interest.

Mr. Goldsborough. You are the only one that ever has called that by its true name, subsidy. We have never heard that before. You cannot find a metropolitan daily in the country that has the guts to call it a subsidy. You are the only one who has ever had nerve enough to call it by its right name.

Governor Eccles. Society, then, is paying the banking system for a service—and you admitted that it was necessary that society should pay for the service which the banking system renders the people and communities——

Mr. Goldsborough. Yes; but they should pay it directly and not by the banking system. That is the bunk, and if the public understood what the banking system was, if the public knew that the banks were allowed to loan the same money 10 times, they would not exist 24 hours, because Congress would be forced to change the law.

Governor Eccles. I do not know that the banking business has been the most desirable or profitable, even with all of the subsidies and privileges you claim it gets.

Mr. Goldsborough. Your reasoning is that, when deflation starts there is no way on earth to stop it?

Governor Eccles. I would not go that far.

Mr. Goldsborough. If you are on a 100-percent basis, you could not have deflation, because the money would always be in existence.

Governor Eccles. I think that, mechanically, inflation is far more easy to control than is deflation.

Mr. Goldsborough. You cannot control deflation under our system, and you cannot do it for this reason: That the creation of money amounts simply to the extension of credit, and whenever the banks start—when the banking system starts to collect its debts, it immediately decreases the circulation medium, it immediately causes a fall in all values, and it immediately causes the calling in of other debts. You just cannot stop it when you once start it under our system of fractional reserves.

Can I illustrate that in this way? In 1920 a very distinguished Member of this House, who is now on one of the boards down town, came to speak for me in my district. He said he had just had a talk with Mr. W. P. G. Harding, who was then Governor of the Federal Reserve Board. Cotton was then 30 cents a pound. He said Harding had told him they were going to bring the price of cotton down to 25 cents and stabilize it. I said, "My God! If you ever start that, you can't stop it." And cotton did not stop until it got down to 5 cents a pound. That is what happened.

Mr. FORD. Mr. Chairman, the Governor was going to read something that I am very much interested in——

The CHAIRMAN. Yes; we are all interested in that.

Governor ECCLES. I had a memorandum on this subject, because I had anticipated that that question might be discussed. With reference to the general opinion that banks are being paid $1,000,000,000 a year by the Government in interest, that is a greatly exaggerated statement. The total interest paid on the national debt during the calendar year 1934 was $817,000,000. Now, the banks, under the most generous estimate that you can figure, taking the bonds that they had, received about $260,000,000. And these are member banks. Figuring all banks, $320,000,000 is the maximum.

If the refunding operations of the Government continued until the holdings of the banks were converted into securities, bearing the current average yields, the interest received would fall to $180,000,000.

Now, it must be remembered that there are expenses in connection with the issuance of currency and keeping it in circulation; and it may be interesting to note that the cost of keeping the greenbacks and notes of the United States in circulation today is more per annum than the present rate that the Government is paying on its 180-day bills.

Mr. GOLDSBOROUGH. If they are entitled to some further consideration, do you not think it is a shame that we are refunding and giving them less interest?

Governor ECCLES. I am not arguing for consideration. I am pointing out the difficulties with no advantages of making the adjustments which you propose and which would be revolutionary, of the whole banking and monetary system, and I think, at this time, it would be disastrous.

Mr. HANCOCK. Will the cost of keeping the greenbacks out compare with the cost of issuing the 180-day bills?

Governor ECCLES. It is estimated here about fifteen-hundredths of 1 percent per annum on the greenbacks, and the 180-day bills were on the basis of eleven-hundredths of 1 percent, about one-tenth of 1 percent, which is less than the cost of keeping the greenbacks out.

Mr. HANCOCK. Where is the cost in keeping the greenbacks out?

Governor ECCLES. The destruction is rather rapid and they have to be reprinted, and the cost of shipping them out and shipping them back is something. Then there are insurance charges and express charges and there is personnel accounting, and other expenses.

Mr. HANCOCK. Does that same cost ratio apply to the Federal Reserve notes?

Governor ECCLES. I do not know what that cost ratio is. Do you, Doctor?

Mr. GOLDENWEISER. It is less than that, because of the fact that the denominations are large. In the Federal Reserve notes there are no $1 bills.

Mr. FARLEY. Mr. Chairman, I read into the record a while ago a rather emphatic protest from the State Bankers Association of Indiana, and just for the Governor's benefit I want to read just a little paragraph from the second largest national bank in the State of Indiana, and which, by your grace, survived all of the storms and is still a wonderful institution:

> We might say we have given the whole bill very careful consideration. In fact, we discussed it for nearly 2 hours in our directors' meeting yesterday, and we believe that the bill, on the whole, is pretty good and meets the present needs.

That is a national bank's attitude.

Governor ECCLES. I am interested, of course, to get that reaction, and I have found, whenever I have had an opportunity to sit down and meet the arguments and questions with reference to the legislation, invariably the bankers feel that this bill is not what it has been reported to be by many of our financial writers and economists. Most of the criticism directed at the bill could be directed toward the act that we have been operating under for the last 20 years.

The CHAIRMAN. Mr. Williams, did you say you have a question to ask?

Mr. WILLIAMS. Yes. Governor, in connection with the interest that is being paid by the Government to the banks—there has been a good deal said about the interest that has been paid on bonds in the national banks and Federal Reserve System, and keeping or using those same bonds as the basis for issuing and lending out money which they get on account of that issue, and getting interest on it. Of course, in other words, that would be double interest, interest on the bonds which they deposit, or which they sell for the purpose of securing the issue, and the currency which they lend out, so they would get double interest on it, would they not?

Governor ECCLES. You are speaking of national bank notes?

Mr. WILLIAMS. National and Federal Reserve notes.

Governor ECCLES. The Federal Reserve member banks, of course, do not deposit bonds and issue Federal Reserve notes, but the national banks have the privilege of issuing national bank notes, which right has now been eliminated.

Mr. WILLIAMS. Here is the question. How much, in number of bonds, is used as the basis of the currency issue?

Governor ECCLES. There is about $800,000,000 of national-bank notes outstanding. They are the only cases where the bonds are used by banks for the purpose of issuing currency.

Mr. WILLIAMS. What about the Federal Reserve bank notes?

Governor ECCLES. The Federal Reserve banks have paid off their liability on Federal Reserve bank notes.

Mr. WILLIAMS. That is right recently, is it not?

Governor ECCLES. Yes; recently. There was never more than about $150,000,000 issued, and that was issued right after the bank holiday; and those Federal Reserve bank notes were put out on the basis of sound assets other than Government bonds and other than gold.

Mr. WILLIAMS. Well, now, I see a statement that the Treasury proposes also to retire bonds upon which the national banks issue notes.

Governor ECCLES. That is right.

Mr. WILLIAMS. When that is done, that activity will be removed from the picture?

Governor ECCLES. That is right.

Mr. WILLIAMS. In other words, there will be no cost of Government interest upon its bonds?

Mr. ECCLES. There are greenbacks which, of course, have been out for a good many years, about $300,000,000——

Dr. GOLDENWEISER. $346,000,000.

Governor ECCLES. $346,000,000, with a certain amount of gold held back of those greenbacks.

Mr. WILLIAMS. And there is the argument that is being made by a great many people, that the Government has favored the banks by permitting them to deposit bonds——

Governor ECCLES. And issuing currency.

Mr. WILLIAMS. And issuing currency, receiving currency, and lending it out and securing interest on it, and at the same time securing interest on the bonds which they deposit for that purpose. Now, as I understand, that is a thing of the past?

Governor ECCLES. The Treasury last Monday announced that they were calling the 2-percent consols and 2-percent Panama's as of July 1, approximately $675,000,000 in total, and on July 1 the circulation privilege which was given to other Government bonds expires.

Mr. WILLIAMS. Have there been none of them used for the purpose of Federal Reserve note issue?

Governor ECCLES. No; not used by the Reserve banks. The Federal Reserve banks are required to deposit with the Federal Reserve agent gold equivalent to 40 percent of the notes outstanding, and the balance of 60 percent may be made up of eligible paper or Government bonds.

Mr. WILLIAMS. That is what I am getting at. Those bonds have been deposited, have they?

Governor ECCLES. Only by the Federal Reserve banks, from one department of the bank to another. In other words, the bank has been required to deposit with the Federal Reserve agent, who is the chairman, gold certificates and bonds, or gold certificates, bonds, and eligible paper.

We are proposing to eliminate the collateral requirement for the Federal Reserve notes; because it serves no purpose, it only adds additional expense, and has no relationship to the amount of currency in circulation, and is not required in any other central bank that has been recently set up anywhere in the world.

Mr. WILLIAMS. In other words, you propose to abolish the principle that has heretofore been followed of issuing currency based upon Government bonds?

Governor ECCLES. Yes.

Mr. SPENCE. Have all of the banks that had that privilege that availed themselves of it been national banks?

Governor ECCLES. Yes; no other banks had that privilege.

The CHAIRMAN. They are using about $150,000,000 extended under the relief act and——

Dr. GOLDENWEISER. That was in the Home Loan Act of 1932.

Mr. SPENCE. What proportion of them have not availed themselves of the privilege? Have you any figures on that subject, Governor?

Governor ECCLES. Mr. Smead could get that. What percentage of the national banks have not availed themselves of that privilege?

Mr. SMEAD. Of the 5,422 reporting licensed national banks on June 30, 1934, there were 4,600 banks issuing circulating notes, and 822 banks which did not exercise the circulation privilege.

The CHAIRMAN. Well, there will be no more notes issued by the national banks, based upon Government bonds?

Governor ECCLES. That is right.

Mr. CROSS. Governor, I want to go back to where we were awhile ago, when I asked you about the $3,000,000,000. As I understood your first statement, it was that if you were to take that $3,000,000,000 and buy bonds with it, call it in or buy that much bonds, it would not cause any inflation to come back; but, as a secondary proposition, there would be inflation through the banks, because they would have more business; is that correct?

Governor ECCLES. There would be a possibility of inflation through the banks, by reason of the increased reserves from——

Mr. CROSS. The $3,000,000,000?

Governor ECCLES. You have a potential inflation, but you would have to use the existing $2,000,000,000 of excess reserves before the $3,000,000,000 would have any effect.

Mr. CROSS. Now, we realize one thing, and this is what is disturbing me: As I get your attitude, we cannot get a measure of value—that is, we cannot make the dollar the measure of value, and I do not know why the atmosphere seems to be so surcharged with the idea of expanding the currency. Everybody is talking about inflation, yet we have inflation until we are as flat as a flounder in the mud.

Now, we certainly cannot come back until we reflate, and I should say that, if we started reflating, we can get back to the normal situation; that we are helpless, or we must go ahead and start on a wild spree of inflation until we explode and plunge back and down into the mud again.

Governor ECCLES. I do not think that is necessary.

Mr. CROSS. That is what I am contending, that it is not necessary. My idea is that, with the levers you have, you ought to be able to agree on a price level that would give you a measure of value in dollars, but if we have these things recurring and are helpless, that is a tremendous indictment of our intelligence.

My idea is that we should certainly be able to get a measure of value. In other words, just to illustrate the proposition, that A borrows from B a certain amount of money, and the present price of the dollar, we will say, is money covering one particle of all of the things that are necessary to feed and clothe and supply the comforts and luxuries of life. Now, the next year, when he wishes to pay it off, because there is no value in the dollar, he has got to pay back two particles of that commodity that will buy the necessities and comforts of life, and it appears to me it is just as much within the law robbing the poor devil as if I had loaned you $100 and I met you on the street next year, when it was due, and took out a 6-shooter and said, "Give me that $200 you have in your pocket", because I am taking it from you, and it will supply me with twice the things that the $100 I let you have would supply me with. In other words, if $1 will take care of me all of my life, I do not need but $1.

Governor ECCLES. Yes; what you say is true, that it is an injustice for a debtor to have to pay back debts in goods and services that have substantially less value when he pays his loan than it had when he received it.

Assuming that a dollar a bushel is fixed for the price of wheat, and the total wheat production at $1 is 400,000,000 bushels, are the farmers, as a whole, any better off than they would be with 800,000,000 bushels of wheat selling at 75 cents a bushel? In one case the income from the wheat would probably be $600,000,000 and in the other case it would be $400,000,000.

Mr. CROSS. I do not think you can take any one commodity.

Governor ECCLES. The point I am making is, it is production we are interested in. No one can pay his debts in terms of the price level. Higher prices do not help a business that only has one-half of the volume of business with which to pay its debts. You need to maintain not only the price level but also production.

Mr. CROSS. I understand. You said that a number of times; but do you think it is possible to get a measure of value or have the dollar come to where it would be the true measure of value?

Governor ECCLES. I do not think that is possible.

Mr. CROSS. Then we are helpless.

Governor ECCLES. No; I do not think we are helpless.

Mr. SPENCE. The Federal Reserve can exercise their power to regulate the rate of interest paid by banks to depositors on time deposits and savings deposits?

Governor ECCLES. That is right.

Mr. SPENCE. I think that is a very beneficial thing, because they have been the victims of competition or of the depression. Now, there is no authority in any national agency to regulate the rates paid by State banks, is there, at this time?

Governor ECCLES. Nonmember?

Mr. SPENCE. Yes.

Governor ECCLES. There is no authority, unless the Federal Deposit Insurance Corporation has it.

Mr. SPENCE. I do not think the Federal Deposit Insurance Corporation ought to have that power.

Governor ECCLES. That is taken care of in the Banking Act of 1935.

Mr. SPENCE. I think that would be welcomed by the banks, because they are the victims of their own competition.

Governor ECCLES. It is absolutely essential that member banks should not be subject to competition of nonmember banks by a limitation of the maximum interest that the member banks can pay and have the nonmember banks benefited and protected by the Deposit Insurance, and at the same time permitted to pay any rate of interest, whether it is a sound rate or not, that they wish to pay.

Mr. SPENCE. It would be very much better, if they could all do that and——

Governor ECCLES. The Banking Act of 1935 provides for that in section 323 (c), page 67, lines 1 to 7.

Mr. SPENCE. Have they exercised that power?

Governor ECCLES. The act has not been passed.

Mr. SPENCE. This act, you mean?

Governor ECCLES. Yes.

Mr. FORD. Let me make an observation there. The banks are fixing the amount of interest that they can pay for deposits, are they not?

Governor ECCLES. We fix the maximum only. There are a great many cases where they pay much less.

Mr. FORD. Would there not be a good deal—there is no attempt made to fix the maximum interest they might charge when they loan that money?

Governor ECCLES. Most States have usury laws.

Mr. FORD. I understand, but they are pretty liberal. We make the price, we will say, to the miller, of wheat at $1 a bushel, but he can charge $10 a barrel for the flour, if he can get it, and that is a competitive matter and I do not think can be fixed. You could not say any maximum rate of interest that the bank would charge, because it was getting money from its depositors at 2 percent, because the demand for that money and the volume of it would determine what rate it would get?

Governor ECCLES. It will bring the rates down, and it is bringing the rates down.

Mr. FORD. But it is a fixed thing, is it not?

Governor ECCLES. Fixing the maximum rate of interest on deposits tends to bring down the rate on loans. That is the effect.

Mr. WILLIAMS. Governor, in order that we might have this clear, did I understand you to say that there is in the proposed law a provision which authorizes the Insurance Corporation to fix rates that could be paid by any member bank?

Governor ECCLES. Requires them to fix the rate? It is fixed by the Reserve Board for the member banks.

Mr. WILLIAMS. Where is that?

Governor ECCLES. Pages 66 and 67. We have not gone into that, because that is in title III of the bill. That is in title III.

Mr. FORD. What page?

Governor ECCLES. Pages 66 and 67.

Mr. WILLIAMS. Does that apply to the nonmember banks?

Governor ECCLES. Yes, that is what it does apply to.

The CHAIRMAN. The purpose of that is to prevent one bank inside of the Federal Deposit Insurance Corporation fighting against another bank?

Governor ECCLES. That is right.

The CHAIRMAN. And taking an undue advantage of it?

Governor ECCLES. That is right.

The CHAIRMAN. Gentlemen, may we not quit until 3 o'clock? I think we had better adjourn until 3 o'clock.

(Thereupon, a recess was taken in the hearing until 3 p. m.)

AFTERNOON SESSION

The CHAIRMAN. Governor Eccles, I believe Mr. Ford desires to make some inquiries.

Mr. FORD. Governor, I am not going to take you into the back-alley finance in my statement. I am just simply going to say, in a very short statement, that it is my reasoned conviction that the present bill, while not perfect as to all of its details, and undoubtedly requiring some minor technical amendments, seeks, on the whole, to accomplish the following desirable results:

First, by broadening the eligibility requirements of the Federal Reserve bank discounts, to uncover a great reservoir of potential credit, which will be made available. Is that true?

Governor ECCLES. There is ample credit today, but, without change in the eligibility features, there will be great hesitancy on the part of the banks to loan on other than short-term commercial paper or Government bonds.

Mr. FORD. All right. We will change that to make it "available so far as the borrower is concerned."

Governor ECCLES. It makes it available, not because they need to borrow funds to do it, but it makes it available because they would be willing to loan existing funds, if they could get borrowers, on longer time loans, that, otherwise, they would feel unsafe in making.

Mr. FORD. My second point is that, by placing in the hands of the Federal Reserve Board the authority to initiate open-market operations, we give them the power to regulate in a material degree or to stabilize in a material degree business operations. Would it do that?

Governor ECCLES. The three powers of monetary control—open market, discount rate, and reserve requirements—put into the hands of the Federal Reserve Board a power to control inflation. And they also put into their hands the power to prevent deflation, so far as can be done by the creation of excess reserves and by the reduction of interest rates.

There is no action that the Board itself can take that will induce people to borrow, induce corporations to borrow, the excess funds which the banks may have as a result of the Board's action in creating excess funds.

Mr. FORD. But it is an effective check on the impulse for inflation, on the one hand, and credit deflation, on the other hand, is it not?

Governor ECCLES. I think so. I think the eligibility changes and the control over the supply of money would certainly tend toward a prevention of deflation.

Mr. FORD. In addition to that, in the third place, does it not add two other desirable things: By broadening the eligibility requirements of the Federal Reserve Board, each member bank with sound but long-term paper could, under emergency conditions, take this paper to the Federal Reserve bank and get currency and thus better serve the needs of its community or meet a sudden emergency? Would that be a clear statement?

Governor ECCLES. The Reserve banks will have the power to loan to member banks on sound assets, which would enable the member banks to meet the demands of their depositors.

Mr. FORD. Certainly.

Governor ECCLES. Which otherwise they might be able to meet only by forcing a contraction of credit or by selling securities; or it might be that they would be unable to meet the demand and thus be forced to close.

Mr. FORD. Now, if I understood you correctly when you were making your various statements, you said that the Federal Reserve banks today had at least $10,000,000,000 that seeks profitable investment.

Governor ECCLES. No, sir. I said that the commercial banks had $10,000,000,000 of time deposits.

Mr. FORD. I mean the member banks of the banking system had excess funds.

Governor ECCLES. No. The banking system has excess funds seeking investment of over $2,000,000,000.

Mr. FORD. What was that 10-billion-dollar figure that you used:

Governor ECCLES. I said that the time funds or saving funds held by the commercial banks amounted to more than $10,000,000,000.

Mr. FORD. But that would be seeking profitable investment, would it not?

Governor ECCLES. A good deal of those funds are loaned already in various types of loans. A great deal of those funds are no doubt invested in Government bonds and other securities and bonds guaranteed by the Government. The excess reserves of the banks, which are in excess of $2,000,000,000, are sufficient in amount to enable the banking system as a whole to extend new loans or to purchase additional bonds to the extent of more than $20,000,000,000 without the banking system as a whole being required to borrow from the Federal Reserve System.

The banking system creates money through its loans and investments. A bank making a loan of $1,000 to a customer creates $1,000 of deposits. However, for every $1,000 increase in the deposits of the bank the excess reserve decreases by 10 percent of the amount of that deposit increase, so that a loan of $1,000 increases the assets of the bank by $1,000 and the liabilities, in the form of deposits, by a thousand, and the reserve requirement by $100, approximately. You see, this increase in deposits would increase reserve requirements by 10 percent of that amount.

Therefore, 2 billion dollars of reserves in the System as a whole are a sufficient amount to enable the banks, on the basis of 10 for 1, to extend credit to the extent of 20 billion dollars, without having to go to the Reserve banks and discount or borrow money.

Excess reserve can be increased or decreased by open-market operations or by a change of reserve requirements? That is where you get your monetary control.

Mr. FORD. Now, then, at the present time we have a potential credit reservoir of about 20 billion dollars.

Governor ECCLES. That is right.

Mr. FORD. If paper eligible for rediscount came along, the banks would be free to make those loans, wouldn't they, knowing that they could take that paper, in an emergency, to the Federal Reserve banks, if they got into trouble?

Governor ECCLES. They would be. It would be very profitable to make those loans if they were available.

Mr. FORD. In comparison with the 2⅞ percent to the banks on long-term Government bonds, you are holding out an inducement to the banks, through this bill, to exercise their functions as banks and make every possible loan that they can——

Governor ECCLES (interposing). With safety.

Mr. FORD. I did not mean that they should go out and go crazy. But, when people come in wanting money, they would be in a position to loan it to them.

That is a thing that has always bothered me. I do not know whether I have got the explanation of it or not.

Now, I note that since 1922 the volume of commercial paper in the United States—the normal commercial paper, under the old law, the 90-day paper, has been greatly diminished. Now, my understanding or my belief is that the reason for that diminution in that commercial paper was that many corporations, both large and small, instead of going, as they used to do, to their banks and getting their short-term requirements, have found that, through the investment bankers, they could issue securities and get that money all in a lump. And in many cases much of that money, after they had gotten it, did not go to their own bank, but went to New York, to be used for other loans, for speculation. Is not that true?

Governor ECCLES. Partly. It seems to me that the transition that has taken place in our business and banking systems during the life of the Federal Reserve System has been that our business system has become more concentrated, into larger and larger units; and that there is today a greater concentration of corporate operations in the country, in fewer companies, than we have ever had before. The trend is in that direction, as evidenced by the chain-store development and the developments in almost every field of manufacturing activity.

Mr. FORD. Steel and all others.

Governor ECCLES. We see a drift toward consolidation and mergers, making for bigness and a greater concentration of control.

That has tended to concentrate commercial deposits to a greater extent than formerly in the centers where the headquarters of the various companies are located; and it has also, in cases where there has been borrowing, largely concentrated all borrowing, at very low rates, on the commercial-paper basis, in the money market; so that the average small bank, or the banks in the towns of 10,000 people or even 25,000 people, and less, have not had the demand, and have not had even during the period of our great activity, in the twenties, the commercial loans to their local business concerns that they had prior to the developments to which I have referred.

It is true that many of the consolidations and mergers were brought about through flotations of securities, bonds, and stocks, and the effect of those flotations was that the banks that formerly carried commercial loans and short-term loans for the carrying on of business transactions, furnished the money through the purchase of bonds, or through loaning to customers, who purchased bonds or stock. So that there was a substitution, to, no doubt, quite an extent, of bonds and collateral loans in banks; whereas, formerly, particularly before the war, commercial paper was used to a far greater extent.

And, of course, in the case of farmer financing, that has been taken away from the local banks to quite an extent through the Production Credit Corporation. The Production Credit Corporations, which are a part of the Farm Credit Administration, get most of their funds by the sale of 6-month and 9-month debentures, outside of their capital, which has been furnished to them by the Government.

These debentures are sold in the market and the present rate is somewhere on the basis of 1½ percent per annum. The big banks, in the centers, with the surplus funds, are the purchasers, largely, of these debentures, thus providing the funds to the Production Credit Corporation, and the Production Credit Corporation supplies the funds to the farmers, through the local communities. So, it means that the banks in the centers, through the Production Credit Corporation, are financing agricultural production; and that, of course, takes away from the banks in the agricultural areas the eligible agricultural paper.

Mr. FORD. I note that in 1929 the commercial paper; that is, the commercial loans made by banks, were only $4,396,000,000, and that was at the peak of our so-called "prosperity", and that in 1934 that sum had dropped to $2,144,000,000; so that there has been a gradual diminution or gradual disappearance of commercial paper as a source of business to these banks, and there is very little likelihood of any substantial increase in that.

Governor ECCLES. For the reason that, if you will examine the statements of most of our business concerns, it will be found that they have an excessive working capital. One of the difficulties today is that they are the owners of huge pools of deposit money now in the banking system, which they are not using and are not able to utilize; so that, even with an improvement of business the most that could be expected from many of our business concerns would be that they would put into use the funds that they now have, and under no circumstance would they be required to borrow.

Now, I am speaking of our business concerns in very general terms. In number there may be, and no doubt are, a great many business concerns that would be required to borrow; but, measured in the volume of the business which they do, which, of course, is the important element, there would be a small percentage.

Mr. FORD. Well now, that being the case, if the reason for the existence of our banks is continued, then we have got to afford them some additional opportunity, where their funds can be employed; and it seems to me that the long-term real-estate loan is about the only outlet that appears on the horizon at the present time to any great volume.

Is that an admissible statement?

Governor ECCLES. There is no prohibition now against banks making collateral loans which are not eligible; and there is no prohibition against banks buying long-term bonds. So long, then, as there is no prohibition now against the banks investing depositors' money in those fields, which are likely, in the event of depression, to be just as frozen as real-estate loans, there should be some liberalization with reference to the power of the member banks to make long-term real-estate loans. To what extent that will be utilized by borrowers it is impossible to say.

Mr. FORD. Oh, I realize that. But we all know, if we read our correspondence, and I know from my particular experience, that it is almost impossible, or it has been up to quite recently, to get a real-estate loan from any bank. Now, the reason the banks gave for that was that that was an unliquid paper, and if they put their money in there it would stay there, and they would have no way of getting it out if they had a call.

Governor ECCLES. They had been made to feel that a real-estate loan is a slow and an undesirable asset to have. And inasmuch as the banks have most of the loanable funds, and mortgage companies and the savings and loan associations, as a whole, have very little, and in most of the communities have no funds to loan, but are in the process of reducing and bringing pressure to bear, it would seem that the situation would be helped and relieved by permitting and encouraging the banks to make long-term, sound, real-estate loans.

Mr. FORD. Not with the idea, Governor Eccles, of making the loan today and taking it to the bank tomorrow and getting a discount, getting the money and coming back to make another loan; but with the idea of making a loan that was a profitable loan—and in our country the rate is 7 percent, which is quite different from 2⅞ percent—they could put that money into that market. Then, should there be a sudden demand on them for more money, they could always take those securities to the Federal Reserve bank and get the money for them, could they not, under this law?

Governor ECCLES. The Federal Reserve banks would have the power legally to loan to member banks on the notes of the member banks, secured by mortgages or other collateral, with such margin as they thought was advisable to make the loan sound. Certainly member banks would not loan money on mortgages and then borrow from the Reserve banks so long as the member banks had excess funds to loan. It could be expected that the member banks would be willing to pay interest on borrowed money from the Federal Reserve banks only when a condition was reached by any member bank that made it necessary for it to borrow to meet its shrinking deposits.

It has never been a policy of the Federal Reserve System to permit its member banks to borrow continuously or to borrow for the purpose of reloaning because there was a profit between the discount rate at the Reserve banks and the loaning rate of the member banks.

Mr. FORD. They were only there for the purpose of the bank getting the money when it actually had to have it and for a proper purpose?

Governor ECCLES. To meet the current demand.

Mr. FORD. Now, Governor Eccles, there is just one other observation I want to make.

There seems to be some apprehension in the minds of some of my correspondents as to this bill being an inflationary measure. We have had that out here before, but I just want to make an observation on it. We discussed this morning the question of fixing a price level.

Now, my conception of the possibilities lying dormant in this bill, and which can be developed if it is passed, for credit, is this: It will make available—and when I say available I do not mean that it does not now exist—but it will make it a little easier and more attractive for the banks to go into the business of loaning money, for the purpose of bringing our production up to a maximum. If we could do that we would bring our unemployment down to a minimum. The result would be a large pool of money poured out over the country and that would give purchasing power to the consumers of the country generally, and that would tend not only to stabilize business but to bring a gradual increase in the price level, up to some point where there might be an attempt made to peg it, within certain limits. Would not that be one of the ways of doing it?

Governor ECCLES. I do not know that I understand what you mean when you say, "Would not that be one of the ways of doing it"? Do you mean the bill as now drawn?

Mr. FORD. I am talking about bringing our production up to a maximum.

At every meeting that this committee has had there have been people who said, "Now, industry cannot get money; and, when industry cannot get money, it cannot produce; and the reason it cannot get money is that the banks are afraid to loan."

Now, the loaning of money of real estate might conceivably have a tremendous influence on industry, because it would put men to work. Now, if you could create conditions so that money could be easily gotten by industry, with a prospect of getting it back and getting a profit, that would immediately create a wage pool, and it would give an increase of income to the country and, with the increase of income to the country—and the wide-spread of the purchasing power that goes to the men that do the work is one of the factors—it would naturally put purchasing power in the country, and, with an increased demand for goods, the price level of all goods would come up, would it not?

Governor ECCLES. Yes.

Mr. FORD. And if there was a tendency on the part of prices to go up wildly, could not the Reserve Board, under this bill, put an appreciable brake or check on that?

Governor ECCLES. Yes; a general increase means an inflation; and that can be, in my opinion, controlled through the powers that this bill provides to be given to the Federal Reserve Board.

Mr. FORD. Well now, taking the questions that I have asked and the picture that I have painted, I ask if this bill tends to make that possible? Do you think it does?

Governor ECCLES. I do.

Mr. FORD. All right. That is why I say in the beginning, that I believe this is the measure that the country needs and that I am going to feel very comfortable in supporting this bill in the House.

The CHAIRMAN. All right.

Does anybody else on this side have any questions?

Mr. CLARK. It will take only a minute for my questions, Mr. Chairman.

I do not think that Mr. Cross, Governor, is very much satisfied with our helplessness in this situation.

In the amendment that you have proposed three objectives are tentatively stated: First, stable business conditions; second, full employment; and, third, a more or less stable price level.

I believe that you stated that, if this bill were passed, it would give the Federal Reserve Board a control over the volume of money. That is right, is it not?

Governor ECCLES. I think it gives the Board a control of the volume of money on the up side. It does not give it such a complete control of the volume of money on the down side.

Mr. CLARK. No; but it tends to give the Board a more nearly complete control of the volume of money than it has had heretofore.

Governor ECCLES. Oh, yes; through monetary control plus the eligibility features.

Mr. CLARK. But you stated, however, that in order to achieve these desirable results—stable business conditions, full employment, and a more or less stable price level—that in addition to the control of the volume of money, there would necessarily have to be more control of the velocity of money—by the velocity of money meaning the ratio between the volume and the national income.

That is right, is it not?

Governor ECCLES. That is right.

Mr. CLARK. And you stated—I believe this is of fair inference from your testimony—that monetary action alone could control only remotely the velocity of the money; that is, by making the money available?

Governor ECCLES. That is, to the extent that low interest rates and abundant supply will induce its use; only to that extent.

Mr. CLARK. Then that is where Mr. Cross, I believe, stopped; that is to say, that is where the matter was let drop. However, I believe that, earlier in your testimony, you stated that there were two other factors which, if added to the control of the volume of money, might tend, in your opinion, to have a control over the velocity of money, namely, a tax system and a program of Government spending. Am I correct in that?

Governor ECCLES. Those are the other two elements which, it seems to me, in our capitalistic economy, must be taken into account to bring about a sufficiently equitable distribution of the national income, to keep up a full employment, full production, and keep the productive facilities adjusted in relationship to the buying power of the Nation.

Mr. CLARK. Yes; that is right. In other words, we have got, in your opinion, a three-legged stool; and this bill is one leg of the stool.

Governor ECCLES. That is right.

Mr. CLARK. This bill is designed to give control over the volume of money.

Governor ECCLES. That is right.

Mr. CLARK. Now, in order to make our stool stand up and in order to get out of that helpless condition in which Mr. Cross assumed we are—as we are—it is desirable, in your judgment, not only to pass a bill of this kind, or something of this kind, in order to build up this leg, but we should do more. Let us take the second leg of the stool—and I do not want to lead you astray, Governor Eccles, but it ties in. We are going to try to get somewhere and we want to get to a stable basis. Mr. Cross thinks it is an indictment of the human intelligence if we do not get somewhere, and I agree with him.

You say we need a tax system, and by that, I assume, you mean regulation of income taxes to the extent that when times are getting better and the price level is increasing and the full employment is reached the income taxes would be raised, as, I believe, you said they should have been raised in 1928, instead of having been lowered. So that is the second leg of the stool.

And then your third leg is a fixed national policy of Government spending, which would be controllable as conditions fluctuated.

By using those three things: first, monetary control, as proposed by this bill; secondly, shifting the income-tax rates; and, thirdly, increasing and diminishing the Government expenditures, not as an emergency proposition only, but as a fixed national policy; those factors would tend, in your opinion, to achieve this desirable state of stable business conditions, full employment, and reasonably stable prices, within limits.

Does that state it thoroughly?

Governor ECCLES. You have stated the case, I think, very completely.

Capitalism, sooner or later, has got to pay whatever it may cost, through the tax bill, to provide employment for people who are employable, and to provide an adequate, decent living for those who are unemployable, when the private employer fails to give employment on a sufficient scale to utilize our available labor.

That is the cost that we have to pay for capitalism; and the sooner we begin to recognize it when unemployment develops, the less the cost will be.

We have never questioned the duty of the Government to protect its citizens, no matter what the cost, against the encroachment of a foreign enemy. We have no more reason to question the obligation of the Government to protect the citizens, through insuring them employment, when private capitalism fails to insure that.

Mr. FORD. That is it.

Mr. CLARK. I think that is all. I really wanted to get that picture, because this is the first step along those lines.

Mr. SISSON. By Government spending, Governor Eccles, the third leg of the stool of which Mr. Clark spoke, am I right in assuming that what you mean is what might be called and what has been termed a long-range or long-term plan of public works, to be carried on when employment shows signs of becoming slack; and that kind of public work or that kind of Government spending to be carried on largely——

Governor ECCLES (interposing). To keep up the national income.

Mr. SISSON. Yes; and such as will least come into competition with private industry, with private business.

Governor ECCLES. I believe that, under capitalism, Government cannot compete with private business without the socialization of whatever field of private business it undertakes to compete in; and that Government spending should be in the fields of socially beneficial, public, noncompetitive activities, either directly or through grants to cities, counties, and States, for use in the same field.

I have no brief to offer against Government entering those fields which may be better handled in the public interest if owned and operated by the Government than if operated privately. But I do believe that when the Government steps in beyond the exercise of its regulatory powers, as a competitor, the natural effect is that all investment in that field, all private investment, stops; and that the field then must be absorbed and monopolized, sooner or later, by the Government.

Does that answer your question?

Mr. SISSON. Yes.

Mr. HANCOCK. Governor Eccles, is there any way of intelligently estimating what percent of short-time paper is usually renewed?

Governor ECCLES. You mean commercial or business paper held by the banks?

Mr. HANCOCK. Yes.

Governor ECCLES. I think it would be practically impossible to do that.

The loan is paid in one bank out of the proceeds of a loan gotten in another bank. That is the way commercial paper is usually handled.

We will take, for instance, a concern is borrowing $10,000,000 on 90-day commercial paper. A number of banks buy that paper and, at the expiration of the 90-day period, the loans are paid. You will find that the borrower on that paper has possibly only reduced the amount outstanding, or may even have increased it, by borrowing, by offering paper in the market, and another group of banks, or the same banks, will purchase their 90-day bills, just as the Government now does in its short-time financing. It is offering 182-day bills; and the purchasers of that paper have short-time paper; but it is only paid by a refunding operation for 182 days, or for two hundred-and-some-odd days by selling new bills—maybe not to the same institutions, but in the market.

Mr. HANCOCK. Well, the reason that is permitted, and the bankers up to now have been seeking short-term paper, has been due to the fact that, if it ran beyond a certain period, it would not be eligible for rediscount.

Governor ECCLES. Under the law, it would not be eligible except as 90-day commercial paper or 9-month agricultural or livestock paper.

Mr. HANCOCK. But, under this bill, there is no time limit with respect to the eligible paper?

Governor ECCLES. You mean there is no time limit as to maturity of the paper that is used to secure advances?

Mr. HANCOCK. Yes.

Governor ECCLES. No; there is no time limit.

Mr. HANCOCK. That would be left to the rules and regulations of the Federal Reserve Board or to the rules and regulations of the individual Federal Reserve banks?

Governor ECCLES. It would be left to the rules and regulations of the Reserve Board, yes, sir; as to the terms upon which advances could be made by Reserve banks to members on sound assets.

Mr. HANCOCK. Governor, there is no limit to the maturity of the paper that could be discounted, is there, under the bill?

Governor ECCLES. What?

Mr. HANCOCK. There is no limit as to the maturity paper which could be rediscounted, is there?

Governor ECCLES. Except as the Board may make rules and regulations.

Mr. HANCOCK. I mean under the proposed law.

Governor ECCLES. No.

Mr. HANCOCK. Is it not a fact, Governor Eccles, that the banks have usually made most of their profits and earnings on so-called "slow paper"?

Governor ECCLES. I think that, without question, the greatest part of the banks' income would be on paper that is not eligible, because over 80 percent of all the paper of the banks, even in 1929, was not eligible.

Mr. HANCOCK. Now, Governor, just one or two other questions.

This morning, you made a comparison as to the cost, between keeping greenbacks out and the cost on 182-day paper. With respect to the 182-daybills, is there any actual money passed in that transaction? Is it not just a sheer bookkeeping transaction? Is it not as I asked just a matter of bookkeeping? No real money is passed or put out.

Governor ECCLES. That is true of any loan, any loan a bank makes. It is a bookkeeping entry, and the money does not pass until the borrower wants to draw it out in currency or check against it; and the check has the same effect as currency. The money is passed then as the account is checked against or as currency is drawn out and used. And the same is true with the Government borrowing. The banks take the bills or bonds and they credit the account of the Treasury and they debit the assets account of their loans and investments; and the Treasury draws against those funds as and when it desires to, just like any other depositor.

Mr. HANCOCK. How much money does the Government carry on deposit with the banks today?

Governor ECCLES. I do not know exactly. I would say around a billion and a half.

Mr. HANCOCK. And what interest do they receive on those deposits?

Governor ECCLES. They do not receive any.

Mr. HANCOCK. No interest return whatever?

Governor ECCLES. No, sir.

Mr. HANCOCK. Of course, the banks that carry those large deposits would naturally buy this short-term paper at a very low rate of interest. Its really the Government's money they are lending to the owner.

Governor ECCLES. The deposits that they have are of absolutely no value to them, because they carry those deposits to the Federal Reserve at no interest. So there is really a loss in the handling of them under the present circumstances.

As a matter of fact the Government deposits of a billion and a half, upon which the banks pay no interest to the Government, and which the banks must secure by Government bonds, are not profitable for the banks at this time when they have large excess reserves.

Taking the banking system as a whole, it carries with the Federal Reserve banks more deposits in excess of what is required than the Government carries with the banks. Therefore, the entire Government deposits could be moved to the Reserve banks; and thereby the excess reserves of the member banks would be reduced from something over $2,000,000,000—whatever it is today—by the amount of the transfer of those Government funds. For that reason, so long as the banks have excess reserves larger than their Government deposits, the Government deposits are of no value; there is no profit to the banks.

Mr. HANCOCK. Governor, let me get this straight in my mind. Did I understand you to say this morning that the policy of this administration and the Government from now on would be not to issue any more currency against Government bonds?

Governor ECCLES. I have no way of knowing what the future policy may be. All I know is that the action which was taken by the Treasury to call, as of July 1, the bonds which were used to secure circulation, means that it eliminates from the national banks the right to issue national bank notes. Now, unless legislation is passed which again permits the national banks to issue currency against bonds which they deposit with the Treasury, that privilege will not exist.

Mr. HANCOCK. I may be misinformed about it; but I was under the impression that, under the present act, the President had the right to extend the time within which that process could be carried on; and that he had recently extended that time for another 2-year period.

Governor ECCLES. No. It may be that you are referring to the extension of the right of the Federal Reserve banks to issue Federal Reserve notes, secured by Government bonds, in lieu of commercial paper.

Mr. HANCOCK. I was probably confused about that. That right still exists?

Governor ECCLES. That was extended a short time ago.

Mr. HANCOCK. Were any other bonds originally issued to the national banks to support their circulation other than the Consols and Panamas?

Governor ECCLES. All of the bonds yielding 3⅜ percent or less. That right expires some time in July, and it cannot be extended without legislation, which means that any currency of the national banks that has been issued on a basis of the 3⅜-percent bonds, or bonds yielding a lesser amount, will have to be taken up.

Mr. HANCOCK. Well, I am glad to get that information from you, because I had wondered, in my own mind, why the Treasury was calling in the 2-percent Consols and 2-percent Panamas while leaving out the 3⅜-percent bonds if the purpose was to lighten the interest burden on the people.

Governor ECCLES. They are not calling in the bonds, but the bonds lose their circulation privilege, which was conferred upon them for 3 years——

Mr. HANCOCK (interposing). The circulating privilege?

Governor ECCLES. The circulation privilege, which will make it necessary for the banks which have used that circulation privilege to pay to the Treasury the amount of money representing the notes which they have used.

Mr. WOLCOTT. Governor Eccles, I have a very few questions to ask. I think all the questions that I had have been quite fully covered, with the exception of one or two.

There has been a feeling on the part of many economists that there should be very little affiliation between the currency of the country and the national debt. I presume that they have in mind that if we are called upon to manipulate the currency as our national debt increases or decreases, that that tends to an unstable currency.

In reading this bill I can see some affiliation between the action of the Federal Reserve Board and the national debt, inasmuch as they have the right, in the open-market operations, to help the Government in maintaining its credit, by at least retiring that part of the national debt which matures within the current year. Do you think that is rather a dangerous practice?

Governor ECCLES. It seems to me that the Government spends only those funds which the Congress appropriates. The Congress that has the power to appropriate money also has the power to create a means of providing that money, if it is not done through the existing banking system. Therefore, I do not feel that to make it impossible for the Government to finance the appropriations which Congress makes is necessarily going to defer what the Government spends, but it is likely to jeopardize the existing banking and credit structure. For that reason, it is desirable and necessary that there should be a relationship existing between the banking system and the Government in the interest, it seems to me, of the preservation of the existing banking system.

Mr. WOLCOTT. And would you say, also, the maintenance of the national credit by the use of the banking system of the country?

Governor ECCLES. The national credit is not dependent upon the willingness of the banks to supply it.

Mr. WOLCOTT. Now, in that connection, I assume that those open-market operations—that the Federal Reserve Board can, by adopting a policy which I understand to be mandatory in its operations upon the member banks, compel the member banks to invest in Government securities, so that, if we came to a time when, as I understand now, a great deal of our Government indebtedness is in the form of short-term paper?

Governor ECCLES. About $13,000,000,000.

Mr. WOLCOTT. About half of our national debt is in the form of short-term paper?

Governor ECCLES. Under 5 years.

Mr. WOLCOTT. And there was an endeavor on the part of the banks to unload that for the purpose of making more remunerative investments in industry, then, the Federal Reserve Board, through its open-market committee, could control that situation. So I see a direct relationship between the national debt and the possible amount of currency which is in circulation and the volume of currency which is in circulation.

Governor ECCLES. Do you mean by currency, deposit money as well?

Mr. WOLCOTT. I think we can confine it to Federal Reserve notes, because, if I understand this bill, together with the policy of the administration, our trend is toward a single currency.

Governor ECCLES. Yes; but I think there is absolutely no relationship between the Government debt and the amount of Federal Reserve notes in circulation. There may be absolutely no Government debt, and there still may be, and likely would be, the same amount of currency in circulation. There is no relationship between the two.

And it was interesting to note, in looking over some charts of other countries, where the debts have greatly increased—in Japan, particularly, I noticed the amount of its currency did not vary 5 percent. And the same thing would show here, that, as a matter of fact, our debt has increased during the last 2 years, and the amount of currency outstanding has come down as the debt has gone up.

Mr. WOLCOTT. Surely it has not increased in proportion to the debt?

Governor ECCLES. It has decreased.

Mr. WOLCOTT. When the debt was about $20,000,000,000, we had $4,250,000,000 of currency, or something like that, and at the present time we have $5,600,000,000.

Governor ECCLES. Something like $5,500,000,000 in currency at the present time.

Mr. WOLCOTT. When you say that it has decreased——

Governor ECCLES (interposing). Decreased in comparison with what it was 2 years ago.

Mr. WOLCOTT. It has increased about $1,000,000,000 in the last 4 years. It has not increased in the last 2 years, but in the last 4 years.

Governor ECCLES. Yes, I think that is right; and that is due to two causes largely: One is the decreased use of checking accounts, due to the service charges and check tax, and also due to reduced incomes of people, which caused many of them to carry currency instead of using the checking account. There has also been a reduction in the number of small banks throughout the country, and thus there are many small communities which formerly supported banks and which today do not and cannot possibly support banks, thus requiring the use of currency in those communities. I think that is largely responsible for the increased use of currency. There is also some hoarding, I suppose, but I do not know how much of a factor that is now.

Mr. WOLCOTT. In other words, instead of a man who owed several people an aggregate of $100, drawing as many checks as he has debtors, he would either draw one check or go to the bank and draw it out in cash, and, for that reason, there has been more demand for cash.

Governor ECCLES. That is right. There have been less checks and more currency in circulation.

Mr. WOLCOTT. So that you claim there is no relativity between the amount of the national debt and the amount of currency in circulation?

Governor ECCLES. That is right.

Mr. WOLCOTT. Getting back to the question which was asked a few minutes ago, about the use of some of this gold profit to retire these Consols, upon which the national banks based their circulation, I assume from that and from this bill that it is the policy of the Government to eventually create a situation where we have a single currency, which will be whatever silver is needed for change and the Federal Reserve bank notes.

Governor ECCLES. This action will reduce the currency to the silver certificates which, from all present indications, may be a permanent part of our currency, and the greenbacks, which are $346,000,000. Outside of those two currencies, the Federal Reserve notes will be the only other currency in use; and, of course, the Federal Reserve currency will represent the great percentage of the currency in use.

Mr. WOLCOTT. So that the Congress, in the adoption of that policy, by passing this bill, would further contribute to the criticism of the Congress as having delegated its authority to coin money. I am not criticizing that policy. I am merely asking for the information. If there has been criticism of our having delegated heretofore to the Federal Reserve banks the prerogative of Congress to regulate the currency, there is a likelihood of a further criticism of our having centered the control of the volume of money in the Federal Reserve System, is there not?

Governor ECCLES. Reaction of Congress in taking away from the national banks this right to create money does not seem to me that it should subject Congress to criticism. It has not deprived the Congress of any of its power to regulate money.

Mr. WOLCOTT. Well, it surely cannot be considered as a recapture of any of the prerogatives of Congress, which they have under the Constitution, to issue currency, can it?

Governor ECCLES. I do not think that it either takes away from or gives to the Congress any powers.

Mr. WOLCOTT. Well, I listened with a great deal of interest to a radio address by Father Coughlin, whom you have no doubt heard.

Governor ECCLES. I have not. I have never heard Father Coughlin. I have heard of him a plenty.

Mr. WOLCOTT. I will not attempt to quote him exactly, of course, but, in the course of his discussion, which was, I believe, the night that it was announced that $642,000,000 of the gold profits would be used for the purpose of retiring these consols, he at least expressed some pleasure at the fact that, at last, the administration was using some part of this fund as a base for the issuance of currency. Now, if I understand that operation correctly, we merely retired national bank currency and substituted therefor Federal Reserve notes. Is that right?

Governor ECCLES. That is right. The calling of the consols, $675,000,000, by the use of the gold profit, resulted in reducing the national debt out of the profits that were created through devaluation, to the extent of $675,000,000.

Mr. GOLDSBOROUGH. It was a deflationary gesture, too, wasn't it?

Governor ECCLES. The national-bank notes outstanding, which were secured by the consols which were called, were naturally retired.

Mr. WOLCOTT. Well, then, by retiring the consols, the Panama consols and these other consols—and there is another consol. What is the other?

Governor ECCLES. The Panamas and the consols.

Mr. WOLCOTT. By reason of having retired those consols, of course, it is necessary to retire a like amount of the currency that was started by those consols.

Governor ECCLES. That is right.

Mr. WOLCOTT. So that, unless we issued Federal Reserve notes to replace them, the volume of money we have outstanding will be $642,000,000 less, provided that was the money out against the consols?

Governor ECCLES. That is right.

Mr. WOLCOTT. So that, instead of being inflationary, instead of using any part of the gold profit for the purpose of increasing the amount of money outstanding, it takes out of circulation the national-bank currency in that amount?

Governor ECCLES. No. There is no difference in the amount of money. Federal Reserve notes will be substituted for the national-bank currency; and it will be done unconsciously, because people holding national-bank notes will use them in the course of business, just the same as they would use Federal Reserve notes or silver certificates. There is no distinction made in the use of the currency. Now, as the national-bank notes become mutilated, the banks will send in the currency, as it comes in through the deposit windows and is sorted—and, as the old notes are sent in to the Reserve banks, new Federal Reserve notes will be sent to the member banks in place of those notes, to meet the demands of the customers. The Federal Reserve banks will send in these mutilated national-bank notes to the Treasury and the Treasury will destroy them; whereas, in the past, they would issue new notes, keeping up the flow.

Now, the national-bank notes will just gradually pass out of existence as they become mutilated and, as they pass out of existence, Federal Reserve notes will take their place. It might take a year before the whole process is worked out.

Mr. WOLCOTT. It was on that that I predicated my previous question concerning the concentration of the circulating medium in the—or the regulation of the volume of the currency in the Federal Reserve System, taking from the national banks the money outstanding against these consols, and the Federal Reserve System issuing in place Federal Reserve notes.

Governor ECCLES. That is right.

Mr. WOLCOTT. There are two provisions in the bill on which I have had a great deal of correspondence. I do not know whether you are acquainted with one of them, Governor; that is, the provision with respect to the examination of private banks. Now, in the bill which we passed in 1933, we provided that within 1 year after the operation of the act all private banks which were not inspected by a State examiner, must, in order to continue to receive deposits, submit to examination by either a Federal Reserve examiner or a national-bank examiner. They had their choice as to which they would elect to be examined by.

Now, I notice that in this bill the law is to be amended somewhat; and I wondered what the reason for that was. It is amended in subsection (b) of section 303, page 52 of the bill. It is an amendment to paragraph 2 of subsection (a) of section 21 of the Banking Act of 1933 and it provides that:

> The expense of the examinations required hereunder shall be assessed against and paid by, the institution subject to examination in the manner and with the same effect as provided by section 5240 of the Revised Statutes, as amended.

What would you say was the purpose of that?

Governor ECCLES. That is under title III of the bill; and there are, of course, a good many phases that the Federal Reserve are interested in under title III, that have not come up or been discussed here. It was my understanding that the discussion at this time would be confined to title II of the bill.

Mr. WOLCOTT. Well, this directly affects the Federal Reserve System.

Governor ECCLES. Well, there are quite a number of——

Mr. WOLCOTT (interposing). I do not quite understand it. I am not very well acquainted with this and it is something that you might not be acquainted with, because it is a matter of detail, and these are a few isolated cases.

Governor ECCLES. Title III is composed largely of the legislation that was in the omnibus banking bill of the last Congress. There are some additions and some modifications and the particular section referred to is a section that is recommended by the Comptroller of the Currency. Under title III there are, I think, some 32 provisions. Thirteen of the provisions, of the total of 32, are provisions that the Federal Reserve System recommended and was interested in. The other sections were proposed by the Comptroller of the Currency and the Federal Deposit Insurance Corporation. They are largely of a technical nature.

Mr. WOLCOTT. Then, you are not in a position, as coming from the Federal Reserve Board, to say what the purpose of those was?

Governor ECCLES. No; I am not; because that was developed by the Comptroller of the Currency.

Mr. WOLCOTT. Would that be true also of the prohibition against bank officers and executives borrowing from their banks?

Governor ECCLES. That prohibition is already in the existing law.

Mr. WOLCOTT. But, there is a change. I have introduced a bill, at the suggestion of the Treasury, and Senator Copeland introduced the bill. It was suggested that I introduce it in the House; and I understand that they have used the language of it here in this bill. I wanted to ask some questions on that. This bill gives bank officers and executives 2 years in which to retire their investments.

Governor ECCLES. Three more years in which to retire loans made before the enactment of the Banking Act of 1933.

Mr. WOLCOTT. I wondered if any thought had been given to placing a limit upon the amount that they could borrow after that or at the present time.

Governor ECCLES. There was no consideration given to that by the officials of the administration who considered that particular legislation. And the Federal Reserve Board and, also, the Office of the Comptroller of the Currency have felt, as I stated here this morning, that bank officers should be prohibited from borrowing from their own institutions; and that, in cases where they have loans, they should be given an extension of 3 years.

Mr. WOLCOTT. I was interested in the matter only to the extent that several have written me about it; and it seems to me that the prohibition would work an injustice in small cities, where there is only one bank. And they think that they should be permitted to make emergency loans, up to $1,000 or $1,500, or something like that. I am not particularly interested in the section, but I am inquiring.

Governor ECCLES. We are not recommending that bank officers be permitted to borrow from their own banks under any circumstances; and it is my personal view that it would be a mistake to permit bank officials to borrow under any conditions from their own institutions.

Mr. WOLCOTT. I appreciate the purposes of this legislation. Yesterday, I think, Congressman Gifford was questioning you, and you remarked that the British national debt is only 7 percent of the national income.

Governor ECCLES. That the servicing, the interest, on the British debt is a little over 5 percent of the national income.

Mr. WOLCOTT. And that the interest on the United States national debt is about 1 percent of the national income.

Governor ECCLES. That is right.

Mr. WOLCOTT. In arriving at that conclusion did you take into consideration the internal, municipal debt of the United States?

Governor ECCLES. No; only the national debt. I think I have the figures on the other debt in my mind. The British municipal debt is, of course, much smaller in proportion than the American debt.

Mr. WOLCOTT. They have a more centralized government?

Governor ECCLES. That is right. I think that the total public debt of Great Britain, so far as the figures are available—and it is difficult to get very accurate figures—is about $48,000,000,000. That, of course, is figuring the pound on the old parity basis of $4.85, and the American debt—in considering the Federal debt, as I said yesterday, the question of what we deduct from it by way of assets which are held in the form of loans that are made by the Reconstruction Finance Corporation, or other loans that are made by other Government agencies, should be given consideration.

Mr. WOLCOTT. After those deductions were made, I believe you said it was about $25,000,000,000?

Governor ECCLES. I said it was less than $25,000,000,000, without deducting the gold profit, which now makes up the stabilization fund—say, $22,000,000,000. I think the municipal debt would be around $17,000,000,000 to $18,000,000,000.

Mr. WOLCOTT. So that our total public debt would be in the neighborhood of $40,000,000,000?

Governor ECCLES. That is right, as against the British debt of about $40,000,000,000, whereas our national income——

Mr. WOLCOTT (interposing). Governor, for my purposes, probably we can shorten this up by saying that the public debt of the United States, based upon your previous statement, is something less than 2 percent of the national income?

Governor ECCLES. No. The public debt of the United States, in total, would be about 50 percent of the annual national income—the normal national income.

Mr. WOLCOTT. I should not have said that. I should say the carrying charges—the interest—for the total public debt.

Governor ECCLES. The ratio between interest on the public debt and national income depends, of course, upon what income you figure—whether you figure on the present income or whether you figure on what you term a normal national income.

Mr. CROSS. What is a normal national income?

Mr. WOLCOTT. Based on the normal national income.

Governor ECCLES. It would be less than 2 percent of the normal national income. Our normal national income, if we can figure 1927, 1928, and 1929 as normal, was about $83,000,000,000.

Mr. WOLCOTT. Do you know what the normal national income of Great Britain has been?

Governor ECCLES. Last year it was about $18,000,000,000, and $20,000,000,000 is about as high as it has been.

Mr. WOLCOTT. Does public debt, in the sense that you are using it, include the debts of municipalities, counties, towns, and villages?

Governor ECCLES. That is right. It is between $17,000,000,000 and $18,000,000,000, in addition to the Federal public debt, making a total of around, say, $46,000,000,000 of public debt.

Mr. SISSON. Do you use the term "national debt" in the same sense?

Governor ECCLES. No.

Mr. WOLCOTT. No. At least I am distinguishing between the national debt of the United States Government itself and the internal public debt of the States, counties, cities, townships, and so forth.

And that public debt, other than the national debt, is between $17,000,000,000 and $18,000,000,000; and the national debt of the United States Government, according to the testimony, is, in round figures, $22,000,000,000.

Governor ECCLES. The national debt, as I stated, depends on what you deduct by way of the gold profit and the assets.

Mr. SISSON. The guaranteed obligations of the Home Owners' Loan Corporation was not included in the national debt?

Governor ECCLES. No.

Mr. SISSON. They are not a direct part of the debt, are they?

Governor ECCLES. No. I am not including those as a direct part of the debt.

Mr. CROSS. When you said a little less than 2 percent, you meant that the national debt, plus the other debts of the municipalities, and so forth, required a little less than 2 percent to service the interest charges?

Governor ECCLES. Yes.

Mr. CROSS. Do you include in public debts, national debts, municipal, State, and other local governmental debts?

Governor ECCLES. The questions of Congressman Wolcott called for making a comparison between the total public debt, which included the State, county, and city debts, plus the Federal debt, as between the United States and Great Britain.

Mr. CROSS. Yes; I understand that; but I wanted to get it stated in the record so that those statements would show clearly that when you said public debt you meant by that the public debts, Federal, State, county, municipal, and so forth.

Governor ECCLES. That is right.

Mr. WOLCOTT. Then, inasmuch as we have not taken into consideration the contingent debt of Great Britain, but have taken into consideration the contingent debt of the United States Government, our total national debt at the present time, without making these deductions, is $31,000,000,000, and our State, county, and municipal debts are $17,000,000,000. That would make a gross public debt of $48,000,000,000, would it not?

Governor ECCLES. That is right.

Mr. WOLCOTT. Or within $1,000,000,000 or $2,000,000,000 of the total British debt?

Governor ECCLES. I think the gross national debt now is $27,000,000,000 plus. It is not $31,000,000,000. It would be $45,000,000,000, if we included State and municipal debts without deducting the balances on hand or the advances which will be repaid, or the gold profits.

Mr. FORD. Governor, do the obligations include any of the obligations of the Reconstruction Finance Corporation?

Governor ECCLES. Yes; that is included.

Mr. FORD. That includes their obligations?

Governor ECCLES. Yes.

Mr. FORD. And from that should be deducted their assets?

Governor ECCLES. Most of the increase in the Government debt is not due to spending but to lending. For instance, $1,000,000,000 of the increase in the Government debt went to the purchase of preferred stock and debentures of the banks and $800,000,000 have gone to the receivers of closed banks as loans against their assets, in order to hasten their liquidation. There are other loans which have gone to the insurance companies, the railroad companies, the mortgage companies, and so forth. In fact, the entire Reconstruction Finance Corporation operation is a huge credit-expending operation, and the amounts will largely be recoverable.

Mr. SISSON. Are you taking into consideration at all the matter which Mr. Ford referred to? I would assume that what be meant by the assets of the Reconstruction Finance Corporation was the repayments. You cannot tell exactly what those repayments are going to be.

Governor ECCLES. That is right.

Mr. SISSON. You are not deducting, then, from the national debt the probable repayments, are you?

Governor ECCLES. Not in figuring the $27,000,000,000. There was no deduction. That was the total outstanding debt; and, from that you would have to deduct the balances on hand, which were over $1,500,000,000, as well as all of these assets; and, of course, there are also the commodity credit loans that have been made, running up to $600,000,000 or $700,000,000. There is also, as I say, the $2,000,000,000 in the stabilization fund. That is not taken into account.

Mr. SISSON. In this comparison which was made between the national debt of this country and the national debt of Great Britain, did your figures contain any comparison which would show what the debt of this country is per capita, as compared with the British debt per capita and what our income is per capita as compared with the British income per capita?

Governor ECCLES. I do not recall just what those figures are. Of course, it would be a very easy matter to get those figures.

Mr. SISSON. I remember reading them, getting them from other sources; but I thought that, before basing any conclusions on those figures, we ought to have them authoritatively. I know that our debt is very much less in proportion than the British debt and that our debt is very much less per capita than the British debt.

Governor ECCLES. Oh, yes. If the committee is willing, I think it may be well, in this connection, and I would like to insert in the record a coordinated, connected statement covering this comparison.

The CHAIRMAN. There is no objection to that. We shall be glad to have it.

STATEMENT BY GOVERNOR ECCLES ON THE PUBLIC DEBTS OF THE UNITED STATES AND THE UNITED KINGDOM

The kind of comparison most frequently made between public debts of two countries is in terms of debt per capita. The most recent authoritative figures of this kind were prepared by the Treasury for the Joint Committee on Internal Revenue Taxation. For national debt per capita—that is, the debt of the central government alone—the figures originating from that source are $850 for the United Kingdom and $215 for the United States. The debt per capita for all public bodies, including central governments, counties, municipalities, school districts, etc., is $991 in the United Kingdom and $370 in the United States, or about two and a half times as much in the United Kingdom as in the United States. Only very tentative estimates can be made of the national income in the two countries for the year 1934, but such information as we possess indicates that the national income in the United Kingdom was about $430 per capita as against $400 per capita in the United States. In all these comparisons the rate used to convert the British into the American monetary unit is $5 to the pound.

Because of the very difficult questions connected with selecting the proper rate of exchange between two currencies in making comparisons of this kind, and because the income of a country is more important than its population in considering questions as to the burden of its public debts, per capita figures of the kind just given may be misleading. For this reason the figures below on the relation of interest on public debt, public debt, and national income are presented. National income as used here means the total money incomes actually paid to all the inhabitants of a country.

Net central government debt, after deduction of Treasury balances, stabilization funds and other assets, is 38 percent of national income in the United States and 158 percent in the United Kingdom, or about four times as much of the national income in the United Kingdom as in the United States.

The debt of all public bodies—that is, the net central government debt plus the debts of all other civil divisions—is 74 percent of national income in the United States and 194 percent in the United Kingdom, or about two and one-half times as much of the national income in the United Kingdom as in the United States. In round numbers, the net debt of all public bodies in the United States is $37,000,000,000. If it was as large in relation to our national income as the British public debt, it would be $97,000,000,000.

Interest on the central government debt is 1.6 percent of the national income in the United States and 5.4 percent in the United Kingdom. Interest on the debt of all public bodies is 3.3 percent of the national income in the United States and 8 percent in the United Kingdom.

The following are the figures on which these comparisons are based:

As of 1934	United States	United Kingdom
	Billions of dollars	*Billions of pounds*
Gross central government debt	27.9	[1] 6.9
Net central government debt (after deduction of treasury balances, stabilization funds, and other assets)	19.4	6.3
Debts of all other government bodies	17.6	1.4
Total public gross debt	45.5	8.4
Total public net debt	37.0	7.7
National income	50.0	4.0
	Millions of dollars	*Millions of pounds*
Interest paid by central government	817	215
Interest paid by all other government bodies	844	105
Total interest paid on public debt	1,661	320

[1] Excluding war debt.

The CHAIRMAN. Governor Eccles, I want to suggest to you that it would be instructive if you would at some place in the record explain what eligible paper is, or what may be eligible paper under the existing law. I will not ask you to do that now. Just put it in the record.

Governor ECCLES. All right.

The CHAIRMAN. If there is no objection, the committee will meet again Monday morning at 10:30. Governor Eccles, we want you back here at that time, please.

Thereupon the committee adjourned until Monday, Mar. 18, 1935, at 10:30 a. m.)

BANKING ACT OF 1935

MONDAY, MARCH 18, 1935

House of Representatives,
Committee on Banking and Currency,
Washington, D. C.

The committee met at 10:30 a. m., Hon. Henry B. Steagall (chairman) presiding.

The Chairman. Gentlemen, we are ready to resume the discussion with Governor Eccles. Mr. Hollister, if you wish, you may have the discussion this morning.

Mr. Hollister. Governor Eccles, I would like to ask you a few preliminary questions before going into the actual gist of the bill itself.

Would you mind telling the committee—and these questions are with respect to title II, because with respect to title I and title III, I think there will be very little discussion. Would you mind telling the committee how this title II was prepared, who wrote it chiefly, and how it was drafted?

Governor Eccles. The members of the legal, economic, and operating staff of the Federal Board, together with myself, were appointed a committee by the board, to prepare Federal Reserve legislation to be considered by what is known as the "Interdepartmental Loan Committee", which the President had asked to consider all legislation dealing with financial matters. That in general is the way the legislation was prepared. Of course, it was——

Mr. Hollister (interposing). That was initiated by the Federal Reserve Board?

Governor Eccles. What is that?

Mr. Hollister. Was that initialed by the Federal Reserve Board, did I understand you to say?

Governor Eccles. The Federal Reserve Board appointed, at my request, a committee to develop this legislation.

Mr. Hollister. And who was that committee?

Governor Eccles. The committee were members of the staff. I was the chairman of the committee. The other members of the committee were Dr. Goldenweiser, who has been with the Federal Reserve Board for about 15 years, Mr. Wyatt, general counsel, who has been with the Board for nearly 18 years, Mr. Morrill, the secretary, who has been with the Federal Reserve Board for 4 or 5 years and prior to that was with the Federal Farm Loan Board, and Dr. Currie, who is Dr. Goldenweiser's assistant. That was the immediate committee.

They were assisted, of course, by other members of the staff, such as Mr. Smead, chief of the Division of Bank Operations, and Mr.

Paulger, chief of the Division of Examinations. Those men have been with the Federal Reserve Board for a good many years.

This committee worked with me in the development of legislation which was considered necessary and advisable. The proposed legislation was, in turn, cleared with a subcommittee of the Interdepartmental Loan Committee, which reviewed it and suggested modifications and changes. Mr. Morgenthau was appointed by the President as chairman of the Interdepartmental Loan Committee.

Mr. HOLLISTER. May I ask you there, was not that Interdepartmental Loan Committee appointed some time ago as a clearing house for the various departments' financial requirements?

Governor ECCLES. No; not altogether. It was appointed to clear any legislation that was coming up from certain departments. All legislation that was to come up from nine departments, including the Federal Deposit Insurance Corporation, the Federal Reserve Board, the Reconstruction Finance Corporation, the Home Owners Loan Corporation, and the Farm Credit Administration, was to be cleared through this committee or a subcommittee. That committee was to——

Mr. HOLLISTER (interposing). It was to clear legislation as well as to coordinate finance?

Governor ECCLES. Largely to clear legislation.

Mr. HOLLISTER. This draft went before a subcommittee for consideration?

Governor ECCLES. Yes, sir.

Mr. HOLLISTER. Who were the members of that subcommittee, if you remember?

Governor ECCLES. Yes. There was Mr. Coolidge, the Under Secretary of the Treasury, Mr. Oliphant, general counsel of the Treasury, Mr. Jesse H. Jones, Mr. Lynn P. Talley, who was formerly governor of the Federal Reserve Bank of Dallas and is now assistant to the directors of the Reconstruction Finance Corporation, and Mr. Leo T. Crowley. I think, Mr. J. F. T. O'Connor, Comptroller of the Currency, was in at one or two meetings, at the last. But most of the work on title II was gone over and discussed by Mr. Coolidge, Mr. Oliphant, and myself, and——

Mr. HOLLISTER (interposing). Title II, then, as it was drafted and presented in this bill, was the result of the preliminary draft which the committee appointed by the Federal Reserve Board had prepared, after it had been checked over by the subcommittee of the Interdepartmental Loan Committee?

Governor ECCLES. That is right.

Mr. HOLLISTER. Was that discussed at all with, or was the benefit of the advice received of, any of the governors or the directors or officers of any of the Federal Reserve banks?

Governor ECCLES. No; not the governors. The matter was not discussed with them.

Mr. HOLLISTER. This was a presentation, it might be said, from the point of view of the present Federal Reserve Board?

Governor ECCLES. That is right.

Mr. HOLLISTER. Was this draft, before being presented to Congress, approved by the Federal Reserve Board?

Governor ECCLES. No. The Board was not asked to approve it. The Board was kept advised of the legislation.

Mr. HOLLISTER. The Board did not give any final approval of the legislation?

Governor ECCLES. In fact, they felt that it would be better to take no official action in the matter; but they were constanly advised as to the development of the legislation, and individually they were invited to express themselves about it, which they did.

Mr. HOLLISTER. But, prior to the introduction of this bill, there was no consultation whatsoever with any of the individual bankers of the country?

Governor ECCLES. Oh, yes.

Mr. HOLLISTER. Federal Reserve or otherwise?

Governor ECCLES. Officials of the American Bankers Association. Mr. Rudolph S. Hecht, president, Mr. Robert V. Fleming, first vice president, and Mr. Tom K. Smith, second vice president, of the American Bankers Association, were advised with—particularly Mr. Smith.

Mr. HOLLISTER. While the bill was being drafted?

Governor ECCLES. Yes; and the report in the press as to the attitude of the American Bankers Association is entirely untrue. I think that, as a matter of fact, they have been cooperative and constructive.

Mr. HOLLISTER. I do not know what that report in the press is that you refer to.

Governor ECCLES. I just saw a report that represented the American Bankers Association as being opposed to title II of the bill. I think it appeared along with an account of the Liberty League's opposition, which, of course, was not——

Mr. HOLLISTER (interposing). There was consultation, then, with some of the officers of the American Bankers Association?

Governor ECCLES. Oh, yes.

Mr. HOLLISTER. But not with any of the governors of the Federal Reserve banks?

Governor ECCLES. Not specifically with reference to this particular bill; but I discussed banking legislation with Governor Harrison, in a general way, but not the specific provisions of this bill.

The proposal to broaden the eligibility requirements has been generally recognized by all the bankers as desirable for some time. The proposed combination of the positions of chairmen and governors is desirable to the governors. It is undesirable to the chairmen, if they are to be eliminated, or it is undesirable to the governors if they are to be eliminated. But the principle of the combination of those officers——

Mr. HOLLISTER (interposing). I do not want at the present time to go into that in detail.

Governor ECCLES. Yes.

Mr. HOLLISTER. What I was trying to get was the preliminary picture and how much consultation there was with those who were to be very substantially affected by the bill, if it were to go into effect in its present form.

Governor ECCLES. Yes.

Mr. HOLLISTER. You have submitted to us a memorandum containing some eight modifications, which you suggest.

Governor ECCLES. There is one of them which is not important, and I prefer to withdraw it. That is the one that suggested——

Mr. Hollister (interposing). No. 6, you mean, the suggestion as to the authority over open-market operations being vested in the Federal Reserve Board?

Governor Eccles. It is the one which suggested that two members on the Federal Reserve Board be selected from Federal Reserve banks, men who have had experience as officers or directors of Federal Reserve banks.

Mr. Hollister. Well, I do not seem to find such a provision on this memorandum.

Governor Eccles. Well, anyway, I don't think that is very important.

Mr. Hollister. Well, these modifications that you have suggested to us, have they been checked up in the same way in which the original bill was drafted? Were they prepared by your committee of the Federal Reserve Board and checked with the Interdepartmental Loan Committee?

Governor Eccles. No. They have been checked only with some of the individual members of the committee, not as official committee action. They were, of course, checked very thoroughly with our own committee and were also checked with the officials of the American Bankers Association.

Mr. Hollister. Now, as I understand it, there is still another change suggested--that is, the withdrawal of one of these suggestions?

Governor Eccles. Well, I do not think it is very important one way or the other. It was not mandatory but simply a suggestion that, in selecting the members of the Federal Reserve Board, the President considered the advisability of including at least two members who shall have had experience as officers of the Federal Reserve banks. The difficulty I see about that is that it is practically impossible to get any officials from a Federal Reserve bank to go on the Federal Reserve Board; because the compensation paid the officials of the Federal Reserve banks is two or three times the compensation paid the members of the Federal Reserve Board.

Mr. Hollister. Is it probable that, as we go along, there will be still further suggestions made to change the draft of the bill as presented?

Governor Eccles. You mean by me?

Mr. Hollister. By you or those representing the Interdepartmental Committee or the Federal Reserve Board.

Governor Eccles. I do not think there will be any. Of course, I cannot say. I cannot speak for others.

Mr. Hollister. I realize that.

Governor Eccles. There may be.

Mr. Hollister. What I am trying to get at, of course, is to what extent the draft of the bill presented to us is a kind of rough draft, which is perhaps quite controversial at points, and how much it is the well-considered judgment, as you might say, of all the financial interests of the administration. Of course, if it is to be submitted in one form and suggestions made for changes by, perhaps, first one branch and then another branch, perhaps the committee would have a little different feeling about it than if it was in one form, which could be finally agreed upon and considered the united suggestions of all the financial branches of the administration.

Governor ECCLES. All except one of these suggested changes were very minor modifications. For instance, the approval of the appointment of governors by the Board each 3 years, instead of annually.

Mr. HOLLISTER. That is rather a major change.

Governor ECCLES. Some may consider it major, but, at least, it is not fundamental. It is extending the period of approval only. When we prepared the legislation we expected, certainly, that modifications would be suggested or made, as is true in all legislation.

Mr. HOLLISTER. Perhaps we might discuss section 201, then, right off. Of course, a Federal Reserve bank is a private bank, which is owned by private capital, the individual banks having the capital stock in that Federal Reserve bank.

Governor ECCLES. It is quite different from the ownership of most private corporations, since the member banks are limited to a 6-percent return on their capital under every circumstance. The board of directors of a Reserve bank must get the approval of the Federal Reserve Board with reference to expenditures and so forth. It is quite different from the average private bank.

Mr. HOLLISTER. It is not exactly the same, of course.

Governor ECCLES. No.

Mr. HOLLISTER. But the fact is that it is the money of private banks which goes to buy the stock of the Federal Reserve banks; and the theory of the Federal Reserve banks was that the private banks, which have the stock, would control the boards.

Governor ECCLES. Of the Federal Reserve Board?

Mr. HOLLISTER. Of the individual banks. Now, you have stated——

Mr. BROWN (interposing). May I interrupt a moment?

Mr. HOLLISTER. Yes.

Mr. BROWN. I have not seen a discussion of it yet, but the law still provides for the issuance of stock to the Government of the United States. I do not think any was ever taken.

Mr. HOLLISTER. But, at the present time, all of the stock is owned by the private banks.

Mr. BROWN. That is the fact, is it not, Dr. Goldenweiser?

Dr. GOLDENWEISER. Mr. Wyatt says there is such a provision. I had forgotten it.

Mr. BROWN. It was in the original Federal Reserve Act.

Governor ECCLES. The purpose of that provision was to enable the Government to provide capital for the Federal Reserve banks if the banks failed to subscribe for sufficient stock; but they did not fail to do so.

Mr. BROWN. It was not put in the alternative, like that, was it?

Governor ECCLES. Yes; I think it was.

Mr. HOLLISTER. It was similar to the method by which the Government had to establish a number of these organizations which are private organizations; to start them by Government backing. It was similar to the home-loan banks, for instance.

You have stated that you did not consider that the change suggested (as to the approval of the Governor) from 1 year to every 3 years, was a major change?

Governor ECCLES. Nothing fundamental. It in no way changes the operation of the system.

Mr. HOLLISTER. It is true, is it not, that the right of the Federal Reserve Board to approve every year the appointment of the chief executive officer—the governor—of the regional banks, makes it possible, of course, for the Federal Reserve Board to insist on someone who is absolutely satisfactory to the Board, and to do it every year.

Governor ECCLES. Well, of course, the right of approval would make it necessary that the Governor be satisfactory to the Federal Reserve Board.

Mr. HOLLISTER. And if that is changed to 3 years, just to that extent the power of the central board over the chief executive of the regional bank is weakened.

Governor ECCLES. It was intended in the original Federal Reserve Act that the chief executives of the regional banks should be the chairmen.

Mr. HOLLISTER. Theoretically, but not as a matter of fact.

Governor ECCLES. Yes; but I think they could possibly be made to be.

Mr. HOLLISTER. Under existing law?

Governor ECCLES. Oh, yes. The law has not been changed in regard to the chairmen at all.

Mr. HOLLISTER. I know that. But I know of no situation, in any corporation, where the board of directors might not designate powers in such a way as to make either the chairman of the board or the president chief executive officer. In some corporations the chairman of the board is the chief executive officer and the president has very little authority, and in some corporations the president is the chief executive officer and the chairman of the board is merely a figurehead.

Governor ECCLES. It depends largely on the strength of the men the respective offices of governor and chairman. The governors have usually exercised more influence than the chairmen. If it was their purpose, the board might make the chairman the chief executive of the bank.

Mr. HOLLISTER. But in the ordinary corporation, if it came to a conflict between two executive officers, the one that would get the power would be the one that the board of directors backed up, would he not?

Governor ECCLES. I suppose he would. That is one of the reasons, if you are going to operate a unified Federal Reserve System; that it is very necessary and desirable that such conflicts should not exist and that there be cooperation throughout the entire system. Otherwise the function of a central bank cannot be successfully carried out.

Mr. HOLLISTER. Well, there is a difference, of course, between cooperation, coordination, and control. What I am trying to get at is whether section 201 does not really take away the control of the regional banks from those who are duly appointed to handle their affairs; that is, their directors, two-thirds of whom are appointed by the banks who own the stock, and actually vest that control in the Federal Reserve Board.

Governor ECCLES. You are not vesting it in the Federal Reserve Board because the Federal Reserve Board would not designate the governor.

Mr. HOLLISTER. They can throw him out at the end of the year if they do not like him. It is rather a strong weapon to hold over his head.

Governor ECCLES. They can only disapprove of the person selected by the board of directors of the bank. The proposal is that the head of the bank be acceptable to the Federal Reserve Board and to the board of directors of the bank, which is certainly necessary if you are going to have coordination. It would not be good organization for a local board to elect or appoint a governor who is also to be a class C director and chairman of the board of directors, under this provision, if that appointee were not acceptable to the Federal Reserve Board.

Mr. HOLLISTER. Is the governor at the present time a class C director?

Governor ECCLES. No; he is not a class C director. He cannot be. Under the present law the Federal Reserve Board appoints all three class C directors and designates one of them as chairman. Under this bill the Board is giving up its power or right to appoint one of the class C directors and to designate a person of its own selection as chairman.

Mr. HOLLISTER. There is no necessity of that if this other suggestion is not effected. There is no particular need of making the governor a class C director.

Governor ECCLES. If he is going to be chairman he would have to be a class C director.

Mr. HOLLISTER. Yes; if he is chairman he would have to be a class C director; but could you not provide for a governor and not change the law with respect to class C director?

Governor ECCLES. The legislation could be left just as it is and you would continue to have a chairman and governor, just as you now have.

Mr. HOLLISTER. You could abolish the chairmanship and still leave the governor, the chief executive officer, appointed by the board of the bank itself.

Governor ECCLES. And have no chairman?

Mr. HOLLISTER. And have no chairman.

Governor ECCLES. The chairman of the board is always a director.

Mr. HOLLISTER. Yes; but the governor could be appointed from one of the class A or class B directors.

Governor ECCLES. That would require that the banks give up their selection of one of the six directors they now select.

Mr. HOLLISTER. I should imagine that in order to keep their control, by having a governor who would not be removable each year, they would be willing to give that up.

Governor ECCLES. I find that the combination of the offices of governor and chairman is universally looked upon as desirable.

Mr. HOLLISTER. And I agree with that. The thing I am doubtful about, very frankly, is the increase in the control of the Federal Reserve Board over the powers of the individual banks.

Governor ECCLES. With this change to a 3-year period, the American Bankers Association is very favorable to this feature. The only opposition comes from one source, and that is New York. Every other place except New York agrees to that change.

Mr. HOLLISTER. The question is whether the independent banks ought not to have the right to name their own chief executive officers without any interference by the Reserve Board.

Governor ECCLES. They cannot do that without at the same time depriving the Federal Reserve Board of the power of appointing or approving of the officers. In that case you might as well do away with the Federal Reserve Board. The Board has no purpose if you are going to make 12 separate banks, to operate as separate banks. Why have a Board if you do that? I do not know what the desire of Congress may be in that regard, but certainly if you want to have 12 independent banks, then there is no reason or no purpose for having a Federal Reserve Board. But if you are going to have a Federal Reserve Board, then it has to be charged with responsibility and it has to be given some authority.

Mr. HOLLISTER. But you have today a Federal Reserve Board that is charged with responsibility, and no one would deny that the Federal Reserve Board today has enormous power, enormous authority, and enormous responsibility; and also that, to all intents and purposes, there are 12 banks which have considerable—not considerable, but some— independence; not as much as they used to have. I am not asking that they have more, but I just dread taking away what that have left.

Governor ECCLES. I do not believe that we are taking it away, because you are giving to them the right to select a chairman and class C director, which they do not now have; and as a consideration for that the Federal Reserve Board would be given the right to approve of the appointment every 3 years. You would have anything but a satisfactory bank situation if the executive head of each of these 12 banks were entirely unsatisfactory to and uncooperative with the Federal Reserve Board.

Mr. HOLLISTER. Well, just to be more specific, at the present time, under the present set-up, what are the unsatisfactory conditions that arise out of the fact that governors of the regional banks are not subject to removal each year or at the end of any specified time by the Federal Reserve Board? I do not mean exactly removal, but they will be in such a position that they may be unapproved at the end of a certain specific time. What are the conditions that arise——

Governor ECCLES (interposing). You mean with the present law?

Mr. HOLLISTER. At the present time in operation.

Governor ECCLES. All the legal relationship of the Board with the bank is through the chairman. The governors, as I stated a while ago, are not directors of the banks. It seems to me that it is a bad organization and that no one would set up a private organization on such a basis.

Mr. HOLLISTER. Well, I understand there are certain mechanics that have to be ironed out, but what I am trying to get at is this: What are the objections under the present operation to having the chief executive officer, who is appointed by the regional bank's board itself——

Governor ECCLES (interposing). The regional banks will appoint their chief executive officers.

Mr. HOLLISTER. Yes; I know. But he can be disapproved at the end of a year. He could be disapproved at the time he is appointed, and if he does not act the way——

Governor ECCLES (interposing). He can be disapproved at the end of 3 years.

Mr. HOLLISTER. That is under the suggested changes?

Governor ECCLES. That is under the suggested changes. He could be disapproved at the end of 3 years, which, I think, is very necessary and desirable in order to avoid friction and to have cooperation and coordination.

Mr. HOLLISTER. Can you point out instances of where governors of the regional banks have conducted themselves in such a way that the Federal Reserve Board has disapproved, and to what extent and what are the nature of such actions? What I would like to get before the committee, if there are such things, is what action these governors take which the Federal Reserve Board feels it should have the right to disapprove. If it is merely a question of making one man both the governor and the technical chairman of the board—that is, of course, easy to settle. What I am trying to get at is, what is the purpose of giving the Federal Reserve Board the right to say to a regional bank, " You cannot appoint the man you want ", or, at the end of the year, " You cannot reappoint the man you want "?

Governor ECCLES. Do you not think that there are enough good men so that it is possible to get a man that would be agreeable both to the Federal Reserve Board and to the regional bank board? Do you think it is necessary to have as the head of one of the Reserve banks a man who is unacceptable, because of inefficiency, we may say, or because of incapacity, and yet have him retained because of the personal relationship existing between the managers of these banks, or the governors, and the local boards? There is a sentimental relationship and friendship that is built up due to very close contacts, and a director of a bank, who personally has no stock ownership in a bank, and only goes to a meeting once every week or so, or every month, is not likely to oppose the reappointment of a governor, even though he may feel that he could be improved upon, or that he may not be entirely desirable.

Mr. HOLLISTER. I can answer that very easily by saying that such a man should not be a director.

Governor ECCLES. That is very true. But, after all, the directors are not stockholders. You must realize that.

Mr. HOLLISTER. Would not your objection be met by a suggestion that the governor could be removed for cause, just as you pointed out the other day that the members of the Federal Reserve Board may be removed for cause, or the Governor of the Federal Reserve Board?

Governor ECCLES. I think they already have that power now—to remove for cause.

Mr. HOLLISTER. What did you say?

Governor ECCLES. They already have that power—to remove for cause.

Mr. HOLLISTER. The governor or one of the directors of one of the regional banks?

Governor ECCLES. Yes.

Mr. HOLLISTER. Well, then, there would be no necessity for this. If a man is inefficient or incapable, he can be removed, so that this legislation is not needed for that purpose.

Governor ECCLES. The legislation, I think, is very greatly needed. The matter of inefficiency or inability is a very difficult thing to prove. A man may be filling a position that somebody else could fill more satisfactorily. Questions of ability or efficiency are matters of degree and you would have a very difficult problem if you should attempt to remove a man for cause unless there were some glaring lack of capacity or some personal act that would justify the removal.

Mr. HOLLISTER. Well, it really comes down to this, then: that you believe that, as between the relative efficiency or inefficiency of several men, the power of designating one of such men to conduct that regional bank should be in the Federal Reserve Board rather than in the board of directors, the majority of whom have been elected by those whose money is invested in the stock of the regional bank.

Governor ECCLES. I think that, in the interest of the System, it is very necessary that the Federal Reserve Board have the approval of these governors who are selected by the directors of the Reserve banks; and, as I stated, it would seem to me that there should be a sufficient number of able men to permit appointments that are desirable to both the Federal Reserve Board and the local board. The governors are the liaison officers under this relationship between the 12 Federal Reserve banks and the Federal Reserve Board; and, for this reason, it seems to me, the Federal Reserve Board should have the approval. Any governor who objects and any board that objects to this Board approving would be actuated by the desire to retain office, even though their retention was unsatisfactory and unacceptable to the Federal Reserve Board.

Mr. HOLLISTER. Of course that is a question as to whom the heads of the regional banks should be acceptable. I had understood that the theory of the Federal Reserve organization was that high-class bankers, of independent judgment, should have some say in the conduct of the System. Now it would seem to me to be fairly clear that, if the head of each regional bank must completely follow what the Federal Reserve Board indicates at all times, he ceases to be a banker of independent judgment. Of course, if that is the desire of Congress, that settles it; but that was not the original plan of the Federal Reserve System.

Governor ECCLES. There is no thought or expectation that such a thing will happen. In practice, I am certain that the banks will be run under this bill very largely, so far as everything except monetary policy is concerned, by the local boards of directors and by the governors of the banks. There is nothing in this bill that provides that the Federal Reserve Board shall select or force on a bank a governor who is unacceptable to the board of the bank.

Mr. HOLLISTER. No; they could not force anybody on the bank who was unacceptable to them; but they could keep refusing to appoint people who might be acceptable to the board of the regional bank, indefinitely.

Governor ECCLES. Why should not the governor be acceptable to both boards? If you want good organization, is it not better to have the governor acceptable to both boards?

Mr. HOLLISTER. You have had enough experience to know that if you have a situation of that character, where something must be acceptable to people, absolutely, that they would have the control.

Governor ECCLES. The Farm Credit Adminstration operates in that way, in the question of the appointment of land-bank officers. They are appointed by the local boards, subject to the approval of the Farm Credit Administration, and the banks are owned by the local farm associations, which is private ownership, so that you have an example and it has worked out very well.

Mr. HOLLISTER. Of course their functions are somewhat different from those of the Federal Reserve System.

Governor ECCLES. Yes.

Mr. HOLLISTER. Now, moving to section 203, and raising again this question of independence: In the draft of the bill at the present time the Governor of the Federal Reserve Board cannot be very independent if he can be removed by the President at will. He cannot be particularly independent from the Executive's desire.

Governor ECCLES. You mean in the present legislation?

Mr. HOLLISTER. The proposed legislation.

Governor ECCLES. That is true in the present legislation. There is nothing in the proposed legislation with reference to that.

Mr. HOLLISTER. What is the exact wording of the present legislation with respect to the removal of the governor?

Governor ECCLES. Do you have that, Mr. Wyatt?

Mr. HOLLISTER. What section is that?

Mr. WYATT. Section 10, page 26, of the 1933 edition of the Federal Reserve Act.

Mr. HOLLISTER. Would you read that into the record?

Mr. WYATT (reading:)

Of the 6 persons thus appointed, 1 shall be designated by the President as Governor and 1 as Vice Governor of the Federal Reserve Board. The Governor of the Federal Reserve Board, subject to its supervision, shall be its active executive officer.

Mr. HOLLISTER. Is that all there is?

Governor ECCLES. Is that all you have on that?

Mr. HOLLISTER. Is there anything in that which permits the President to remove the Governor of the Federal Reserve Board?

Mr. WYATT. It has been interpreted in practice that it does.

Mr. HOLLISTER. I realize that it is so stated, and it has been stated in this room a number of times. It has been stated in the papers, but I have never yet been able to find where the President of the United States has the power to remove the Governor of the Federal Reserve Board.

Mr. SISSON. Is it not true, Mr. Hollister, that these officers are executive or administrative officers, and is it not true that any executive or administrative officer may be removed arbitrarily by the President?

Mr. HOLLISTER. I think it has been settled by the United States Supreme Court.

Governor ECCLES. Yes, sir.

Mr. SISSON. It has been settled, I think.

Mr. HOLLISTER. Let us not get into a discussion of that. I do not want to get into a discussion with any members of the committee, although I think I can point out to Mr. Sisson that he is incorrect in his interpretation of the decision.

Let me ask you a question right in that connection. The Comp troller of the Currency is appointed for how many years?

Governor ECCLES. Five years.

Mr. HOLLISTER. Can the Comptroller of the Currency be removed by the President?

Governor ECCLES. I do not think so. The term of his office is provided under the statute.

Mr. HOLLISTER. Is the term of office of the Governor of the Federal Reserve Board provided by the statute?

Governor ECCLES. Not as Governor. His term as member is provided for.

Mr. HOLLISTER. It is a 12-year term as director?

Governor ECCLES. That is right.

Mr. HOLLISTER. Then he is appointed Governor?

Governor ECCLES. Yes.

Mr. HOLLISTER. So, theoretically, he is Governor up until he is removed?

Governor ECCLES. Up until the time Governor Meyer was appointed the President designated the Governor each year. It had been the custom from the beginning of the Federal Reserve System for the President to designate the Governor from year to year.

Mr. HOLLISTER. And the fact remains that at the present time it is provided that the Governor shall be appointed, and there is no statement as to how he can be removed. It is also true that the change from the existing statute to the proposed statute is that, in the existing statute, there is a provision for the appointment of the Governor, with no provision as to removing him from office; whereas in the proposed statute it is specifically provided that he shall serve solely at the will of the President. That is the case, is it not?

Governor ECCLES. That is correct. It seems to me that it is a matter that should be clarified and that, if it is not the wish of Congress that the Executive shall have the right to appoint a Governor and remove him, the term of office as Governor should be made specific, and the interpretation that has always been placed upon it should be clarified.

Mr. HOLLISTER. I agree with you fully. I am merely trying to bring out by questioning what this bill does. Naturally, the Congress must make the decision as to what they want. I want to make it perfectly clear what the provision of the proposed law will bring about; and it is also true, is it not, that if the changes which you have suggested in your memorandum are not made effective, as I think you have stated earlier in the hearing, it would be possible, always assuming that an Executive desires to do it, for the President to change completely the personnel of the Federal Reserve Board by designating each member of the Board Governor in turn and removing him the next day.

Governor ECCLES. I do not believe that is possible.

Mr. HOLLISTER. I think it is highly improbable, but it is possible.

Governor ECCLES. If a member of the Reserve Board desired to retain his position on the Board, he would refuse to accept the position of Governor, knowing that he would go out the next day or the next week. If, on the other hand, he did not choose to stay on the Board if the President desired to remove him, he very likely would resign without going through the formality of being appointed as Governor.

Mr. HOLLISTER. I think that is highly probable. What I am trying to get at is—I do not like to be influenced into legislation which would make make possible the arising of a dangerous condition, when some irresponsible person might be in the position of Chief Executive, and when such legislation is not necessary. I believe, to that extent, the suggestions for amendment which you have made are excellent.

Governor ECCLES. The possibility of a President resorting to sharp practice of that sort in order to change the Board, of course, did not occur to me, or, I think, anybody else who had anything to do with this legislation. The reason for providing that a Governor's term as a member shall expire when he is no longer designated as Governor was not to give to the President additional power but to make it possible for a Governor who was no longer designated as "Governor" to resume business without waiting for a period of 2 years.

Mr. HOLLISTER. Of course, that could be done by other phraseology.

Governor ECCLES. That is what is proposed. In other words, the same thing has been accomplished, for all practical purposes, by the suggested change; and because of the objection that was raised, that you mention now, the amendment was proposed.

Mr. HOLLISTER. Do you consider it wise that the President should have complete control over the Governor of the Federal Reserve Board?

Governor ECCLES. I think so. It is my feeling that the President should have the right of appointment of the Governor of the Federal Reserve Board. That is true in practically every country in the world.

Mr. HOLLISTER. He should have the right of appointment; but I am talking about the right of removal.

Governor ECCLES. That is right. He should have, it seems to me, the right of appointing the Governor to serve at his pleasure. I think that is in the interest of the Federal Reserve System. I think it is very necessary that there be a very close relationship and liaison between the banking system and the administration in power; and I think that the Governor of the Federal Reserve Board is the channel through which that relationship should develop, in the interest of the banking business.

Mr. HOLLISTER. Can you not conceive of a situation where political exigencies might be in direct conflict with wise banking policy and wise credit policy?

Governor ECCLES. All I can say is that, if you have such exigencies—war is a case in point and depression is a case in point—then I think it would be very unfortunate if the administration was unable to carry out its program. I stated, I think, when I first testified, that the responsibility of any administration in power is largely a social and an economic one. Practically all political questions relate to social and economic problems. An administration cannot be charged, when it comes into power, with dealing with those problems separately, free, apart, and divorced from the money system.

Mr. HOLLISTER. You believe that even though from the point of view of wise banking and a wise handling of the financial business of the country a certain policy would be desirable, that if an administration decided that it should pursue a policy which might be otherwise, it should be in a position to control the banking and credit systems, to force it along with its policy, irrespective of what the best minds of independent banking might think?

Governor ECCLES. Of course, we have an independent banking system, to an extent; and I do not believe that anybody would feel that for the system to be more independent would be in the best interests of the bankers——

Mr. HOLLISTER. I do not want to interrupt you. I believe there is a great deal in what you say. I do not believe we can answer present questions by referring to the improper actions of the past. I am just asking the question of whether or not it is unwise to put the complete control into the hands of the Executive; and I am generalizing entirely, with reference to no particular executive and no particular condition of the country. Before you answer, let me put it a little more specifically. In our democracy, every so often the party in power must appeal to the country, once every 4 years for Presidential elections and once every 2 years for congressional elections. It is a definite time at which such things have to be done, unfortunately. Is it not very unwise to give the power of manipulation to the Executive entirely when it comes to the credit situation and the banking situation? Would it not be probable that the greatest man imaginable, with an election coming on, would try to take advantage of every possible facility to see that that election is assured, and would it not be possible for him to control the banking and credit system of the country for that purpose?

Governor ECCLES. There is nothing in this bill that proposes that.

Mr. HOLLISTER. But it gives the President a much greater control over the credit and banking facilities of the country?

Governor ECCLES. In what way, except as the Federal Reserve Board has increased power?

Mr. HOLLISTER. It gives the Federal Reserve Board increased power.

Governor ECCLES. That is right.

Mr. HOLLISTER. It gives the President greater power over the Board?

Governor ECCLES. No. The President has no different power over the Board.

Mr. HOLLISTER. Well, the President has greater power over the Governor, who is the Chief of the Board.

Governor ECCLES. Not unless you construe the proposal to mean that it gives the President greater power than he now has. Of course, there has never been a legal test as to the power of the President to remove the Governor; but as I say, in practice it has always been accepted as giving him that power.

Mr. HOLLISTER. If it does not give any more power than at present, there is no need of the change.

Governor ECCLES. No; there is no proposal to make the change, except——

Mr. HOLLISTER (interposing). As to the ability of the Governor to go back into business?

Governor ECCLES. That is the sole purpose of it; and there was no purpose or expectation that this was giving to the President additional power.

Mr. HOLLISTER. Then you would be perfectly willing to strike out the provision for removal?

Governor ECCLES. I do not see a particle of objection to it, because, in practice, that is what happens and will happen.

Mr. HOLLISTER. You say you see no objection to striking it out?

Governor ECCLES. The whole purpose of getting that into the legislation was to make it easier to get someone to act as Governor; in other words, to make it easier to get a man to accept.

Mr. GOLDSBOROUGH. May I interrupt? In that connection, Governor Eccles, if there is in fact any legal obstacle to putting into effect the practice that now obtains, you would favor a change in the language which would legalize and carry forward the practice?

Governor ECCLES. Yes; I think it is desirable in the interest of banking and in the public interest that the administration in power designate the governor and that the governor serve during the pleasure of that administration. That has been true in most other countries.

Mr. HOLLISTER. That is not true in England.

Governor ECCLES. England is about the only exception. It is true in practically every other country. It has been recognized, in the establishment of all the central banks, within recent years, that it is very necessary and desirable that the administration in power have that responsibility and that authority.

Mr. HOLLISTER. Now, with respect to those banks, of course, you have one central bank, where the board is privately elected or appointed, and the chief executive, governmentally appointed, who, of course, cannot exceed what the board will let him do. The board itself controls the executive officers, even in the Bank of France—or in most of the great countries, outside of Italy and Russia. In all those cases the board itself, which ultimately controls the chief executive officer, is privately elected or appointed.

Governor ECCLES. There are differences in the various organizations. The Bank of Canada is the most recent; and in Canada the board is really an advisory board and the governor can veto an action of his board. He does not have to follow their recommendations or their authorizations, as I understand it.

Mr. HOLLISTER. In the Canadian bank a board of seven directors is elected from diversified occupations by the shareholders.

Governor ECCLES. That is right.

Mr. HOLLISTER. The Canadian bank has a governor, a deputy governor, and an assistant deputy governor, who have to be appointed for 7 years by the Governor General in council.

Governor ECCLES. The board does not control the governor there to the extent——

Mr. HOLLISTER (interposing). But, after the first term, however, these officials shall be selected by the directors, subject to the approval of the Governor in council.

So that still puts the control of the central bank pretty well in the hands of the private shareholders.

Governor ECCLES. It puts it in the hands of the Governor in Canada, practically. Of course, there is this difference. In every other country except this country, the commercial banks are not the shareholders, but the public are the shareholders.

Mr. HOLLISTER. That is so in England.

Governor ECCLES. It is so in Canada, too. I think it is so in France, and it is so in practically all the countries. I believe this is the only coutnry where the banks control the central banking system through their stock ownership and the majority of the board of directors.

Mr. HOLLISTER. But the public owns the stock in the banks, which, in turn, own the stock in the Federal Reserve banks.

Governor ECCLES. There is a great difference between——

Mr. HOLLISTER (interposing). The governors——

Governor ECCLES (interposing). In fact, in some of the countries the banks are directly prohibited from owning any stock whatever in the central banks, and the bankers are prohibited from being represented on central banks.

Mr. HOLEISTER. Well, of course, under our system, with our regional banks, we have only half of the directors that can be appointed by the member banks.

Governor ECCLES. No. Two-thirds of them are appointed by the member banks.

Mr. HOLLISTER. Yes; but half of these are drawn from industry, and only half may be bankers.

Governor ECCLES. Yes; but they are appointed by the banks. Two-thirds of the board are appointed by the banks, and the stock is owned by the banks.

Mr. HOLLISTER. I want to bring out the change in control this bill will make, so I will take up for a few minutes section 205, which provides for the open-market committee, a committee of five, which is to be appointed and will consist, first, of the Governor of the Federal Reserve Board, who, in turn, serves at the pleasure of the President; next, two members of the Federal Reserve Board; and, next, two governors of the Federal Reserve banks, who, in turn, if the provisions of this bill should become effective, may fail of approval by the Federal Reserve Board at the end of a year, in the event, we will say, that they are unwililng to go along with what the Federal Reserve Board desires. That, of course, places the open-market committee and its operations entirely in the control of the Federal Reserve Board, does it not?

Governor ECCLES. You are discussing the provisions of the bill with reference to the operation of the open-market committee, as provided in the bill.

In my opening statement, if you will recall, I stated that that provision of the legislation was not satisfactory, and that open-market operations should be placed with the same body that had the authority to fix discount rates and reserve requirements; that they were three functions of monetary control that should be together, in the same body, and that I felt that the Federal Reserve Board was the body charged with the public interest; and that it should, therefore, have that power and authority, subject, however, to securing the advice of a committee of 5 governors selected by the 12 banks. I made that suggestion in my opening statement. I suggested that, rather than having an indirect way of putting the Federal Reserve Board in complete control.

Mr. HOLLISTER. Your theory is that it might just as well take the whole thing right over and have no control whatever by the regional banks?

Governor ECCLES. I feel that the authority over open-market policy must be placed in a body that is charged with the responsibility that the present legislation gives to the governors, who are not even directors of the banks, the right to make open-market policies. The Board approves or disapproves of the policy, and then the 12 banks can either participate in the adopted program or they can refuse to do so, so that you have——

Mr. HOLLISTER (interposing). You say all of the 12 banks or each of them?

Governor ECCLES. Each or any.

Mr. HOLLISTER. And any of them might nullify what the others did.

Governor ECCLES. And what this proposed legislation is doing is putting the responsibility and the authority for open-market policy, discount rates, and reserve requirements, which are three instruments of monetary control, in the Federal Reserve Board.

Mr. HOLLISTER. You feel, then, that, notwithstanding how clear it might be, we will say, to practically all the bankers in one particular locality of the country, Dallas, San Francisco, or wherever it might be, they should not participate in the open-market operations. The Federal Reserve Board should have complete power, and no matter how much the bankers might disapprove they should be compelled to take participation?

Governor ECCLES. Absolutely. The question of monetary policy is a national matter, and it cannot be dealt with regionally without having such situations as we have had in the past. I think open-market policy, discount rates, and reserve requirements should be controlled by the Federal Reserve Board, while making it mandatory that the Board advise with the committee of governors before any action is taken with respect to any one of the three instruments of monetary policy that the Board controls.

Mr. HOLLISTER. That, however, is not in the draft as presented.

Governor ECCLES. No. That is the recommended provision.

Mr. HOLLISTER. Just a few questions on the matter of the collateral behind the Federal Reserve notes. In discussing this question on the days you have been before us you have stated that you did not see the collateral added anything to the value of the notes.

Governor ECCLES. That is right.

Mr. HOLLISTER. Do you feel that the gold provision does?

Governor ECCLES. It certainly does not under present circumstances. And under past circumstances, when there was not sufficient gold, or we felt there was not, to back up notes which were secured and issued, the requirement was suspended, as an emergency matter. In other words, when we get into an emergency, these rigid requirements are suspended. So long as everything goes normally and there is no difficulty in carrying out the requirement, they seem to operate all right.

Mr. HOLLISTER. Well, of course, there are those who do not quite agree with the wisdom of suspending such requirements, who do not believe that the emergency justified the suspension. But I am trying to get at your viewpoint. You say that the collateral does not add anything, neither does the gold. Query: Do you go the whole way, that we should remove all provision for some kind of collateral behind Federal Reserve notes?

Governor ECCLES. No. Personally I think it is very desirable to leave the gold-reserve requirement back of the Reserve notes, and also back of the deposits. The law provides that 35 percent of gold should be held back of the deposits.

Mr. HOLLISTER. Gold or lawful money?

Governor ECCLES. Gold or lawful money; and, of course, our lawful money now is——

Mr. HOLLISTER (interposing). Not gold.

Governor ECCLES. Gold certificates and other forms of currency.

The CHAIRMAN. That provision was written into the law when the law was that the legal money was gold?

Governor ECCLES. Yes.

Mr. HOLLISTER. What is the advantage of that gold behind the notes? Is it the limitation on the amount of notes that might be issued?

Governer ECCLES. That is the effect it might have, I suppose.

Mr. HOLLISTER. So that there is some upstairs limit, beyond which you cannot go?

Governor ECCLES. If you have a bank run, and banks closing, just as we did have, and you permit demands in gold again, and you permit the exportation of gold freely, then, through that action you precipitate financial troubles and bring about a suspension of the requirement. Now, if the payment of gold against deposits and the free exportation of gold should be suspended, and serious banking difficulties develop again, we would possibly go off the gold standard, and then these restrictions would be suspended.

Mr. HOLLISTER. Oh, we are off it today, of course, aren't we? But I don't want to get into a long discussion of that. Some people say there is a gold standard, simply because we can ship gold to settle international obligations.

The CHAIRMAN. Nobody can get gold.

Governor ECCLES. We have a price for gold now.

Mr. HOLLISTER. You believe there should be a gold reserve behind the Federal Reserve notes that should be maintained?

Governor ECCLES. I think it is desirable that it should be.

Mr. HOLLISTER. What is the reason for it? Is it to give confidence to the holder of the note that there is something behind it, or what is it?

Governor ECCLES. I think that there is no necessity of making the change. There would be nothing particularly to be gained by it. Without that requirement of holding so much gold back of deposits and back of currency, you would have, I suppose, no restriction of any kind. I think, psychologically, it would have a very bad effect upon the country, and it is unnecessary. It would, of course, leave our money a completely managed currency without any relationship to gold.

Mr. HOLLISTER. In other words, it would shake people's confidence in the pieces of paper that they carried around in their pockets?

Governor ECCLES. I think it would. Whether justifiable or not, that is the effect it would have.

Mr. HOLLISTER. And the shaking of that confidence would immediately be inflation of a kind, would it not?

Governor ECCLES. I doubt that. It has seemed difficult to get inflation.

Mr. HOLLISTER. What I am trying to get at is, if the gold reserve of the Federal Reserve notes were entirely removed, you say it would have a bad psychological effect and it would shake the people's confidence in some way?

Governor ECCLES. Yes.

Mr. HOLLISTER. What would be the result of that, stagnation of business and increasing unemployment?

Governor ECCLES. If you eliminate any gold requirement for Federal Reserve notes and for Federal Reserve deposits, then you would be completely divorced from gold. Your currency would be purely and completely a managed currency, without any regard whatever to a metallic base. It would be a complete divorcement. Now, if it is desirable completely to abandon gold now, to make all the gold we have serve only as a commercial commodity, then, of course, it would be desirable to abandon all Reserve requirements for Federal Reserve notes. Otherwise, it is desirable to keep them, because it is the only recognition we have of the use of gold as a base for money.

Mr. HOLLISTER. You see, what I am trying to get at is the advantage of collateral behind notes.

Governor ECCLES. That is a very different matter, the question of gold and that of collateral.

Mr. HOLLISTER. Both are some assurance of value.

Governor ECCLES. Why not have collateral back of deposits? Gold is held as a reserve against both deposits and notes. Now, other countries have gold requirements back of their notes, but most have no collateral requirements back of them. They have gold requirements back of their deposits, but they do not have collateral requirements——

Mr. HOLLISTER. But we do not have.

Governor ECCLES. Oh, yes.

Mr. HOLLISTER. It does not require gold.

Governor ECCLES. Or lawful money.

Mr. HOLLISTER. Yes.

Governor ECCLES. But, of course, that was based upon the requirement that lawful money was redeemable in gold.

Mr. HOLLISTER. You think that there is an advantage in retaining that?

Governor ECCLES. I think at this time there is, until it is determined what is likely to develop in the future, with reference to the gold standard, and whether other means of stabilizing exchanges can be developed. To divorce completely our money from gold at this time would seem to me to be rather a costly thing for us to do, while we own 40 percent of the world's gold supply.

Mr. HOLLISTER. You feel, as I understand you to say, that there is some advantage in limiting the total amount of Federal Reserve notes that may be issued by the keeping of the gold requirement?

Governor ECCLES. The keeping of the gold requirement does not put a limit, in and of itself, on Federal Reserve notes. As I explained the other day, the notes which the Federal Reserve System issues are the notes which the customers, the depositors, of the commercial banks require to conduct the business of the country. Only when unlimited hoarding is permitted would there be any possibility of the need of suspending specie payments and gold exports.

The amount of gold, of course, which is held, without regard to the gold held by the Treasury, is considerably more than 100 percent of the amount of notes outstanding. The amount of notes outstanding is as great as we have ever normally used in our business operations.

Mr. HOLLISTER. But the existence of the gold requirement does make a decided limit, beyond which Federal Reserve notes could not be issued?

Governor ECCLES. It is a limit beyond which Federal Reserve notes could not be issued. You would have terrible inflation long before you reached the limit.

Mr. HOLLISTER. Unless further devaluation occurred, in which event you would have still more?

Governor ECCLES. That is right.

Mr. HOLLISTER. Still more gold, against which you could issue more Federal Reserve notes?

Governor ECCLES. Yes.

Mr. HOLLISTER. I would like to ask this question: Is there anything in the existing situation, or what anybody could reasonably predict, that makes this legislation a matter of great present urgency?

Governor ECCLES. I think it is very desirable and necessary that it be passed. I think it is several years late. I think that if legislation of this sort had been passed 4 or 5 or 6 years ago we might have avoided most of the banking difficulties that the country went through.

Mr. HOLLISTER. One of the chief purposes to be accomplished that you see, is the power of checking speculation under the powers granted by this proposed legislation?

Governor ECCLES. Control of speculation is one of the important features. Another is to make a better coordination of the system through the changes in the relationship of the Board to the banks and the governors, combining the governors' positions with those of the chairmen. The eligibility feature is a very necessary and important change in the legislation, in order to make banks feel more free to extend long-term credit.

Mr. HOLLISTER. There are many of the provisions of the Federal Reserve Act, are there not, that ought to be revamped, gone over, and studied pretty thoroughly?

Governor ECCLES. There are quite a number of provisions proposed in title III of the bill.

Mr. HOLLISTER. I realize that.

Governor ECCLES. That go quite a way toward correcting and toward clarifying the existing Federal Reserve legislation. I do not believe that we will ever reach a point in this country where we will have perfection in our banking legislation. We are, of course, in a changing economy and, looking over the past hundred years, we have found that no one has been able to develop a perfect system of money and banking; and I do not believe that this proposed legislation means that we have reached the millenium in banking and in dealing with our banking and money problems.

Mr. HOLLISTER. It comes down to the individuals who are running the thing, finally.

Governor ECCLES. What is that?

Mr. HOLLISTER. I say, it comes down to the individuals who are running the thing, finally.

Governor ECCLES. The individuals who are managing the enterprise are certainly a very important element in any private or public field of activity. The administration can go a long way toward either wrecking or making successful what is done under any legislation.

Mr. HOLLISTER. I asked that because there is a difference in philosophy of government. Some people say there is no need of checks and balances, if you can secure a race of supermen to run things properly. But there is no indication that we are going to have supermen running the banking system any more than in the past, no matter in whose hands it is put.

The CHAIRMAN. You mean there is no such thing as a benevolent despotism?

Mr. HOLLISTER. I think that is very well put. I think that question really answers itself.

With respect to the raising of rediscount rates, the strengthening of reserve requirements, and entering the open market, it has been stated by you and others, with a great deal of justice, that our trouble in the past has been that our so-called " great bankers " have not been equal to the emergency and have not foreseen what was to happen, or, if they did, they did not have the strength to take advantage of the machinery which was available to stop the inflation and boom. Realizing that these men were theoretically the best bankers of their time, are we going to be in any better position by placing the matter entirely in the hands of a Federal Reserve Board, appointed by the Chief Executive? What is there to indicate that the men so appointed, having these supreme powers, would be able to handle them any better than they were handled by the so-called " great bankers " of the past?

Governor ECCLES. There is a great difference between thousands of banks acting independently and a small board charged with the responsibility of monetary control. In the first place, the bankers acting independently have no way of expanding money, and they had no way of stopping the contraction of money, even had they so desired, because they did not have control over the issuance of money, such as is held by the Federal Reserve System. In other words, the independent, private, commercial bank is not a central bank charged with or having central-bank functions, neither has the Federal Reserve Board in the past been charged with the duty of creating business stability. I feel that certainly a board, if given the authority and charged with the responsibility for our monetary policy, is more likely to feel personally that great responsibility and to discharge its obligations and its duty in the public interest than we have had any reason to expect in the past of the banking system, as it has been constituted.

Mr. HOLLISTER. Do you not fear that—and this is a repetition of the question that I asked you a little earlier—that in the event the situation were to create a condition of continued deficits, a time arising when the floating of Government bonds became more and more difficult—would it not be almost impossible for the Federal Reserve Board, constituted as it would be under this bill, to refuse to cooperate with the Treasury in continuing a financial policy which independent bankers might deem was unwise?

Governor ECCLES. I think it would be extremely unfortunate for the bankers if a situation was reached where the Government, having a continuous budgetary deficit, was unable to get the cooperation and support necessary from the Reserve banks and the bankers; for the reason that it would probably mean, under those circumstances, the issuance of currency rather than bonds to pay for the budgetary deficits. It would mean the possibility of the Government taking over the banking system. As I stated the other day, it seems to me that a Congress that can appropriate money to carry out emergency needs, which create deficits, also has the power to create the means of providing that money, in case the existing private system fails to do it. Certainly we would not question that, if we were in war, and the private system failed to meet the demands of Congress in the emergency, the means would be provided otherwise. I think that, in the interest of the banking system, it is important and it is necessary that you have this cooperation in helping to finance the program of the administration in power.

Mr. HOLLISTER. You have just stated that Congress, of course, would have to use its various powers. That is admitted.

Governor ECCLES. Yes.

Mr. HOLLISTER. This bill, however, asks Congress to give to the Federal Reserve Board these powers, which is quite a different proposition; and I ask you whether it is wise to give these powers to a board which undoubtedly would have to be, to a great extent, controlled by the Executive. The question is whether we could afford to give these powers to follow a certain procedure which might be very unwise, from a banking point of view. If Congress were retaining its power, that would be quite a different matter, but it is not.

Governor ECCLES. If I understand your question, it is whether or not I think it is desirable that the Federal Reserve Board, or the Federal Reserve System should be in a position where it could finance a continuing budgetary deficit.

Mr. HOLLISTER. No matter how unwise it might appear.

Governor ECCLES. Yes.

Mr. HOLLISTER. That is, you understand the question?

Governor ECCLES. Yes.

Mr. HOLLISTER. Your answer to that is yes?

Governor ECCLES. Yes.

Mr. HOLLISTER. I meant to follow up the question asked you a little while ago. If the fate of any system depends ultimately upon men, whether or not it was not wiser to include checks and balances?

Has consideration been given to the fact that legislation might be so drafted that, in the event of a rise of a certain percentage in commodity prices or an expansion of deposits over and above commercial loans by certain proportion, or of stock prices, or of capital exports, that then there should be, automatically, rediscount raises, and the reserve requirements strengthened, and open market operations, so that the discretion is not as broad as this bill would give—almost unlimited discretion?

Governor ECCLES. It is not unlimited. The proposal which was made the other day as to what should be the objective confines the responsibilities of the Federal Reserve Board and places upon it a very definite obligation. The proposal was that it should be the duty of the Federal Reserve Board to exercise such powers as it possesses to promote conditions making for business stability.

Mr. HOLLISTER. Exactly. I understand that. But the very point I am raising is that, because of the frailty of human nature, the Board either would not perform its duty or would not be able to do it, and is it not wiser to put some checks and balances in there? Would the Board be gifted with such insight that they would be able to tell——

Governor ECCLES (interposing). In the past, the Board had neither the authority nor the responsibility. That has been the trouble in the past.

Mr. HOLLISTER. The trouble in the past was not the lack of authority or responsibility. The trouble in the past was that they did not see what was coming. No one has intimated that the failure to check the boom was due to lack of authority or responsibility.

Governor ECCLES. I do not know; but certainly there were a good many people who thought they knew what was coming.

Mr. HOLLISTER. They were voices crying in the wilderness.

Governor ECCLES. However, I personally think it would be a great mistake to put into this bill rigid mandatory requirements that may be impossible of accomplishment; and, even if they are possible, they may not be desirable. Even if the attainment of certain mandatory requirements were desirable at the moment it may be that the conditions and circumstances would be such in a year or in 2 years or 3 years that these automatic controls would not be desirable at all.

Mr. HOLLISTER. I note that there has been stricken out in the proposed act subsection (c), section 12A of the Federal Reserve Act, which provides that:

> The time, character, and volume of all purchases and sales of paper described in section 14 of this act as eligible for open-market operations shall be governed with a view to accommodating commerce and business and with regard to their bearing upon the general credit situation of the country.

What was the purpose of taking that out?

Governor ECCLES. Because we do not think that should be the objective of monetary policy. The provision that we are proposing to substitute for it, and which I think is much more desirable, as expressing what should be the objective, is the promotion of conditions conducive to business stability and the mitigation of unstabilizing influences in the general level of production, trade, prices, and employment, so far as may be possible within the scope of monetary action.

Mr. HOLLISTER. That is a pretty big order.

Governor ECCLES. I know. But simply to attempt to provide credit for agriculture, commerce, and industry does not meet the problem at all. Credit is now provided for agriculture, commerce, and industry.

Mr. HOLLISTER. If these powers are granted, if the bill should go through approximately in its present form, what powers of a central bank will the Federal Reserve Board not have, outside of its ownership of gold, or the right to change its value, of course?

Governor ECCLES. It will exercise all the powers of a central bank, so far as monetary policy is concerned, which is very desirable and very necessary.

Mr. HOLLISTER. That is what I am getting at. This bill really makes an entirely Government-controlled central bank.

Governor ECCLES. No; not an entirely Government-controlled central bank. The Federal Reserve System is not a Government-controlled system.

Mr. HOLLISTER. When this bill becomes effective, what powers are there, which the Federal Reserve Board, which is appointed by the President, and the Governor, who is subject to removal by the President—what power hasn't it got?—You say it has the power but is not governmentally controlled?

Governor ECCLES. No; it is not governmentally controlled.

Mr. HOLLISTER. You say it is not governmentally controlled?

Governor ECCLES. The members are appointed for 12 years.

Mr. HOLLISTER. It will be more governmentally controlled than it is at the present time.

Governor ECCLES. The Board will not be more governmentally controlled. The Board will be given more power. What I am contending for is not a governmentally controlled central bank at all. What I am contending for is a central body, charged with responsibility for monetary control, in the public interest. Now, whether it is the Federal Reserve Board or some other board is a thing for Congress to decide. But what I am advocating is that the power and the responsibility for monetary policy be placed in a central body that is charged with the public interest, and if it is felt that the Federal Reserve Board is a political board and will be dominated by political expediency, let us say, rather than public interest, in monetary policy, then, certainly, there should be some changes. But I do not think that the Federal Reserve Board under this legislation should be considered a body that will act in connection with its monetary policies, by reason of political expediency rather than in the public interest.

Mr. HOLLISTER. Is it not true, as a matter of fact, however, that, as a general rule, boards with limited terms, appointed by the Executive, are to a great extent under Executive control, particularly when the chief officer can be removed at will?

Governor ECCLES. I do not think that that is necessarily true. Twelve years is rather a long period for board members. I have suggested, in order to make the board members even more independent, that there be an increase in compensation for future appointive members, and that pensions apply to all members, if they are not reappointed. I think that would give them a degree of independence, under the provision which is suggested or provided for in this legislation.

Mr. HOLLISTER. That is all.

The CHAIRMAN. Well, gentlemen, it is 20 minutes to 1. I suggest that we meet again at 3 o'clock.

Mr. GOLDSBOROUGH. Just one moment. This is not a question of mine, but one of the members called my attention to it. On page 46 of the bill, at the bottom of the page, the second paragraph of section 16, it is said:

> Every Federal Reserve bank shall maintain reserves in lawful money (other than Federal Reserve notes or Federal Reserve bank notes) of not less than 35 percent—

And so forth.

At this time, what is that lawful money—what does it consist of? Do you remember?

Governor ECCLES. There is, first, the national-bank notes, which have just been called; and then there are the greenbacks, $346,000,000; and there are silver certificates. And there is coin, of course, the silver dollar and smaller coins.

Mr. BROWN. Gold certificates could be used also for that purpose.

Mr. GOLDSBOROUGH. Do you remember how much that amounts to—how much that reserve could amount to?

Governor ECCLES. Well, of course, the national-bank notes will soon be out.

Mr. GOLDSBOROUGH. Yes; I know that.

Dr. GOLDENWEISER. I can give you an answer in a few minutes.

Mr. GOLDSBOROUGH. Will you give us that later?

(Recess, 12:45 p. m. to 3 p. m.)

AFTERNOON SESSION

The committee reconvened at 3:15 p. m., Hon. Henry B. Steagall (chairman) presiding.

The CHAIRMAN. Tell us about the amount of money in circulation.

Governor ECCLES. According to Doctor Goldenweiser, the amount of lawful money outside of Federal notes was approximately $2,400,000,000.

The CHAIRMAN. This language excludes Federal Reserve notes and Federal Reserve bank notes?

Governor ECCLES. With the retirement of the national-bank notes, which have now been recalled, the amount of lawful money will be reduced to approximately $1,500,000,000.

The CHAIRMAN. Of what would that consist?

Governor ECCLES. Silver certificates——

The CHAIRMAN. How much?

Governor ECCLES. $702,000,000 the first of the year; silver dollars, $32,000,000; subsidiary silver, $309,000,000; and minor coin, $130,000,000; United States notes, $346,000,000. The national-bank notes, on January 1, amounted to $888,000,000, and Federal Reserve notes amounted to $3,520,000,000.

The CHAIRMAN. Federal Reserve notes are excluded?

Governor ECCLES. Yes. After the call of the national-bank notes, there will be $1,500,000,000 lawful money outside of Federal Reserve notes.

Mr. SISSON. I should like to clear up or correct a statement that I made this morning which has reference to an observation of Mr. Hollister. He made the statement, in substance, that it was well settled by the Supreme Court of the United States that the President has the power arbitrarily to remove any administrative or executive officer appointed by him. I want to modify that in this way: It is my understanding that in every instance where the question has been raised as to the power of the President arbitrarily to remove any executive or administrative officer appointed by him, where that question has been decided by the Supreme Court the Court has upheld the power of the President so to do. Mr. Hollister, very likely with some reason, says that is not settled. There is, of course, as we know, a case before the United States Supreme Court involving that question, which case has not been decided. My own opinion is that at any time that question is decided by the United States Supreme Court that power of the President will be upheld. In view, however, of the fact, that it is not entirely conceded, at least it seems to me, as the chairman this morning suggested, that it becomes of some importance to the committee to decide whether the language recommended by Governor Eccles in this bill should be contained in the bill. Therefore, that question does become of some importance here. It appears to me, aside from the reason that the chairman advanced, that it becomes of some importance to have it in the act, so that, in the light of experience, it might obviate a contest in the future. I think that any limitation upon the power of the President in this regard would be unconstitutional—that is, if we attempted to say that he shall not have the power—but for the reason stated by the chairman and also in the interest of clarity, as Governor Eccles has said, and also that it might obviate any question being raised about it in the courts, if we believe that this should be a national body in which there should be some unity of purpose between the administration and the body in control of the monetary policy, it seems to me that at least this committee should decide it while considering the bill. I myself favor the language recommended by Governor Eccles.

I think that is all I have to say.

The CHAIRMAN. Mr. Brown, do you desire to ask questions?

Mr. BROWN. I should like to ask Governor Eccles what the present policy of the Federal Reserve Board is relative to open-market operations.

Governor ECCLES. The open-market committee is composed of the 12 governors. The law recognizes it as their responsibility to intiate a policy and to submit recommendations to the Board for its approval, disapproval, or suggestions; so that the law as now constituted does not require the Federal Reserve Board as such to adopt an open-market policy; except, as I understand it, in giving their approval or disapproval to the policy initiated by the governors' committee, they are required to take into account the credit needs of agriculture, commerce, and industry.

Mr. BROWN. Under the present section B of 12–A you are given practical control of open-market operations, are you not?

Governor ECCLES. In the present law?

Mr. BROWN. Under present law.

Governor ECCLES. Under proposed amendments?

Mr. BROWN. No; under present law. Section B of 12–A provides that—

> No Federal Reserve bank shall engage in open-market operations under section 14 of this Act except in accordance with regulations adopted by the Federal Reserve Board. The Board committee from time to time shall constitute, adopt, and transmit to the committee and to the several Federal Reserve banks regulations relating to the open-market transactions of such banks and the relations of the Federal Reserve System with foreign-controlled or foreign banks.

It seems to me that the power to regulate there is the power to control. I addressed my question having in mind that you are asking us to vest complete authority which will be largely, I think to a greater extent than at present, under the control of the Federal

Reserve Board; and I think it would be interesting to Members of Congress, and particularly to this committee, to know what your policy would be under present conditions. I assume it is the same policy we have at the present time.

Governor ECCLES. I cannot speak for the Federal Reserve Board as to what the policy of the Board would be if this legislation is enacted. That would naturally be a matter that the Board would have to determine.

Mr. BROWN. Do you not think it is fair for us to ask what you would do if given this power under present conditions? It seems to me that we ought to know, that Congress ought to know your attitude as chairman of the Board.

Governor ECCLES. I can speak only for myself with reference to the matter. I cannot speak for other members of the Board, who would be just as independent in exercising their judgment as I would try to be.

Mr. BROWN. When I say "your" I am referring directly to you.

Governor ECCLES. Yes; I understand. Under present circumstances there is very little, if anything, that can be done.

Mr. GOLDSBOROUGH. You mean you cannot push a string.

Governor ECCLES. That is a good way to put it, one cannot push a string. We are in the depths of a depression and, as I have said several times before this committee, beyond creating an easy money situation through reduction of discount rates and through the creation of excess reserves, there is very little, if anything that the reserve organization can do toward bringing about recovery. I believe that in a condition of great business activity that is developing to a point of credit inflation monetary action can very effectvely curb undue expansion.

Mr. BROWN. That is a case of pulling the string.

Governor ECCLES. Yes. Through reduction of discount rates, making cheap money and creating excess reserves, there is also a possibility of stopping deflation, particularly if that power is used combined with this broadening of eligibility requirement.

Mr. BROWN. Does not a Federal Reserve bank have two main functions? Eliminating the temporary loans we provided for last year and other various forms of aid to all banks and industries, are not the main functions of a Federal Reserve bank, first, rediscounting of paper turned in by the member banks?

Governor ECCLES. Eligible paper.

Mr. BROWN. And, secondly, to engage in open market transactions, which, as I understand, relates to the buying of warehouse certificates and other evidences of property back of indebtedness throughout the country as a whole and not confined to the particular Federal Reserve district?

Governor ECCLES. It is largely the purchase of Government bonds.

Mr. BROWN. Do you not engage in the purchase of warehouse certificates?

Governor ECCLES. Bankers' acceptances.

Mr. BROWN. Sometimes you do and sometimes you do not. Is not that a question which the open-market committee decides whether you shall engage or not in that line of work?

Governor ECCLES. The open market committee determines whether or not it shall purchase or sell Government bonds and bankers' acceptances.

Mr. BROWN. Under section D of 12-A of the present law you cannot compel a particular Federal Reserve bank to engage through your open-market committee or Federal Reserve Board in open-market operations, can you?

Governor ECCLES. That is right.

Mr. BROWN. Under the proposed bill is it your idea that such authority will vest in the open-market committee?

Governor ECCLES. That is right.

Mr. BROWN. In other words, you feel that it is proper for the Federal Reserve Board to say to a Federal Reserve bank that it shall engage in the purchase of Government bonds and bankers' acceptances?

Governor ECCLES. That is right. The way it is done is through the system account. The holdings are largely prorated to the banks in relation to their size and their own reserve situations.

Mr. BROWN. Under the second portion of the present bill, section 12-A, it really does not seem to me that it gives you authority to compel banks to engage in open-market operations. I do not find anything in there requiring them to do so. It says that "they shall conform open market operations to the provision hereof." I do not think it provides that they shall engage in open-market operations against the wishes of their own board of directors.

Do I understand that you have proposed an amendment to section 205?

Governor ECCLES. Do you mean additional amendments to the bill that was introduced?

Mr. BROWN. Yes.

Governor ECCLES. Yes.

Mr. BROWN. Is there any language in your amendments that makes it obligatory upon the Federal Reserve banks to engage in open-market operations if they do not want to do so.

Governor ECCLES. It was expected in the original legislation that, where there was a committee of five proposed, the governor and two other members of the board, and two governors of reserve banks, the reserve banks would be required to participate in the purchase of securities or bills as determined by the open-market committee.

Mr. BROWN. Does your general counsel think that the language of the act as you propose is sufficiently broad to enable the Board to so command the Federal Reserve banks? It does not seem so to me. If it is desirable that such an authority should be effected, I think the language of the bill should be broader.

Governor ECCLES. It was intended to be; whether it is or not I do not know.

Mr. WYATT. The bill as introduced contains this language, on page 45, lines 3 to 9: "The committee from time to time shall consider, adopt, and transmit to the Federal Reserve banks resolutions setting forth policies which, in the judgment of the committee, should be followed with respect to open-market operations of the Federal Reserve banks, and the Federal Reserve banks shall conform their open-market operations to the provisions thereof." That means that the

Federal Reserve banks must conform their open-market operations to the provisions of the resolutions adopted by the committee.

Mr. Brown. Suppose the bank says, "We have only sufficient funds, in our judgment, to take care of the necessary rediscounting of our own member banks and we do not desire to engage in open-market operations." Is there anything in that law to compel them to so engage in open market operations?

Mr. Wyatt. Suppose that the committee adopts a resolution directing that the banks shall purchase a billion dollars worth of Government bonds and that each bank shall buy its pro rata share of such bonds. How can they conform to the provisions of that resolution without each bank buying its pro rata share?

Mr. Brown. By simply refusing to engage in open-market operations and confining their business to rediscounting with its own member banks. That is a logical conclusion, I believe.

Mr. Wyatt. I think the point you raise is a good one and that the bill should be clarified so as to eliminate any doubt on the point.

Governor Eccles. The intention is to make it mandatory, otherwise it would be impossible effectively to carry out any monetary policy.

Mr. Brown. I do not mean to say that I approve the policy, because I am inclined to agree with some things Mr. Hollister indicated this morning, among them being that such control of Federal banks and district banks is more than we ought to give. I want to point out that it did not seem to me that your statement at the beginning of these hearings said it was desirable.

Governor Eccles. It seems to me that when we speak of centralizing control outside of the banks we fail to recognize the peculiar structure of our Federal Reserve banking system as contrasted with central banks elsewhere in the world. If we had here, which may have been the more desirable arrangement, one bank with 12 branches, or as many branches as may be necessary to serve the country, then the board of directors would be charged with the responsibility of the monetary policy as well as the responsibility of providing credit to business, agriculture, and industry.

Mr. Brown. Instead of that kind of system we have 12 separate, distinct banks.

Governor Eccles. Yes.

Mr. Brown. With 12 different capital set-ups varying in amounts of surplus.

Governor Eccles. Capital and surplus do not determine the ability to lend or to participate.

Mr. Brown. It determines the amount of money they have available.

Governor Eccles. No; they create money.

Mr. Brown. Only based upon the assets?

Governor Eccles. Only based upon the gold limits.

Mr. Brown. So that you are attempting here to give such control to the Federal Reserve Board similar in authority to that of a board of directors over one bank with 12 branches?

Governor Eccles. But, actually, so far as open-market policy is concerned, if we recognize the need of a monetary policy, it must be carried out in the public interest. It cannot be left to the 12 banks, acting independently.

Mr. Brown. I grant that. But I do not agree with you that your control relates only to open-market operations. You are establishing under this law, or, at least, you are given the right to establish, general rules for the eligibility of paper for discount.

Governor Eccles. That is correct; but that does not mean that the Federal Reserve Board has anything to do with the passing upon the loans which are made. The Board has only the responsibility of making rules and regulations with reference to the conditions under which Federal Reserve banks can rediscount for or lend to member banks; and its power is strictly limited, according to the present statutes, to permit loans only upon certain specific types of paper, of which there is very little in existence.

If the Board were given more discretion, the system would become more flexible. The proposed amendment in no way gives the Board power to compel the Reserve banks to make the loans. It is expected that the Reserve banks will be just as independent as they have been with reference to their autonomy in matters of regional interest.

Mr. Brown. Principally rediscounting?

Governor Eccles. Not only in rediscounting, but also in all relations with member banks. The examinations are all conducted through the Reserve banks. The Federal Reserve Board depends upon the Reserve banks to carry on all of the relationships with the member banks and with the communities. We are only providing here for the placing of responsibility in a comparatively small body that can be charged with the public interest, to deal with monetary policy. That seems to me to be absolutely essential, if we expect to avoid in this country the dangers inherent in a purely banker control over the creation and the extinguishing of credit. We have had experience with that, and we know that it does not work very satisfactorily. Whether it will work any differently under the proposed arrangement, time alone will determine. But it does seem to me that to deal with the monetary needs of a Nation on other than a national basis and with any other purpose than that of serving the public interest is to invite disaster.

Mr. Brown. In that connection, I note that by section 208 of the pending bill, you repeal the provisions of the banking law, I think, of 1933, by which we authorized the issuance of Federal Reserve notes based upon the eligible paper that had been turned over to the Federal Reserve banks by the member banks. And it was under the authority of that section that the President recently extended the right so to do from March 3, 1935, on for 2 years. That was done 2 or 3 weeks ago, was it not?

Governor Eccles. That is right.

Mr. Brown. Now you are repealing that provision of the law?

Governor Eccles. That is right.

Mr. Brown. And you propose to substitute section 16 of the law, I presume, where the Federal Reserve Board have practically complete control of that matter of the issuance of new money. Is that right?

Governor Eccles. As I understand what you mean, the Emergency Banking Act referred to permitted the Federal Reserve banks to secure Federal Reserve notes with Government bonds, in addition to commercial paper. The period of time during which that could be done was extended, very recently, for a period of 2 years.

Mr. Brown. That is right. Governor Eccles, not only Government bonds, but notes, bills of exchange, and acceptances were eligible as collateral for the issue of Federal Reserve notes, were they not?

Governor Eccles. Yes; that is right.

Mr. Brown. Now we are repealing that section of the law.

Governor Eccles. Because we are making it unnecessary to put up any collateral with the Federal Reserve agent for the purpose of securing Federal Reserve notes. It adds nothing whatever to the value of the notes, as I have explained here on several occasions; and it is an unnecessary requirement. No central bank requires it except that it is still adhered to in the Bank of England; but no other bank in the world requires it, and the amount of Federal Reserve notes that are used has no relationship whatever to the collateral requirement. Federal Reserve notes may be required in great amount when there are practically no discounts. The amount of the rediscounts by member banks with the Reserve banks has no direct relationship to the amount of Federal Reserve notes required. Only the people of the country can determine the amount of currency is required by the drawing of currency instead of checks.

Mr. Brown. It seems to me that there is a considerable disagreement upon that matter of policy. We specified in the Banking Act of 1933 certain types of commercial paper that were eligible as collateral for the issue of Federal Reserve notes, the issue of new money. Now, you repealed that, and, under section 16, you cover it all by one sentence: "Federal Reserve notes shall be issued and retired under such rules and regulations as the Federal Reserve Board may prescribe and shall be legal tender for all purposes." Now, is it not a fact that when people borrow money from banks it shows that they are engaging in business, that they need credit? Their notes are turned over to the Federal Reserve banks and money issued.

Governor Eccles. No.

Mr. Brown. It was under the Banking Act of 1933.

Governor Eccles. No currency is issued as a result of that transaction at all.

Mr. Brown. I am glad to hear that, because we have heard a great deal over in the House about money being issued. You say there is none issued?

Governor Eccles. No. The borrowing by a member bank from the Federal Reserve bank does not determine the amount of currency that the member bank or the banks as a whole or the public as a whole may require or use.

Mr. Brown. Well, was not that law passed for the purpose of supplying the need of banks for currency to pay their depositors when they demand it?

Governor Eccles. No; 40 percent of the amount of notes outstanding must be secured by gold certificates and 60 percent was required to be secured by commercial paper. As a matter of fact, there was so little commercial paper that it was impossible to provide the 60 percent; and therefore at one time there was over a billion dollars of gold, in addition to the 40 percent gold reserve, that had to be used as a substitute for the lacking commercial paper. In other words, it was used to help make up the 60 percent; because there was not sufficient commercial paper available. There is not the quantity of commercial paper in the country upon which to——

Mr. Brown (interposing). How about the individual banks? Let us take a bank with a capital of a million dollars and a deposit liability of 10 million dollars, and it has commercial paper that would be eligible under this section of the Banking Act of 1933. I think this committee supposed that if that bank wanted to convert that commercial paper into cash it would be able to do so.

Governor Eccles. It still can do it under this. There is no change in the law proposed that prevents that. That bank can still go to the Reserve bank and can take that commercial paper and can get credit in its reserve account with the Reserve bank and can draw down currency to the extent that it needs——

Mr. Brown. That is, by rediscounting its notes?

Governor Eccles. Or, as we are proposing here, if it has not the eligible paper and it has other sound assets.

Mr. Brown. I may be dense on this, but it seems to me that you are throwing out the basis for the issue of currency by issuing currency upon the resolution of the Federal Reserve Board instead of basing the issue upon the assets that are in the vaults of the member banks of the country and the demand for money on the part of the depositing public.

Governor Eccles. Let me explain that again.

The Federal Reserve banks have two kinds of liabilities—three with their capital and surplus: Deposit liability, note liability, and the capital and surplus liability. Loans and discounts and investments, lawful money, and gold certificates are the assets of the Reserve banks.

The member banks which carry their reserves with the Reserve banks ask the Reserve banks for currency only to the extent that they have deposits with the Reserve banks. They must maintain a minimum reserve balance with the Federal Reserve banks, and when they want currency they must acquire additional balances to which they can charge the currency withdrawn. In order to get that, they may send paper to be discounted with the Reserve banks.

The member banks supply currency to their customers, to their depositors, when the depositors want to draw out their deposits, or a portion of them, in currency; and if a bank reaches a position where the customers have called upon the bank for currency and it is unable to meet that call, that bank closes. Many of the banks in this country were unable to meet that call, not because they were not sound but because they did not have the eligible paper with which to go to the Reserve bank and get credit; and therefore, because of the fact that the banks were unable to do that, those banks were compelled to close.

As the number of banks closing increased, the demand for currency increased, not because of the activity of business but because of hoarding; and the very fact that the banks were unable to go to the Reserve banks with sound assets to meet the demands of these depositors meant finally a banking collapse. Had the banks been able to pay their depositors in currency, the depositors would not have wanted the currency, as was demonstrated after the bank holiday.

Mr. Brown. Does it not come down then to this question, or to this situation: That the reason for the collapse of the banks that were actually solvent, but that had so-called "frozen assets" or "frozen loans"——

Governor ECCLES (interposing). Deflation created a frozen condition.

Mr. BROWN. But it was a lack of liberality in regard to the eligibility of paper for rediscounting that caused a good deal of the distress.

And, by your next section, 206, you seek to liberalize those rediscounting rules?

Governor ECCLES. That is right.

Mr. BROWN. Now, that brings me to the meat of my discourse, What are those rules going to be? That is the same question I asked you regarding the open market operations. I think this committee and this Congress ought to know what your own idea, Governor Eccles, is and what those rules of eligibility are going to be. I recognize that the law sets a standard as to real-estate loans.

Before you make your answer let me get one of my favorite objections to Government practice in the past with regard to those notes stated on the record. I am thinking of a small national bank in the country. Now, the Comptroller's office has a rule by which certain collateral listed on the New York Stock Exchange, or other large exchange, is recognized as collateral and the paper which that collateral secures is eligible for loans. We have tens of thousands of small manufacturing concerns, whose securities are good, but which are not listed upon the New York Stock Exchange or the Detroit Stock Exchange or the Chicago Stock Exchange, or any other large exchange. Their statements show them to have plenty of cash assets back of those securities. But, because of the rules of the Comptroller's Office—and I am not very familiar with the examination made by the Federal Reserve banks, but I presume they are the same—the collateral of those small concerns does not stand nearly as well for loans as does the stock of large concerns. Now, it seems to me that that condition is unfortunate for the small banks and the small businesses; and I am wondering, with respect to that situation, whether or not there is going to be any liberalization regarding the eligibility of that type of paper as collateral for loans rediscounted with the Federal Reserve banks.

Governor ECCLES. The matter that you refer to has reference to the treatment of certain types of loans in banks by the Comptroller's office.

Mr. BROWN. Well, and by the Federal Reserve Board's examiners.

Governor ECCLES. The Federal Reserve Board's examiners accept the Comptroller's examinations for all national banks. They make no independent examinations. That would be only a duplication. The Comptroller's examinations are accepted by the Federal Reserve banks.

Mr. BROWN. That would apply to thousands of member State banks.

Governor ECCLES. There are only 900 State banks, and these are examined by the Reserve banks. But there is no prohibition either under the law or in the regulations, to my knowledge, against banks making loans secured by other than listed collateral, either stocks or bonds.

Mr. BROWN. You say there is none?

Governor ECCLES. There is no prohibition either in the regulations or in the law against them.

Mr. BROWN. There is in the practice.

Governor ECCLES. No; not in practice.

Mr. BROWN. I disagree with you.

Governor ECCLES. There is none in practice. The question is, of course, to establish values back of loans which are secured by unlisted collateral. Now, if collateral is listed it becomes much easier to establish whether or not that particular loan is adequately secured than is the case where the loan is secured by some local security that it is very closely held and has no market ability. It becomes difficult for an examiner to determine whether or not a loan is adequately and safely secured for that reason, but——

Mr. BROWN (interposing). Governor Eccles, don't you know it to be a fact that, with regard to the bonds of concerns throughout the country, the Comptroller's office has refused to approve bonds that are not listed on the New York Exchange or some other large exchange so as to be readily marketable?

Governor ECCLES. Refused to accept them for what?

Mr. BROWN. As loans.

Governor ECCLES. To secure loans?

Mr. BROWN. Yes.

Governor ECCLES. There is no prohibition in the law.

Mr. BROWN. There is no prohibition in the law, but the practice is to decline to approve such loans.

Governor ECCLES. There is no such requirement.

Mr. BROWN. What I am wondering is if you are going to be a little more liberal on this?

Governor ECCLES. I know that there are literally thousands of bond issues, municipal issues, all kinds of issues, which are held by banks; and, so long as those bonds are not in default, and their payments are being met——

Mr. BROWN (interposing). I will except municipal bonds.

Governor ECCLES. There is no restriction or prohibition against the holding of those bonds. It is true that the examiners make an effort to establish the value back of them, in the absence of a quoted market, which is very desirable and necessary, in order to determine whether or not the loan which the bonds or stocks secure, or the bonds which are held directly, are worth what they purport to be worth.

Now, in the case of a local stock issue or local bond issue, there is, naturally, the problem of attempting to determine the value of that security.

I know, in my own banking experience, over a period of 20 years, that we have had no trouble with the Comptroller's office with reference to matters of that sort; and many loans have been made on local securities, and various bond issues have been purchased that were not listed. The main thing is to have available and be able to give to the examiner information with reference to the local company whose stock is put up as collateral or whose bonds are put up as collateral. Such information is necessary to establish the value of the collateral which secures the note in question.

I find that most of the trouble is that in accepting local securities, stocks or bonds, banks fail to provide sufficient information to enable the examiners to substantiate the value of the securities which they have taken. It is lack of information.

Mr. BROWN. I want to say to you that it is my judgment, then, that the attitude of the Comptroller's office has been very much more severe in the Chicago district than it has been in the San Francisco district or the Salt Lake City district, because that rule was enforced when the banks were reorganizing in Michigan and Ohio in 1933 and 1934; and they did insist that those bonds be listed bonds.

I am glad that you have stated in the record what I think is a more liberal policy regarding local stocks as collateral, as well as local bonds.

I have two or three other questions, but I would like a little further answer to my question as to what other classes of paper, in your judgment, the Federal Reserve Board should determine to be eligible paper, for rediscount in the Federal Reserve banks.

Governor Eccles. It would be my personal opinion—I cannot speak for the Board—that very broad rules and regulations should be made with reference to this subject and that a broad discretion should be left to the Federal Reserve banks. I think that, in matters of local credit concerning each Federal Reserve district, if they are given discretionary power, the Federal Reserve banks can be relied upon to make only sound loans; and I do not think, as a practical matter, that there should be a lot of limitations and restrictions with reference to what may be considered sound paper.

Mr. Brown. Well, for instance, as I understand it, 3-months' paper has been rediscounted, one renewal allowed, and after that it was taken out of the class of commercial paper that was eligible for discount. That was a general rule in the Minneapolis and Chicago districts and always enforced. Now, that was a general rule, whereas there are a great many businesses that take a year for a turnover; and they were limited there to 6 months' credit. Now, would your own personal disposition be to so liberalize the rule, if what I say is true of that, so that paper for 9 months or 12 months could be taken?

Governor Eccles. I would not like to say, under normal conditions, that paper should be taken on a bills-payable basis, for longer than a 6-months' period, because it is always an easy matter to renew the paper.

Mr. Brown. Well, what would you say?

Governor Eccles. That would be up to the Reserve banks, the question of renewal would be up to them. Certainly it would be bad for the banking system as a whole to permit continuous borrowing from the Reserve banks by the member banks. Continuous borrowing from the Reserve banks by the member banks could only mean that the member banks were lending money and rediscounting or borrowing because of the difference in the rate that they paid the Reserve banks and the rate at which they were able to loan. However, I can well imagine a situation where you would have a crop failure, drought conditions, catastrophes, and so forth, where it would be very necessary for the Reserve banks in those areas not to expect liquidation in that particular area; and it would be desirable to carry the loans over for an additional time. Past experience and the attitude of member banks toward borrowing indicate that we can be assured that member banks are not going to borrow from the Reserve banks except for short, seasonal periods of time, unless an emergency develops, which may require that they borrow for longer periods of time; and that is the purpose of this legislation.

Mr. BROWN. But I am talking about the small business man now. It happens that in my district, in one of the large resorts of Michigan, the practice in the merchandising business there is for a merchant to buy his goods in December. If he can pay for them then he gets a substantial discount. He will not get his return on the bulk of those goods until the following August. Now, it seems to me that it is just as legitimate for that purpose to get a 9 months' loan, in that type of business, as it is in certain other types of business, where the turnover is made in 3 months, as it is in the grocery business; and that he should be accommodated for the 9 months' period. Now, do you have in contemplation, when you lay down these rules and regulations for eligibility, such a situation, and that the normal course of a business of that character should be accommodated?

Governor ECCLES. There is nothing to prevent the individual banks from making loans of that sort today.

Mr. BROWN. I am talking about rediscounts.

Governor ECCLES. Of course, there is not any rediscounting today. There are excess reserves of tremendous amounts.

Mr. BROWN. There is, of course, in some banks.

Governor ECCLES. That is true of the country as a whole. There is practically no borrowing from the Reserve banks, and most banks have excess reserves. In addition to that, if they had to borrow, they would borrow on their Government bonds; because they would be the easiest assets upon which to borrow.

Mr. BROWN. Well, I take it that, on all these questions, you are very much adverse to stating what, in your judgment, the policy of the Federal Reserve Board will be in regard to the rediscounting of paper.

Governor ECCLES. I think——

Mr. BROWN (interposing). But, with the utmost good humor, I do not think you have told me yet of any particular liberalization that you propose to make in the rediscounting rules.

Governor ECCLES. Rediscounting rules today are not made by the Board.

Mr. BROWN. But they will be under this bill, if it becomes a law.

Governor ECCLES. Yes; but the law today states that only certain specific types of paper, which are known now as eligible, short-term, self-liquidating paper, are eligible. Now, this proposed legislation broadens the power to a point where the Reserve Board is able to make rules and regulations which will permit Reserve banks to make advances against any sound assets.

Mr. BROWN. What I am trying to find out is, what is your idea as to what they should do?

Governor ECCLES. I would leave that up to the Reserve banks. I would favor broad enough rules to leave discretion to the Reserve banks in passing upon credit. You might put a limitation of 6 months advances on a bills-payable basis. To make rules and regulations in Washington as to what would be adequate security for advances to member banks would be rather a complicated procedure and would certainly be inadvisable and unnecessary.

Mr. BROWN. But the banks are given the authority, under the law, to make those rules and regulations.

Governor ECCLES. Which banks?

Mr. BROWN. The Federal Reserve banks and the Federal Reserve Board are given that authority.

Governor ECCLES. That is right.

Mr. BROWN. To determine the maturities and other matters.

Governor ECCLES. That is right.

Mr. BROWN. Now, what I am trying to find out is what your present attitude is toward the eligibility of the various classes of paper.

Governor ECCLES. I am just saying that I would permit the Reserve banks to loan on any and all assets, real-estate mortgages, collateral loans, bonds, or other assets, which they considered sound, on such a basis as they considered sound.

Mr. BROWN. And with what maturities?

Governor ECCLES. My personal opinion, without giving any thought or study particularly to the problem, would be that 6 months advances on a bills-payable basis should be adequate. That does not necessarily mean that a bank, at the end of 6 months, could not renew for another 3 months or 6 months. But I do not believe that, on a bills-payable basis, for advances, that 6 months would be working any hardship upon the banks.

But in case of a rediscount, you would have maturity based upon what would be considered the period of natural liquidation. For instance, agricultural and livestock loans are 9 months, as it is considered that the underlying transactions take that length of time. Those are rediscountable now. Collateral loans, loans which are not considered rediscountable and are not self-liquidating, through the completion of business transactions, such as loans against mortgages or loans against bonds, would likely only be made in cases of emergency, in cases of deflationary situations, and they would not be made in the natural course of business except to a very limited extent. Certainly, the Reserve bank should be given the power to enable a bank that has an unusual shrinkage of its deposits, and yet has sound assets, to get credit on them until it can carry out a normal process of liquidation, without closing and without bringing about an undue deflation. That is the purpose of this legislation.

The CHAIRMAN. And you mean sound assets made within the limitation of the law establishing the rules under which those loans should be made?

Governor ECCLES. Yes.

The CHAIRMAN. In other words, if the borrowing bank had made those loans within the law?

Governor ECCLES. That is right.

Mr. BROWN. Now, getting back to commercial paper—expressed in my poor way—should not the rule be that the discount should be permitted for such length of time as would cover the normal period from production to sale of the goods?

Governor ECCLES. I think that is what is contemplated under the law now.

Mr. BROWN. Personally, I would like to have you say that you feel that way about it yourself. In other words, that you feel that that is the kind of rediscounting that you, as a member of the Board, would favor.

Governor ECCLES. You mean in case the Board is making rules with reference to rediscounting?

Mr. BROWN. Yes.

Governor ECCLES. What do you have in mind, what particular item?

Mr. BROWN. Let us take something that you and I know something about. Suppose we did not have the system of handling sugar by warehouse receipt. It takes from September, generally, to August, in Michigan, to bring about the cycle from payment to the farmer for the production of sugar beets, to the final payment for the sugar and collection. Now, it seems to me that the period of discounts should be that length of time and that notes for that period should be eligible for rediscount.

Governor ECCLES. Do you mean on a straight bills-payable basis?

Mr. BROWN. Straight bills-payable basis; yes.

Governor ECCLES. As a general rule, manufacturing companies, such as sugar companies and other companies, borrowing from the banks, seldom want to borrow for a period longer than 6 months, or, maybe, even 90 days, because they are constantly reducing the outstanding loans.

Mr. BROWN. That is right.

Governor ECCLES. And they do not know exactly by what amount they are going to be able to reduce it; and, hence, they do not want to rediscount up to the maximum amount of the financial requirements for a period of 9 months, because it may be that they can pay a substantial amount in 3 months and renew the balance. I believe that, even if a 9-month rediscount were permitted in that type of transaction, there would be very few that would use it.

Mr. BROWN. But you might find one fellow that would want to do it.

Governor ECCLES. I see no objection to that, if the condition of the company is such that an open line of credit is desirable, and they were willing to borrow for 9 months, and the bank should take 9 months' paper. There would be no reason for the Reserve bank not taking such paper as quickly as they would take livestock paper.

Mr. BROWN. In other words, you feel that no such rule should be established by the Federal Reserve Board as would prevent the taking of paper having such maturity or length of time as would cover the normal period from production to final consumption, sale, and collection.

Governor ECCLES. It would seem to me that that should be permitted. If a borrower wanted to borrow for that length of time and the credit was good credit, and the member bank was willing to accept that type of credit as being self-liquidating commercial credit, there should be no objection and the Reserve bank should be permitted to take that type of loan from the member bank.

Mr. FORD. Governor Eccles, you used the phrase there "good credit." Now, is not the Federal Reserve bank in a district, when a member bank comes to the Reserve bank with its assets, going to be reasonably certain that the assets offered are sound?

Governor ECCLES. I think there is no question about it.

Mr. FORD. Then, I think that the question that Mr. Brown brings up is largely a matter of local prestige, based on the actual knowledge of the member bank that makes the original loan, of the soundness of the person who makes the loan, and it can back him up if it has to go to the Federal Reserve bank.

Mr. BROWN. Up to the present time they have held them down to the 3-months' period, which I think is too short.

Governor ECCLES. I think that is largely due to the member banks, rather than to the Reserve banks. The member banks prefer 90-day paper, because they have seen in the past the very wide fluctuation in the value of commodities against which they loan. In loaning for a period of 9 months on any commodity, there is room for very wide fluctuations in prices; and it is my belief that the member bank passing on the credit, for its own protection, will adhere to 90-day paper, and renew; because, after all, even if it borrows from the Reserve bank, it is responsible for the obligation, and the Reserve bank is not making the loan directly to the original borrower.

Mr. FORD. Would there be anything wrong with this type, or would there likely be a refusal to discount this type of paper: A man borrows $20,000 for 90 days; at the end of 90 days he pays $8,000 back; there is still $12,000 left. An emergency arises, where the local bank has to go to the Federal Reserve bank to rediscount; would there be anything against that remaining $12,000, if it were sound, if it is part of the renewal note?

Governor ECCLES. Not the fact that it is a renewal note.

Mr. FORD. Does it not give it the status of the original?

Governor ECCLES. Yes. In fact, that is what is usually done with commercial paper. It is paid off by renewals.

Mr. BROWN. The rule has been in the Minneapolis district, at least, that they would allow one renewal, and at the end of 6 months you would have to pay back.

Governor ECCLES. The member banks did that.

Mr. BROWN. The member banks would.

I want to discuss with you just a moment a subject that I took up with Mr. Crowley, Chairman of the Federal Deposit Insurance Corporation, this matter of bank examinations. It seems to me that we have too many governmental authorities examining banks. We have 3 at the present time, and 4 if we include the Reconstruction Finance Corporation, which, I grant, is a temporary organization. We have the Federal Reserve banks, the Comptroller's Office; the Federal Deposit Insurance Corporation has now asked for authority, in the present bill, to examine national and member State banks.

I want to ask first if the Federal Reserve Board has followed the policy of appointing only such examiners as are designated by the Comptroller of the Currency? Now, I will explain that. Under the first section of the law on bank examinations, it appears to have been the policy of the act to require that Federal Reserve bank examiners should be designated by the Comptroller of the Currency. Then, under a section or so later, it is provided that the Federal Reserve authorities themselves may designate examiners.

Now, what I am wondering is whether the general practice has been to get examiners designated by the Comptroller of the Currency or to use the authority conferred in the second portion of the law, which is section 483 of the United States Code, annotated. The first section I referred to is section 481.

Governor ECCLES. I cannot speak as to what the Reserve Board may have done in the past. I am not familiar with it. But it is my understanding that the Federal Reserve Board chooses its own examiners entirely. The Examining Division of the Federal Reserve Board deals, of course, with the member State banks. The Comptroller's examinations are accepted for national banks.

Mr. BROWN (interposing). For the national banks?

Governor ECCLES. There is no point, of course, to duplications of examinations.

Mr. BROWN. Well, am I right in assuming, then, that the Comptroller is not examining member banks of the Federal Reserve System who are not national banks?

Governor ECCLES. That is correct. They are not examining them, and the Federal Reserve Board is not examining the national banks.

Mr. BROWN. No.

Governor ECCLES. The examination reports are available and are given to the Federal Reserve banks, so that they can get any and all information that they desire from the Comptroller's office, with reference to national banks, which, of course, are members.

Mr. BROWN. The statute says that the Comptroller of the Currency shall appoint examiners who shall examine every member bank. Evidently the law is not being followed in that respect. I do not have any objection to it.

Governor ECCLES. Do you know whether that question has ever come up, Walter?

Mr. WYATT. The original Federal Reserve Act required the Comptroller to examine all members banks; but section 9 was amended by the act of June 21, 1917, so as to say that State member banks shall not be subject to examination by the Comptroller of the Currency but shall be subject to examination by examiners selected or approved by the Federal Reserve Board.

Mr. BROWN. You will find, two sections later, that special examinations are provided for by the Federal Reserve Board, but I do not believe that the first section was ever repealed. But that is an academic question; I am not particularly interested in that. But I believe that the examinations should be conducted by 1 bureau of the Government and not by 3.

Governor ECCLES. So do I.

Mr. BROWN. And I think it is a good time to change the law in that respect. The expense of the Government examination of the bank is borne by the bank?

Governor ECCLES. It is.

Mr. BROWN. Not only the examination by the Federal Reserve Board but the examination by the Comptroller's office?

Governor ECCLES. That is right

Mr. BROWN. Take a community having 3 banks, 1 a national bank and 2 member State banks, and you have a great deal heavier expense upon that bank by reason of a trip by the national bank examiner and then a subsequent trip for the examination of the other 2 banks by the Federal Reserve bank examiner; and it seems to me that it is an unjust and unnecessary expense upon the banks.

Now, the Federal Deposit Insurance Corporation is the only all-inclusive bureau with respect to the examination of banks in the Government, is it not?

Governor ECCLES. I do not understand that the Federal Deposit Insurance Corporation was given the power to examine national banks.

Mr. Brown. Yes; it is under this bill. They may, with the consent of the Comptroller of the Currency and with the consent of the Federal Reserve Board, examine any bank.

Governor Eccles. Yes.

Mr. Brown. National banks or member State banks.

Governor Eccles. Yes.

Mr. Brown. I say " an all-inclusive bureau ", with respect to the examination of banks, because of the fact that they, of course, include all national banks, all member banks in the Federal Reserve System, and a great many nonmember banks; in fact, all nonmember banks which are in the Federal Deposit Insurance Corporation. That is a fact, is it not—that they cover them all?

Governor Eccles. They cover them all.

Mr. Brown. And the only banks in the country that they do not cover are the uninsured banks, which are very few in number?

Governor Eccles. That is correct.

Mr. Brown. I think I will close that part of the discussion by this: I understand that you, yourself, feel that it would be best if we could have one examining authority to examine all the banks of the country.

Governor Eccles. Let me first state that the existing duplication is not as serious as it appears on the face of things. The Reconstruction Finance Corporation make no examinations, as a regular thing. The examinations they made were in connection with subscriptions to preferred stocks and debentures; and those examinations were made only once, at the time they were determining their investment in the capital stock of the particular bank.

Mr. Brown. And, to be perfectly fair, I understand now that they are not making even that examination. They are accepting the other examinations.

Governor Eccles. That is right; and they have always accepted the other examinations, except in very important instances, where a great deal of money was involved and there was a good deal of question about the bank.

The Federal Reserve Board only examines the member State banks. Their examinations are usually made along with the State banking examinations, so as to avoid duplication. The Comptroller's office examines all national banks. No other agency examines national banks. The Federal Deposit Insurance Corporation makes no examination of national banks and makes no examination of State member banks but examines the nonmember State banks, along with the State banking departments, so as to avoid duplication there, so that there is really not the duplication in actual examinations that would appear on the face of things.

However, there is, of course, a division of the examining authority between the 48 State banking departments, with reference to State banks, and the Comptroller's office with reference to the national banks, and the Federal Reserve with reference to the State member banks, and the Federal Deposit Insurance Corporation with reference to all banks. There is not any question that you would get a much more general unification of the policy in making examinations if the examining were all done under the direction of one organization.

Mr. Brown. You certainly would eliminate the duplication of organizations.

Governor Eccles. That is right. You would eliminate the duplication of organizations, more than duplication of examinations.

Mr. Brown. Or, we might say, triplication of organizations.

Governor Eccles. Yes, sir; you would do that; and you would make, probably, for a greater unity of examination policy, which has been very sadly lacking. However, there has been a great amount of work done in the past 6 months with reference to improving the matter of unifying the policy as to examinations. The Comptroller's Office, the Federal Deposit Insurance Corporation, and the Federal Reserve have had a great many meetings, and much progress has been made toward the development of unification of examinations.

The Chairman. Let me ask you a question. What is the purpose of the examinations?

Governor Eccles. To determine the condition of the banks.

The Chairman. What I want to develop in asking you the question is this: Is not one of the purposes of the examination of the banks to develop and disclose bad practice and any fraud that is being perpetrated by those in charge?

Governor Eccles. It is to see that the bank is carrying out the provisions of the law.

The Chairman. One purpose of conducting the examination is to make sure there is no criminal violation or mispropriation of funds?

Governor Eccles. That is one reason.

The Chairman. Do you think that one system of examination, under one standard, is more likely to uncover or disclose fraud in the conduct of a bank than two examinations?

Governor Eccles. As a matter of fact, there is only one system in effect now. As I explained, the Federal Reserve accepts the Comptroller's examinations of national banks. If the banks were required to pay the examination expense of all these independent agencies, they could be constantly harassed and bothered with two examinations a year from each one of them; and I cannot see how they could endure it. As it is today, the banks are pretty well harassed with examinations and with the various reports that they are required to make to the various agencies, which is a great expense to them.

The Chairman. Are not the reports worse than the examinations?

Governor Eccles. They are both bad enough, but necessary.

The Chairman. From what I have heard, it would appear that the reports are worse than the examinations.

Governor Eccles. In most countries they have no examinations. In Canada there are no bank examinations whatever; and there never have been any bank examinations whatever. They have never had them.

The Chairman. Of course, they enforce criminal law in Canada, you know.

Governor Eccles. They have reports. As I understand it, in Canada they have complete monthly reports. That is correct, is it not?

Dr. Currie. Yes, sir; but they also have examinations now.

Governor ECCLES. No; not examiners going out into the banks. What they do is this, they get the monthly reports into the head office; and there are two examiners that go over those reports in the head office. What I meant was that there are no examiners who go out into the banks and carry out the examinations.

Mr. FORD. Unless they find something wrong with the report?

Governor ECCLES. They make an inquiry. But, you see, those banks have numerous branches, and the banks themselves have their own examiners. That is the way the British banks operate, in the same manner; they have their own examiners.

It is not expected that this proposed legislation will create a perfect banking system by any manner of means. We will still have plenty to consider, looking into the future.

The CHAIRMAN. Mr. Brown, have you finished?

Mr. BROWN. There is nothing in there to abolish the human equation.

Mr. CROSS. I was wondering how to abolish these glass eyes.

The CHAIRMAN. Well, gentlemen, we will ask Governor Eccles to come back in the morning, at 10:30.

(Thereupon the committee adjourned until tomorrow, Tuesday, Mar. 19, 1935, at 10:30 a. m.)

BANKING ACT OF 1935

TUESDAY, MARCH 19, 1935

House of Representatives,
Committee on Banking and Currency,
Washington, D. C.

The committee met at 10:30 a.m., Hon. Henry B. Steagall (chairman) presiding.

The Chairman. Governor Eccles, Mr. Goldsborough desires to ask you some questions.

STATEMENT OF MARRINER S. ECCLES, GOVERNOR FEDERAL RESERVE BOARD—Resumed

Mr. Goldsborough. Governor, you have been here for some time now and have been exceedingly patient, and I will not take very long, I am sure.

During the discussion of this bill, and, practically every bill the committee considers, the question of inflation is raised. I do not want to get outside of the issue, and I do not think I am. I have made, so far as I am able, a very careful study of so-called "inflation." I understand it means an increase in the volume of money to the point where its value is either worthless or partially worthless. I am unable to find in history any single instance where, under a stable government there has ever been that sort of inflation, and I am wondering if you are able to cite a case where there has been any inflation under a stable government.

Governor Eccles. I am not much of an authority on the subject of what has happened throughout the history of the world with reference to the matter of inflation. What study I have given to it applies more to recent developments, particularly since the war.

The conditions in this country at the present time are in no way, to my mind, parallel with the conditions in those countries that have had more or less inflation.

Mr. Goldsborough. Generally, the cases that are cited by those who are sometimes called reactionaries—and I do not want to be offensive, but that is the best I can do—the cases cited by them are the continental money, the French assignats and the German money after the war. Of course, the Continental money was issued at a time when nobody knew in this country whether we were going to be under a king or under a president, or what the government was going to be. Conditions were almost absolutely chaotic.

The same thing existed when the assignats were issued in France, and insofar as Germany was concerned, that inflation was deliberately created for the purpose of destroying the internal debts.

I remember not very long ago, Mr. Bernard Baruch had an article on inflation in the Saturday Evening Post—you may have seen it—which was propagandized by pictures, some 3 or 4 pictures or cuts were in the article depicting the printing presses in Germany during the immediate post-war period, which seemed to me to be so utterly unfair and inappropriate as to make the article absolutely valueless.

In this bill which we are considering, the banking system is allowed to remain in exactly the same position that it has been for a great many years. We have in all the banks, State and national, capital, surplus, and undivided profits of less than $7,000,000,000. The deposits of those banks have been as high, I think, as $57,000,000,000 during 1929.

Governor ECCLES. Including time deposits.

Mr. GOLDSBOROUGH. Including time deposits. Do you care to express your opinion as to that sort of a system, or do you think that is outside the inquiry?

Governor ECCLES. What was the question?

Mr. GOLDSBOROUGH. I am asking you if you care to express your opinion about a monetary system which is not the creation of society, but is the creation of a private institution, and which is based on debt.

As I said before, that may be, in your opinion, so far afield that you do not care to discuss it.

Governor ECCLES. I do not believe that it is practical at this time to abandon the present system of creating money by bank credit.

Mr. GOLDSBOROUGH. By bank debt.

Governor ECCLES. Bank credit means a debt of somebody.

Mr. GOLDSBOROUGH. It is better to use the word debt, because that is what you are speaking about.

Governor ECCLES. I do not know that we have any alternative. It is my view that we should attempt through this legislation to make the existing system of banking more responsive to the needs of the country than it has been, and also to exercise a greater degree of conscious control over the creation and the extinguishing of money, and thereby attempt to create a greater degree of business stability than we have had in the past.

Mr. GOLDSBOROUGH. You agree with me, do you not, that permanent prosperity cannot be based on debt? You cannot have debt, which is increasing all the time, and have any sort of permanent prosperity, can you?

Governor ECCLES. I do not agree that it is not possible to have permanent prosperity with the existing banking system, if, in connection with its operation, a taxing system is recognized as an adjunct in helping to bring about a more equitable distribution of income during periods of prosperity.

Mr. GOLDSBOROUGH. We never have had any such tax system, have we?

Governor ECCLES. No; we never have, and we have never had very much control over the banking system.

Mr. GOLDSBOROUGH. Do you or not agree with me that under the present set-up, insofar as banking is concerned and currency is concerned and taxation is concerned, we can only have pseudo prosperity which will collapse from time to time—do you think that is true?

Governor ECCLES. In our past history we have had periods of prosperity by the process of building up debt and then periods of depression by the process of bankruptcy and the extinguishing of debt. That has been true of all capitalistic countries.

Mr. GOLDSBOROUGH. That has not been the condition in France, has it, where the banks only have about a 50-percent reserve? France has never had these recurring periods of collapse.

Governor ECCLES. It is more or less true of every country, I think. Possibly it may be less true in France than it has been here, and I think it is possibly less true in Britain than it has been here because in recent years they have exercised, I think, a better control over their money system than we have.

The volume of money in Great Britain during the period of our depression did not decline. It remained very stable.

The wiping out of a third of our deposit money by bank liquidation of debt, and by bank closings, accentuated the depression.

Mr. GOLDSBOROUGH. Now I am old enough to remember that part of the deflation period from 1886 to 1896, and I, of course, remember the much better economic condition existing between 1898 and 1914.

I think it is thoroughly understood and agreed by everybody that it was the want of money which caused the depression in 1879 and 1896, which culminated in the Bryan free-silver campaign. After that time gold was discovered in South Africa, in the Klondike, and in Australia—we were on the gold standard, with a continually increasing supply of money—so that from about 1898 to the opening of the World War this country had what can be termed, at least relatively speaking, "considerable prosperity."

It was not the banking system, or fractional reserve system, that gave us that prosperity. It was the fact that we were able to put into the market a continuously greater supply of money. I do not believe anybody disputes that. Let us see what happened to our debt structure during this period about which I have just spoken, from 1896 to 1914, and up until 1920.

After 1920 our supply of gold was of such a character that we could not put it in the market as fast as our production wanted to increase, so our production did not increase, but our debt increased and our speculation increased.

Take, for instance, the period from 1913 to 1921. Our real estate, Government, State, and local debts increased from $38,000,000,000 to $75,000,000,000, and $15,000,000,000 of that was the war debt.

So that, as a matter of fact, our debt increased, outside of the war debt, 60 percent, and our income increased 83 percent. Our national wealth increased 67 percent.

In the period from 1922 to 1929 which is spoken of as a period of prosperity—and I never could see any prosperity during that period and I have never been able to see any since; it was a period of speculation—during that period our debt, that is, our real-estate debt, our Government debt, and our State and local debts increased from $75,000,000,000 to $126,000,000,000. The increase was 68 percent.

Our wealth only increased 20 percent; that is, from 321 billions to 385 billions. Our income only increased 29 percent, from 66 billions to 85 billions. We liquidated during that period $4,000,000,000 of long-term debts, and we took on $55,000,000,000 of other debts.

That was a period in which our present monetary system, as handled by bankers, was in full sway, but a period in which our money supply, based on the gold standard, was not increasing. It ended up in collapse.

I have never seen anybody who could, but if you can, I wish you would give us your view as to how, loaded up with all this debt, we are going to get out of this depression under the present system, with what amounts on the average, to a 10-percent bank reserve. How can it possibly be done, unless we have complete deflation and wipe out the debts by bankruptcy.

Governor ECCLES. There are two ways of doing it. One is the way you have just stated, that is, continuing a process of deflation and wiping out a large part of existing debts through the process of bankruptcy, because the national income at the present time is not sufficient to support the existing debt structure.

And that is one reason we are possibly not getting recovery today, because liquidation and the pressure of debt is very, very great, and it acts as a millstone around the neck of the economic system.

The other way to get recovery, the only other way I can think of, is by a process of reflation.

Mr. GOLDSBOROUGH. Under our present system we cannot have any reflation without an accumulation of more debts, you know.

Governor ECCLES. I believe it has been very genereally recognized, certainly since March 1933, when the banking structure collapsed and closed, that it was not practical or possible, without involving very great political and social upheavals, to continue the process of deflation. The situation had reached the limit of human endurance, beyond what the people were willing to stand by way of deflation, which creates unemployment and all of the other attendant ills, and reflation was desired and was expected.

The only way that that can be brought about is by increasing the means of payment, either currency or bank deposits, in the hands of those who will spend faster than production increases.

Mr. GOLDSBOROUGH. Can you spend faster than you accumulate debt, under our present system? That is the difficulty, the debt is always ahead of the spending.

Governor ECCLES. Interest is a very important element in connection with the creation of money by debt. Very low interest, it seems to me, creates a far less dangerous situation than debt created on a basis of very high interest.

Mr. GOLDSBOROUGH. That is true, but of course the banks ordinarily now charge the same interest as they always have been charging.

Governor ECCLES. Not generally. Most of the debt today is at a much lower rate than it was. I would say the average interest income of the banks today is 40 percent less than it was in 1928 and 1929.

Mr. GOLDSBOROUGH. That is because they have accumulated long-term Government obligations.

Governor ECCLES. And other Government obligations.

Mr. GOLDSBOROUGH. When they loan to their customers they do charge a large rate. In our State it is 6 percent. They have not reduced it, certainly within the range of my observation.

Governor ECCLES. I think that is true more in the country banks than in the city banks, where they are largely influenced and affected by the money market. And the rate of lending goes up and down in pretty close relationship with the general supply of money, and you get an excess of money as you have now, when the rates are at a ridiculously low figure for certain short-term eligible paper.

Now, to get back to the question of creating prosperity out of debt. It is true that the bulk of the means of payment under the present system is created by an expansion of bank credit.

Mr. GOLDSBOROUGH. In other words, you create more debt to pay the present debt.

Governor ECCLES. A part of the debt of the country is not bank debt. The debt that the banks create in creating money is, in fact, only a small part of the total debt.

Mr. GOLDSBOROUGH. That is true.

Governor ECCLES. And it is not by any means the burdensome part of the total debt.

Money is created in our present system by banks loaning to corporations, to individuals, and to the Government. During the past 2 years there has been no increase in the supply of money as the result of the banks lending to individuals or to corporations. As a matter of fact, the money supply would have been actually diminished since 1933 had it not been for the Government not only making up the deficiency, but greatly exceeding it by its borrowing and spending. Had it not been for the Government's budgetary deficit, I do not believe the deflationary processes would have stopped.

The credits which the banks have extended to others than the Government are less now by several hundred millions than they were right after the bank holiday.

The Government has been forced to supply the money deficiency by reason of the other creditors being either unable or unwilling to supply it. I believe I made a statement yesterday in connection with the Government supplying money by borrowing from the banks that might have been misunderstood. I am sure it was misunderstood by many of the press comments that were made. That is, the question of the Government paying the banks a subsidy.

Mr. GOLDSBOROUGH. I probably made the mistake of accentuating that too much myself. I am at fault probably more than anybody else.

Governor ECCLES. I would like, for the purpose of the record, to make an explanation of my understanding of the question of the Government interest paid to the banks.

In purchasing offerings of Government bonds, the banking system as a whole creates new money, or bank deposits. When the banks buy a billion dollars of Government bonds as they are offered—and you have to consider the banking system as a whole, as a unit—the banks credit the deposit account of the Treasury, with a billion dollars. They debit their Government bond account a billion dollars, or they actually create, by a bookkeeping entry, a billion dollars.

Mr. GOLDSBOROUGH. By a sort of magic or necromancy.

Governor ECCLES. The Government in turn draws out those deposits and disburses them in the payment of all of its obligations and various appropriations.

Mr. GOLDSBOROUGH. These payments, of course, go in the banks.

Governor ECCLES. Yes; these payments of the Government, of course, immediately go right back into the banks, and therefore the total deposits of the banks are not changed; but the ownership of the deposits is transferred from the Government to individuals and corporations, who can spend it or use it to reduce their debts to banks.

Mr. Goldsborough brought out the point that the Government, because of its sovereign power, is able, if Congress so wills, to finance its operations by payment of currency for its obligations, and that it could go so far as to take up its bonds by paying out currency. The result of that operation, insofar as the bonds were purchased from others than banks, would be that bank deposits would increase.

Mr. GOLDSBOROUGH. Bank reserves, not deposits.

Governor ECCLES. Deposits. If the Government paid its bills in currency, that currency would be disbursed, the money would come into the banks to the credit of individuals and corporations, and thus the deposits would be increased in exactly the same way.

Mr. GOLDSBOROUGH. I wish you would speak about that for a while. The deposit would not increase, but the reserves would increase.

Governor ECCLES. Both would increase, both the reserves and the deposits would increase. To the extent that the bonds were purchased from banks, reserves would increase and deposits would not. To the extent that bonds were purchased from others both deposits and reserves would increase.

The proposal was that, when you substituted currency for bonds, the reserves would be greatly in excess of what they now are; because the banks would not have the deposits invested in Government bonds, but would be carrying those deposits as excess reserves, and to the extent that present holdings of governments by the banks were taken up by currency, the reserves of the banks would increase by about 11 or 12 billions of dollars. Thus, you would have excess reserves of, say, 13 or 14 billions including the more than 2 billions now held by simply taking up the existing holdings of Government bonds.

That, of course, would be a means of potential inflation of a tremendous amount.

Mr. CROSS. Could you not raise the reserves of the banks so as to check that?

Governor ECCLES. I was just going to say, it was suggested that the reserves of the banks would be increased by the amount of the Government bonds that were taken up, as the result of the issuance of currency in payment for them, and the currency would come right back into the banks as a deposit.

The point I raised was that the banks would under no circumstance be willing to handle the deposits which would be created without getting a return, without being able to invest them at interest. But, if reserve requirements were increased by the amount of the increase in reserves, the banks would be unable to perform the services which they do perform in the handling of the business of the community, of their customers, of the clearing of financial transactions and the keeping of the individual and corporation accounts without making service charges that would compensate them for their loss of income or interest, as a result of depriving them of interest on the Government obligations.

Mr. Goldsborough stated the other day that that charge could be socialized and I stated that the best way to socialize it was to do as is being done now, by permitting them to get interest on Government bonds.

Instead of the interest on Government bonds being a subsidy to the banks, it seems to me it is a payment for services which they are rendering in handling the deposit accounts which are created as a result of the Government deficit.

Mr. GOLDSBOROUGH. Now, Governor, it seems to me, now, and has always seemed to me that the real way to do a thing is to do it directly, instead of going through the pretense of issuing bonds to the banks that have not anything to loan, except what their bookkeepers can put on their books.

The banks have nothing except their capital and surplus, which amounts to less than 7 billion dollars, and they have used that up long ago in loaning to individuals.

Governor ECCLES. Except their time-deposit funds.

Mr. GOLDSBOROUGH. Except their time-deposit funds.

Governor ECCLES. That represents half of the deposits of the banking system.

Mr. GOLDSBOROUGH. But long before that they come to the Government for help. They have used up all they have.

We go through the racket—and that is all I am able to see that it is—of issuing to the banks, sending to the banks bonds, and they put a money credit on their bank books in favor of the United States Government. The United States Government by depositing that money as it does, when it gets the money credit, lends the money back to the banks and proceeds to pay them interest on it. That is a racket.

If we owe the banks for that service they render, and we do, there is no doubt about that, they render service outside of their lending service and they should be compensated for that; they will have to be compensated for that to live.

But there is created in the public mind the idea, and it is done deliberately by the class which controls the money of the country—there is created in the public mind the idea that there is some economic impropriety in the Government furnishing its own medium of exchange, that it has to do it through borrowing money from the banks that the banks do not have.

Society has everything; the banks have nothing, and yet we go through this farce of borrowing money from the bank and creating the impression that it is inflationary for society itself to issue the necessary medium of exchange with which to conduct the country's business.

What I am getting to is this. I am not suggesting any immediate revolution. But we could pay these bonds as they are callable; we could pay these bonds when they come due with money issued on the credit of the Government of the United States. And if the public knew that would be done it would have two effects, first it would reconcile them to this debt, which is having a terribly depressing effect on their minds and on their psychology. It would do that.

And the second thing it would do would be to have them understand, to make them understand, that society is not dependent upon a banking system for its currency. Our currency system in this country was not the creation of society; it was the creation of the banks.

Last year about this time a subcommittee of this committee considered what was called a monetary authority bill. The goal of that proposed legislation—whether it could be reached or not—the goal of the proposed legislation was to separate the profession of banking from the issuing of the money of society. It placed the issuing and the control of the money which society uses in the hands of an independent authority, which would have no selfish interest in making the medium of exchange as scarce as possible and as high as possible.

I am wondering if something of that same idea is not involved in this present bill, which undertakes to take from the Federal Reserve banks and place in the hands of the Federal Reserve Board the control of the open-market operations of the Federal Reserve System.

Governor ECCLES. Discount rates and reserve requirements.

Mr. GOLDSBOROUGH. Discount rates and reserve requirements. Is that so?

Governor ECCLES. It is contemplated to centralize the responsibility and the authority for control over the volume of money.

As I have stated upon several occasions, so long as most of our money supply is created by the willingness of private citizens and corporations to borrow from banks, the control of deflation is much more difficult than that of inflation. If there is too much borrowing from banks and, as a result of that operation, the creation of inflation, when the means of payment is increasing faster than the raising of discount rates and the selling of securities in the market would discourage further expansion of private borrowing from the banks and would act as a means of retarding the inflationary process.

On the down side, the reverse action, the reduction of rates and the creation of excess reserves, would tend to slow up liquidation and would tend to encourage the use of credit.

In our present money system I know of no other means within the banking system itself of influencing or effecting a control over the supply of money.

I have stated that we should seek to use these controls which I have just mentioned to combat deflation, which means unemployment, and unemployment means reduction in national income, in wealth production, and wealth consumption.

That is where the problem must be met, and it must be met, it seems to me, by society as a whole, through government.

The tax system—our income-tax system—must be worked in and timed with the money system. When private credit is expanding and there is a budgetary surplus, the Government debt should be reduced. The reduction of the Government at a time when there is a rapid expansion of private debt tends to offset the inflationary effect of the expansion of private debt. That is where the contraction comes, as result of the banks reducing their holdings of Government bonds.

It is very important that the problem of income taxation and the operation of a central banking monetary policy should be coordinated and properly timed. A substantial increase in taxes at the present time, if they would pull into the Treasury money which would otherwise be spent and thus reduce private spending, would be of no particular help in our economic as a whole. The time to increase income taxes, of course, is when incomes are such that income taxes would produce substantial revenue; in other words, in the upswing.

I believe that there is only one way by which we will get out of the depression, and that is through the process of budgetary deficits until such time as private credit and private spending expands. The expansion of private credit depends upon the will and ability of private interests to borrow and spend. Until private borrowing and spending expands, and puts people to work, the Government must do the borrowing and spending.

Mr. GOLDSBOROUGH. Governor, going back to the subject of inflation, it seems to me that the fear of so-called "inflation" is the thing which makes it increasingly difficult to improve our monetary system.

I have been following this whole matter through for a great many years, and I remember very distinctly that back in 1931—I do not want to go too far back—but I remember that in 1931 we were told that if we adopted the policy of buying Government bonds that would cause violent inflation. That was when the original so-called "Goldsborough bill" was passed through the House.

During that period, and before that period, if anybody had suggested that it was possible for the Government to raise any money except by borrowing it from the banks, he was immediately cast into outer darkness; he was not even thought fit to sit in the room with intelligent people. That was the exact condition.

We went off the gold standard and nothing happened. We passed the so-called "inflationary bill" in 1933 and nothing happened.

And it is the feeling, I am sure, of a great many Members of Congress—it is certainly my own feeling—that one of the things we need in this country is more real money and less false money in circulation.

If, as a matter of fact, we could get to the point where the money we use was real money and could not be contracted by the payment of debt, then you could not have any violent deflation; we could not have any violent inflation; you could not have either one.

Governor ECCLES. It depends upon the distribution of that money and the willingness of people to put it in circulation.

Mr. GOLDSBOROUGH. I know that it would be very much more difficult than it is now to have deflation, or inflation, either.

Governor ECCLES. I agree with you that all of this inflation talk we have heard for 3 years has been largely imaginary.

It is true that, based upon existing excess reserves of the banks, there is a possible means of creating a tremendous credit inflation. That, of course, does not necessarily mean that you are going to get that inflation.

In the first place, in order to get it, we have to get people willing to use the bank credit. It cannot be gotten in any other way.

Then it also would be necessary that there be no control exercised after private credit began to expand to a point where prices were going up rapidly and production had reached a peak.

I do not believe that it is going to be so easy to get inflation. Certainly efforts have been made now for several years to get it; but from all indications, we are as far from it now as we were 2 or 3 years ago. There is not the slightest indication of inflation.

Unless the people in this country have money and jobs or are put in possession of money through jobs or without jobs, so that the means of payments increases, and unless those people and corporations with money will spend the money that they have, we cannot get inflation.

It cannot be obtained merely by changing the gold content, or by silver legislation, unless the result of such changes will actually put money in the hands of people to spend, and unless it induces the holders of existing money to spend. Otherwise you do not increase the volume of money and you do not increase the velocity of money, both of which are necessary in order to get inflation.

Mr. KOPPLEMANN. Mr. Eccles, with reference to section 210, page 49, in regard to making loans on mortgages, you know about that?

Governor ECCLES. Yes.

Mr. KOPPLEMANN. As I understand it, it authorizes commercial banks to make loans on real estate for a period of 3 years, and repayment is to be made in full at one time or up to 20 years to be amortized. It puts commercial banks and investment banks in the building and loan business.

Governor ECCLES. They are already in.

Mr. KOPPLEMANN. But this bill is intended to put them into it further than ever.

Governor ECCLES. No. The bill is not for the purpose of putting them into any particular business that they are not already in. They are in the investment business and in the mortgage business and have been to a very large extent for a great many years. They are in the investment business in that there is no limitation as to the amount of long-term bonds of all kinds that they are permitted to buy. There is a limitation with respect to making first real-estate mortgages on improved properties. That limitation is 50 percent of the time deposits and up to 50 percent of the appraised value of the property, and up to a period of 5 years; and the banking system today holds over $2,000000,000 of those mortgages. Therefore, they are not being put into any business that they are not already in. What we are attempting to do in this case is to permit them in the making of real-estate loans to make loans on an amortized basis over the life of the loans or over a period of time which would give to the borrowers some assurance of being able to pay. The straight 5-year mortgage has proven to be a very bad form of instrument, both for the banks and for the borrowers, and also for the building and loan companies engaged in making mortgage loans and a few insurance companies and mutual savings institutions engaged in that type of mortgage lending.

I have said, and I repeat, that either the banks in this country will have to give up their time deposits or they will have to be permitted to invest or loan those deposits in the same field where the mutual savings banks, the insurance companies, and the savings and loan institutions, loan their deposits; because the time deposits of the banking system are of the same type and represent the same type of money as the funds which the mutual savings banks and the building and loan companies loan and invest.

Mr. KOPPLEMANN. It was the bad practice of the banks which caused the debacle.

Governor ECCLES. I do not agree with that.

Mr. KOPPLEMANN. Did not the banks themselves claim that it was their long-time loans which were the chief cause of their difficulty?

Governor ECCLES. I do not think so.

Mr. KOPPLEMANN. Is it not commonly so stated?

Governor ECCLES. It is commonly stated; but it is not the fact.

Mr. KOPPLEMANN. I might digress for a moment and ask you if you can in a single statement, without taking too much time of this committee, let me have what is your opinion of the cause of the difficulty of the banks?

Governor ECCLES. I think the record of my answers to the questions that have been asked quite a number of times shows it; but I can state it very very briefly. One of the principal troubles or difficulties that brought about the depression was not the shortage in the supply of money altogether, but it was due in part to the inequitable distribution of income which contributed to a speculative situation in the security markets and to an expansion of productive capacity out of relationship to the ability of the people of the country to consume under the existing distribution of income. That condition was not created by the banking system. Long-term credits were not responsible for the depression; they only became unsound when the national income shrank. A perfectly good credit over a short term or a long term may become a very bad credit if business conditions change. Short-term credit is not necessarily a sounder loan than long-term credit. Most of the short-term bonds which were held by the banks that became due during the depression could not be paid but had to be refunded.

Mr. KOPPLEMANN. Supposing that I ask you this further question.

Governor ECCLES. In order to obviate that situation of forced deflation, this bill proposes that Reserve banks be legally permitted to make advances to member banks against sound assets. The only place where liquidity can be created is through the Reserve System and that would permit the Reserve System to stop forced credit deflation and bank failures so long as banks had assets upon which they could secure credit.

Mr. KOPPLEMANN. In part you anticipated the question I was about to put to you, which is: Are loans made on real estate expected to be rediscounted by the Federal Reserve?

Governor ECCLES. They are expected to be available as security for advances to be made by the Reserve banks. The credit departments of the Reserve banks will pass upon credit extended to member banks in the future as they have always done in the past, except that in the past they have been limited by statute to a certain type of what is known as eligible paper which today is small in volume.

Mr. KOPPLEMANN. Where in this bill does it provide that such discounting, or in effect rediscounting, can be done?

Governor ECCLES. It provides in section 206 that section 13 of the Reserve Act is to be amended so as to authorize the Federal Reserve banks, subject to the regulations of the Federal Reserve Board, to discount for member banks any commercial, agricultural, or industrial paper and to make advances to member banks on their promissory notes secured by any sound assets.

Let me say this in connection with extending credit against mortgages. That does not mean that Reserve banks will discount a 20-year mortgage for 20 years. It means that the Reserve banks can make advances to the member banks for such periods as reasonable banking practice permits, which would be 90 days or possibly 6 months, secured by mortgages, collateral loans, or bonds with such margin as the credit divisions of the Reserve banks may deem necessary to protect the Reserve banks.

Mr. KOPPLEMANN. Then it does not compel the Federal Reserve to rediscount these loans?

Governor ECCLES. No.

Mr. KOPPLEMANN. Now, supposing I go to you as a banker and ask for a loan upon my property in the form of a mortgage and the banker knows that he cannot rediscount, what will be the effect upon your mind if I ask for a loan of you as a banker?

Governor ECCLES. The banks today will not make such loans. In the first place, they cannot make real-estate loans for more than 5 years. That precludes people from borrowing. Nobody today that can secure a long-term, amortized loan will go to a bank and borrow on a straight loan for a period of 5 years. They want longer-term credit on mortgage loans.

Mr. KOPPLEMANN. I am trying vary hard not to take any more of your time than possible. Now, if section 210 should succeed in encouraging banks to make long-time loans, they cannot be rediscounted?

Governor ECCLES. But they can be borrowed against.

Mr. KOPPLEMANN. Yes. What becomes the bank's liquidity which, after all, as you and I know, is the foundation of the safety of a commercial banking system?

Governor ECCLES. The liquidity of the banking system depends upon the Reserve System as I have indicated.

Mr. KOPPLEMANN. What I am trying to bring out is this. I am not opposing the bill nor do I want to appear unduly critical. What I am trying to bring out is that the effect of section 210 is more apparent than real. It seems to me that it contains language rather than a real and effective method of giving property owners a chance to obtain mortgage loans.

Governor ECCLES. That will depend entirely upon the willingness of the banks themselves to extend mortgage credit. In the absence of any field for investment of the excess funds of the banks, it seems to me that there will be a willingness, not only a willingness but a desire, of bankers to invest those funds where a substantial portion of the deposit money is represented by time money upon which they are paying 2 to 2½ percent.

Mr. KOPPLEMANN. Right there may I ask you this question? You talk about time loans. Are not time deposits in reality nothing more than demand deposits?

Governor ECCLES. Only in case of bank runs. The time deposits in a bank remain stable unless banks are permitted to fail.

Mr. Kopplemann. That answers my question. Only in time of bank runs.

Governor Eccles. That is right. At other times time deposits fluctuate very little and, as a matter of fact, usually, or at least during the past, they have shown a gradual increase over a long period of years.

Mr. Kopplemann. What effect will such loans have upon building and loan associations and do you interpret that commercial banks are to compete with them?

Governor Eccles. I think there is a field for both. It seems to me that we might ask what effect will it have upon insurance companies and mutual savings banks.

Mr. Kopplemann. That is right.

Governor Eccles. The more agencies we have for extending credit the more likely the borrower is to get favorable terms for his credit; and I think that, in the interest of recovery, long-term low rates are necessary.

Mr. Kopplemann. Yet under section 210 all of this is quite improbable of happening insofar as banks making loans due to the fact that they cannot rediscount excepting on short time, as you say, 90 days, perhaps 6 months.

Governor Eccles. That is very true; but that will not deter the banks from making long-time loans. The banks today can only borrow on Government bonds on a 15-day basis but they can renew. Banks are certainly not expected to make real-estate loans and sell them to the Federal Reserve banks and then take the funds and make additional loans, because that would create credit inflation. Banks should not loan beyond the amount of their available funds and the rediscounting facilities of the Reserve banks are for the purpose of enabling the bank system to meet temporary fluctuations in their deposits and to meet withdrawals due to unusual conditions that may develop.

Mr. Kopplemann. I agree with you that commercial banks should do a safe and sound business, and that under section 210 of this bill, it would be bad business to make these mortgage loans. That is all. Thank you.

The Chairman. Would you like to come back this afternoon or tomorrow morning?

Governor Eccles. I would appreciate it if I could come back in the morning.

The Chairman. We will ask you to come back tomorrow morning at 10:30. Mr. Goldsborough and Mr. Cross and Mr. Williams would like to ask you some questions and with that we hope to conclude.

(Thereupon, at 12:05 p. m., the committee adjourned to meet again at 10:30 a. m., Wednesday, Mar. 20, 1935.)

BANKING ACT OF 1935

WEDNESDAY, MARCH 20, 1935

HOUSE OF REPRESENTATIVES,
COMMITTEE ON BANKING AND CURRENCY,
Washington, D. C.

The committee met at 10:30 a. m., Honorable Henry B. Steagall (chairman) presiding.

The CHAIRMAN. Mr. Cross, do you desire to interrogate Mr. Eccles at this time?

STATEMENT OF MARRINER S. ECCLES, GOVERNOR FEDERAL RESERVE BOARD—Resumed

Mr. CROSS. Governor Eccles, you know, I am very much disturbed about your testimony as it has been given. You have testified that with the levers you have in this bill you feel that you could control inflation, but that the question of deflation was another story. In other words, you have a string with which to pull down inflation, but you have no string with which to pull up deflation.

And you also testified as to the depression, as I recall your testimony, that deflation meant depression, and as long as you have deflation you will have depression.

What is troubling me is how to get some means by which we can lift deflation.

Also, in your testimony you stated that you thought the income-tax question would have to be worked into the monetary system somehow.

I introduced a bill—I do not suppose you ever heard of it, or have ever read it—in an attempt to control the whole commodity price level through the system of the income tax. That bill provided that when the wholesale commodity price level was below the purchasing power of a dollar; say that the purchasing power was up to twice what it was in 1926 and 1927, for the sake of argument, that the Government, or some agency of the Congress be permitted to lower the income tax, to pay the running expenses of the Government, the salaries of the civil-service employees, and the Army and the Navy, and other governmental expenses, and pay off the bonds and other obligations as they fall due by simple currency, having it printed, until the prices of things rise, or the purchasing power of the dollar fell, whatever it was, taking it in the year that you are taking as a standard.

Now, if the prices rise more than 2 percent, as was provided in the bill, above where they were in the year taken as a standard, you are going to be laying on income taxes and taking currency out of circulation; in other words, performing the same function as the open-market transactions, and you would take currency out of circulation the same as you would if you were to sell bonds and take it out, or you put currency in circulation by paying the expenses off, doing it in one or the other way.

Do you not think that by means of the currency you could get a string to lift up your depression?

Governor ECCLES. I do not know that I can add anything to what I have already said on that subject.

Mr. CROSS. It is very patent that we cannot get out of this depression, depending upon credit, as long as the conditions remain as they are. You can reduce the rediscount rate to nothing, and you can put the reserves of the banks down to nil, but as long as conditions are such that a man cannot produce his goods and sell them for what they cost him, as long as there is no purchasing power among the people he cannot get a price that will enable him to pay the expenses of operating his factory or his farm, or whatever he is operating, because the banks could not loan him anything. If I was a banker, or if you were a banker, you could not afford to loan him any money; he could not borrow that money to produce the goods and pay the money back because he has to have buyers, and that means purchasing power, and upon that depends credit.

I do not see any way in the world to bring the country out of this depression unless we get it out by deflation.

It is not a question of the income tax taking money out of circulation; it will have the same effect as if you sold bonds and took them out of circulation. It is the same thing, is it not?

Governor ECCLES. I do not see what you mean. You say it is not the income tax.

Mr. GOLDSBOROUGH. Mr. Chairman and Mr. Cross, I was examining the witness yesterday when I yielded to Mr. Kopplemann, and now I have yielded to Mr. Cross. I had under discussion with Governor Eccles yesterday the discussion of a major subject.

Mr. CROSS. You go ahead; I thought you were through.

Mr. GOLDSBOROUGH. You have started on a major operation.

Mr. CROSS. You go ahead.

Mr. GOLDSBOROUGH. Governor Eccles, at a meeting of economists the other day, and also on the floor of the House, I made the statement that, under our present banking system, if every man in the United States had the financial genius of the senior Morgan and the inventive genius of an Edison or a Ford, and the energy of a North German farmer, we could not have any permanent prosperity in the United States because of the fact that just as soon as they began to show their ability and pay off this load of debt it would immediately cause another deflation, and prosperity would therefore defeat itself.

What is your criticism of that statement?

Governor ECCLES. That goes into the whole subject of the way money is created and extinguished.

Mr. GOLDSBOROUGH. I mean under our system.

Governor ECCLES. I feel that it is possible to have prosperity under our system, if we have the intelligence to manage our banking and our money systems, and our tax system in conjunction there-with, and our public spending, so as to insure employment; that you can have prosperity under the system whereby money is created through bank credit, and is extinguished by the paying off of the bank credit. Whether there are other ways of getting it or not, I do not know that I am prepared to say. It is difficult to make changes; we found that out.

People are prone to change their habits, their customs, and their belief very, very slowly; and changes largely come about as the result of social and economic pressure.

Mr. GOLDSBOROUGH. I will put it in another way.

Summer before last, at the Century of Progress Fair, a very noted statistician made a speech in which he said that the country owed in debts about $200,000,000,000, but that if we all got good and were thrifty, and saved our money and kept out of saloons, and things of that kind, we could pay off $25,000,000,000 of the debt a year, and in 8 years we would not owe any money at all.

I knew him very well, and I wrote him a letter and asked him what, under our system, we would use for money, when that happy condition arose. He wrote back and said he had not thought of that. When the debts were all paid off we would not have any money with which to do business.

Governor ECCLES. When the community begins to pay its debt to the banks, it extinguishes money, deposits currency, and if that process of deflation gets under way it is more or less self-generating and it is very difficult to stop it.

You can reduce rates through the operations of the Federal Reserve System; you can create excess reserves; you can broaden the eligibility requirements so as to make it unnecessary for banks to bring pressure to collect debt.

When the community's volume of money is rapidly contracting, it means that unemployment is developing; and the compensating factor is the budgetary deficit, which keeps up the volume of money, and those funds are used to give employment when unemployment develops.

That is what I meant when I said that the money system and the tax system, Government borrowing and paying must be worked in with our banking system as the compensatory agency. Otherwise, it seems to me what you say is likely to be what will happen. It is what has happened in the past, to a very large extent.

Mr. GOLDSBOROUGH. Of course, what I have in mind—and I do not know that you should be questioned particularly about it, in view of the fact that it does not bear directly on any item in the bill—but what I have in mind is that society should begin to bear in mind the fact that our present banking system is an artificial one, built up by the bankers themselves for the purpose of controlling money. That society should begin immediately to endeavor to take that control out of the hands of any one class and place it back where it belongs, in society itself, and that one way to begin that is to inject money into business. As an example, by reduction of Government debt, paying off Government debt with currency.

Governor ECCLES. I think that this discussion came up the other day, and I stated my objection to paying off the Government bonds in currency, which would result in the creation of very large excess reserves by the banking system, unless the reserve requirements were increased accordingly.

Mr. GOLDSBOROUGH. Of course, that could be done by legislation, and that very thing is contemplated by the bill we are now discussing.

I have never had in mind, and I have never introduced in Congress any bill which would require the national debt to be paid immediately. There is only about 5 billion dollars of bonds which are callable now. It seems to me that to start a system of teaching society that banking is one thing, and the issuance of currency an entirely different thing, would not only relieve society of a tremendous burden of interest, but would be a great educator, because in my opinion we are never going to do anything by creating more debt except to create a pseudo prosperity which will carry us along a few years longer and then, as by building up capital goods and selling on the installment plan with the use of more credit, have a greater collapse than we have now.

Governor ECCLES. I do not think the change in the system that you propose would put money into the hands of people that do not have it.

Mr. GOLDSBOROUGH. When you reduce taxes you declare a national discount, do you not? You are speaking of income taxes, but that would apply to any kind of taxes, any sort of taxes?

Governor ECCLES. Yes; when you reduce taxes that is true.

Mr. GOLDSBOROUGH. It is fair to suppose, is it not, that society would get the benefit of that discount?

Governor ECCLES. If you reduce income taxes it should be kept in mind that they are paid by a very small percentage of the total population—it would mean that the funds saved by the class that received the benefit of the reduction——

Mr. GOLDSBOROUGH. You do not think the ultimate consumer would get any benefit at all?

Governor ECCLES. They would possibly get some benefit; but it would tend to go into the capital field, and get productive facilities out of relationship to consumer buying power.

I do not like the idea, personally, of paying off the Government debt through currency; because it seems to me that it gives to a great many people the idea of expecting benefits that they will not get.

The paying off of the debt by currency would simply increase the bank reserves by the amount of Government bonds that they hold. When the reserves are increased by that amount, you have created a very difficult problem, unless you increase the reserves by the amount of the Government bonds that have been retired. Otherwise you have huge excess reserves.

If you retire the Government bonds with currency, that currency is the property of the banks and they will immediately send it into the Reserve banks; so it would not go into circulation at all. It would simply become a credit to the member bank on the Reserve bank's books; and, as I said, would make for an increase in the excess reserves by the amount of the bonds retired with currency.

Let us see what problems that creates. In the first place, you would have to increase the reserve requirements then by the amount of bonds which you retired, which would be today about 40 percent of the banks' loans and discounts. Government bonds are about 40 percent of the total loans and discounts.

Mr. GOLDSBOROUGH. If you retired them all at once.

Governor ECCLES. Of course; or you would increase it as you retired them.

You have a short-term financing of about 13 billion dollars, so that there are more short-term maturities than the total holdings of the banks. So in the course of a year or two the whole amount could be retired, because of the very large amount of short-term financing.

Let us assume, then, that you increase the banks' reserves by the amount of the bonds which you retire, or, we will say, 40 percent. Some banks only hold 10 percent of their resources in Government bonds, and if a 40-percent increase in reserves were imposed upon them they would have to reduce the credit they are now carrying by 30 percent in order to meet the reserve.

Mr. GOLDSBOROUGH. Could not that be controlled by a system of rediscounts between the banks?

Governor ECCLES. Reserves would have to be uniform among the banks; you could not have every one of the banks with a different reserve requirement. If you made a uniform reserve requirement in the banking system, with a bank holding 10 percent in bonds, when the reserve requirement is 40 percent, it would either have to go into the Federal Reserve System and borrow 30 percent, which was the deficiency, or it would have to collect loans and discounts to the extent of the 30 percent, in order to build up its reserves. Most of the banks in small communities hold Government bonds in the small amounts, and the deflation would come in those areas.

In the reserve cities the percentage of bonds held by banks, I think, is in excess of 40 percent, on the average. That is one problem it creates.

Another thing is that the State nonmember banks, which would not be influenced by the increase in the reserve requirements made by the Reserve System——

Mr. GOLDSBOROUGH. Yes; they would be.

Governor ECCLES. They are not members of the Reserve System.

Mr. GOLDSBOROUGH. That does not make any difference, you can put a check tax on them which will make them amenable.

Governor ECCLES. And force them into the Reserve System?

Mr. GOLDSBOROUGH. No; but force them to abide by the Reserve Board's dictum in the matter of raising and lowering reserves, under penalty of having their checks taxed.

Governor ECCLES. Then we get back to this problem. The retirement of these bonds through currency, or through giving the banks credit on the reserve bank books, would not, of course, in any way reduce the total deposits of the banks. It is 12 or 13 billions of the Government bonds issued.

Mr. GOLDSBOROUGH. You said yesterday it would increase the deposits. I agree it would not decrease them.

Governor ECCLES. It would increase deposits if the Government's expenses and its future deficits were paid with currency. That would increase the deposits by the amount of the deficit. But if you simply retire the bonds now held by the banks, it would in no way change their deposits.

Mr. GOLDSBOROUGH. That was our discussion yesterday, in reference to the retiring of bonds.

Governor ECCLES. That in no way would change the deposits.

Mr. GOLDSBOROUGH. In other words, we agree on that.

Governor ECCLES. The deposits would just remain the same.

Mr. GOLDSBOROUGH. Correct.

Governor ECCLES. But those deposits are not the deposits of the Government now. Twelve or thirteen billions of Government bonds held by the banking system represent money which the Government has spent. It has gone into circulation, and it has become the property of the individuals and corporations, and the banks have the responsibility of managing it and serving those customers in the handling of their business, in their deposit accounts. Unless they can invest those deposits which the Government has created as the result of its borrowings, at an interest return, they would have no object at all in handling the deposits. If they had to carry reserves equal to the amount of the deposits which are created, there would be no interest in the banks handling the accounts. Therefore, I think, as you stated the other day, the cost of handling that business should be socialized, and I stated that it was being socialized through the interest which was being paid on the bonds which the banks hold.

Mr. GOLDSBOROUGH. You think that is the proper way to socialize it?

Governor ECCLES. I think it is, and I do not think it is an unjust way to socialize it for the reason that the banking system as a whole has never been more remunerative than the average business, and there is no indication at the present time that it is particularly attractive. Bank stocks have possibly suffered as much or more than any other kind of an investment security, and based on my own experience in the banking business as well as in various other lines of business, I would say that from an investment standpoint the banking business is the least attractive.

Mr. GOLDSBOROUGH. My dear sir, before the war the banks were extremely prosperous, and there were practically no bonds out at that time.

Governor ECCLES. Before the war we were in a rapidly growing, new country; we were a debtor nation.

Mr. GOLDSBOROUGH. Being a debtor nation does not create prosperity.

Governor ECCLES. Being a debtor nation creates a degree of prosperity for the banks; I mean, in part, because of the shortage of capital, and the high interest rates that were generally being paid.

The banks, like every other business, have had periods of prosperity and profits, and then they have had reverses. But outside of the banks in the large centers, the average banks throughout the country have certainly not been overpaid for the services which they render, and if any revolutionary change is made in the method of creating money, and if we should take all the Government bonds up from the banks, as you propose, by currency and other methods, how would they be compensated for the very necessary and the very valuable and the very useful services which they render the community in the clearing and handling of the transactions which they are required to handle?

Mr. GOLDSBOROUGH. But now an artificial institution, our present banking system, creates the necessity of rediscounts, intermediate credit banks, and the army of bank examiners, and divides the country into simply a creditor and a debtor class.

It is this artificial system that has created all this trouble, and you cannot cure that by making additional paper or additional collateral eligible for rediscount; you are simply prolonging the final debacle.

You have to get some real money into circulation in this country, in my opinion.

Governor ECCLES. I do not know how, under capitalism, you are going to avoid the debtor and creditor relationship. Communism or socialism, of course, would not——

Mr. GOLDSBOROUGH. I did not even suggest communism or socialism. I did not intimate any such thing as that.

What I am suggesting is that in a country as rich as this is we ought to be stockholders and not bondholders, and we ought to get rid of the enormous creditor element and creditor complex and manipulation which is going on in this country.

That is what I am talking about, and in my judgment, unless it is done, we are ultimately destroyed; the debtor is a slave to the creditor, and the tremendous banking forces of this country absolutely run the country. Either that class has got to take its normal position in society, or else it is going to swallow us all up, and for this reason:

In this machine age where, as a matter of fact, labor is constantly being released from industry, you have got to get some system whereby you can declare a national dividend, either by a direct dividend or by a discount system. It cannot be done in any other way, in my opinion.

I am not suggesting for one minute that we shall revolutionize the banking system in one stroke, but it does seem to me that we are not helping matters any to be saying, "It is not time now; let us wait until next week, or next month, or next year." We have been saying that for 200 years.

Governor ECCLES. I think this bill is taking a very great step forward, and I believe that it is as far as we should go at this time with reference to the matter of control of our system of money.

Mr. GOLDSBOROUGH. Just along that line—and I only have one or two more suggestions I want to throw out—let me say this: During all of the ages the battle of the people has been for a government of laws and not of men; and all of my investigations during a period of 35 years have taught me the truth of a saying of one of the Rothschilds, "If you give me control of the credit and money of a country, I will control everything in it."

So, it seems to me that a legislative direction ought to be directly injected into the monetary system, and that too much discretion, except insofar as the mechanics and the technical phases of the law are concerned should not be left to the administrator. It seems to me it is the duty of Congress to lay down the policy on behalf of the people, that policy to be carried out by technical experts.

Under this bill, members of the Federal Reserve Board—that is, under the bill as amended—who are not necessarily benevolent despots, and who are certainly not immortal, have almost the economic destiny of the American people under their control, without control. Do you think that is a good thing?

Governor ECCLES. I am proposing it. The Board is in session all of the time; Congress is in session part of the time. There is nothing to prevent Congress at any time it is in session giving such instructions by congressional action as it chooses to give to the Reserve Board, which is appointed by the President, and is required to operate in accordance with the Federal Reserve legislation passed, and amended from time to time, by Congress.

I cannot see how it is possible for Congress to operate a money system except through a body such as the Federal Reserve Board, or some other board that they may create for the purposes of carrying out the wishes of Congress, as provided in legislation which Congress passed.

I do not think the proposed legislation in any way takes away from Congress the sovereign power which they have and should have and should retain. It is simply delegating to a body which should represent the Nation and the interests of the Nation, the carrying out of the mandates of Congress.

Mr. GOLDSBOROUGH. Of course, if we are going to assume that Congress has no wisdom in this country, I agree with you.

Governor ECCLES. I am not assuming that.

Mr. GOLDSBOROUGH. But if you are going to assume that Congress has the wisdom it is supposed to have, then it certainly is fair to say that Congress should give legislative direction to those who are to carry out the law.

Governor ECCLES. I think that is being done here.

Mr. GOLDSBOROUGH. It is a declaration of policy.

Governor ECCLES. Yes.

Mr. GOLDSBOROUGH. Which, in the case of a cynical board, would simply amount to a stump speech.

Governor ECCLES. The question of how to make rigid requirements that will better represent the best interests of the people is a question I do not know how to answer, and I doubt if anybody else does.

Mr. GOLDSBOROUGH. I am going to conclude by saying this, that in my judgment what you have proposed is infinitely better than anything we have ever had before.

Governor ECCLES. I thank you.

Mr. CROSS. Governor Eccles, what disturbs me is that it seems that this system upon which you rest, judged by your statement, is that debt is a good thing, and the more debts the better off we are. I cannot figure that out.

You say you think the Budget ought not to be balanced and we should keep going in debt.

Governor ECCLES. No; I did not say that.

Mr. CROSS. In substance.

Governor ECCLES. The Budget must be balanced over a period of time; but I think we should not look at the question of Budget balancing purely on the basis of a year.

Mr. CROSS. No; the more debt you have the more money you create; that is, the more money the banks can create.

As you said a while ago, the banks are prosperous when there are a lot of debts, with high rates of interest. But does that make people prosperous?

Governor Eccles. The intimation is that all debts are created and carried by banks, and that if we in some way can create money without bank credit we have prevented people from getting in debt.

As a matter of fact, the money which we create as the result of bank debt is not very much more than 10 percent of the debts of the country.

Then, what about the insurance companies of this country? One class of people save and pay into an insurance company, and another class make it possible for the savings to return something to their posterity, because somebody goes in debt.

The whole system of capitalism is built up on a basis of debtor and creditor relationship, and the debt that the banks create, or the money they create, is a very small part of the debt. You have not taken the people out of the bondage of debt that you refer to by simply changing the banking system and finding some other method of creating money.

Mr. Ford. If it were possible to create money by a Government just making the money, and if it should just go on paying its bills and making money, would it be necessary for the Government ever to go in debt, on the theory that it can just print the money and hand it out?

Governor Eccles. The Government is a sovereign power, and it has the power to create such money as the Congress appropriates. There is no question about that. It does not have to depend upon the banking system, as I have stated upon several occasions, to provide credit for it. But it is my feeling that that is the most desirable way.

Mr. Ford. If the Government could make all the money it needed, it would not have to go into debt, would it?

Governor Eccles. You mean if it could collect in taxes what was spent?

Mr. Ford. No; I am talking about this idea of running printing presses. If the Government could print all the money it needed, it never would need to go in debt, would it?

Governor Eccles. It could do that, but if it did it to a sufficient extent it would certainly make an inflationary condition which would destroy the value of all money.

Mr. Ford. It would break it down some.

Governor Eccles. Of course.

Mr. Cross. You have to have controlled currency, if you are not going to stick to a metallic base.

Governor Eccles. You have to have a managed currency, and I believe that the present system, through the banking system, with the public interest represented through the Federal Reserve Board, is as desirable a way of controlling the value of money as has been devised in capitalistic economies.

Mr. Cross. The proposition is to devise something more than has been devised, if possible, because under the very system we are talking about you may create debt and prices may rise and you create more debt, and it is inevitable that the crash will come directly, and we go right back into the condition in which we find ourselves now.

Suppose we have a severe crisis, and people commit suicide, or go into bankruptcy, and then finally come out again. Then the same cycle starts over, and you keep going and coming back.

It seems to me we ought to have, if possible, more of what might be called backbone money, or development money or credit-creating money. If we can, we ought to get something that is more substantial than currency, or money that will fade out over night, pocketbook money.

It seems to me our trouble is that when prices begin to fall, this credit money, or check-book money, all vanishes and leaves us helpless, and ruins us.

Governor ECCLES. It would be very fine if we could find some method of avoiding these cyclical changes and always have complete and full employment and business stability. But I do not know of any rule whereby we can accomplish that. We can make that an objective.

Mr. CROSS. You will agree with me on this, will you not? Suppose there was no money; as long as crops were good and people raised plenty, it would be a golden era, would it not?

And if you had currency that would reflect the real exchange values of those things which society needs; if you could get a currency that would reflect the real values of those things in response to the law of supply and demand, we still ought to be in the heyday of prosperity, ought we not?

Governor ECCLES. It depends on whether or not the currency is distributed so that people could spend. If you still had inequitable distribution to the point where a great majority of the people had no money to spend, it would not make any difference whether you used a currency system or some other system. The buying power has to be in the hands of people, no matter what kind of money system you use.

Mr. CROSS. When you trap a lot of people into debt and distress them and they want to eat something, then what would be the result?

Governor ECCLES. But the banking system, as I have indicated, is not responsible for trapping the people into debt. This system of Government loaning agencies, the Howe Owners' Loan Corporation, the Farm Credit Administration, and the Reconstruction Finance Corporation, are three of the greatest credit-extending agencies or creators of debt that we have in the Nation today.

Mr. CROSS. Really, it is just postponing the day of execution, is it not, to shift that from private concerns to the Government? If the Government insists on foreclosing later on it is just postponing the day of execution, is it not?

Governor ECCLES. There is not any question about it; but a debt can be supported when the national income is sufficient to support it. The trouble was that our national income went down in a hurry, and it was going in that direction through the process of bankruptcy and foreclosure. But debt was adjusting itself through that process so that it could be supported by the national income.

Mr. CROSS. What I am trying to get at is this, if it can be done, to evolve a system that is not fatalistic. I believe that if we continue in this helpless condition, in substance, it will get in time where it means the end of capitalism.

Mr. FORD. Governor Eccles, is not the plan you have in mind of creating debt on the part of the Government for the purpose of priming the pump, and when the pump catches and the fluid begins to flow, then let the Government, through its taxing power, wipe out that deficit, and therefore have self-liquidating recovery. Is that not what you want to do?

Governor ECCLES. When you correct the causes for the deficit and the deficit disappears, with an increase in employment and an increase in the national income, the Government's revenues would increase and you would no longer have a deficit.

As private-bank credit expands, and the velocity of existing funds held by corporations and people in banks increases, you would likely have a condition of pretty full employment. At that time income taxes should be increased and not decreased, and Government obligations should be reduced as the community's obligations are increasing. Thus you would be creating a compensatory condition in the money system which would help to iron out the difficulties, if it is done with proper timing. If it is done in that way it would help to iron out the tremendous cyclical depressions which create booms and collapses, which create huge armies of unemployed and the terrible loss of national income.

Mr. FORD. We have that condition now, and we are trying to prime the pump, and by priming the pump create increased business and increased national income, and when the income increases, then the plan, in substance, is self-liquidating, is it not?

Governor ECCLES. Yes.

Mr. WILLIAMS. Governor, I do not know that I have anything additional to ask you about, but there is a feeling among some people, as has already been indicated here, that we should substitute currency for Government bonds, retiring them as they become due, not only what the banks hold, but the entire amount that the Government has outstanding. What would be the result of that?

Governor ECCLES. In the case of the bonds that the banks have, it would increase their reserves by that amount.

Mr. WILLIAMS. What percentage of the bonds outstanding do the banks own?

Governor ECCLES. Oh, I think, of the total outstanding it is somewhere around 44 to 45 percent.

Mr. WILLIAMS. Almost half. What would happen to the rest of them, to the other 55 percent?

Governor ECCLES. Insurance companies are very large holders of those bonds, and the savings banks are very large holders, and the trusts of various kinds, hospitals, educational institutions, and charitable organizations of various kinds, as well as private or individual trust estates——

Mr. WILLIAMS. Would not that release their holdings in bonds and give them currency that might be invested in other securities?

Governor ECCLES. Where other securities are available for such investment. If they were available the excess reserves of the member banks would go into those securities; but what that would create would be an inflation of the security markets, because the volume of money available in relation to the volume of investment securities would cause the bidding up of the stocks and other securities.

Mr. WILLIAMS. Then finally the currency would all come into the banks?

Governor ECCLES. Yes; it would go into the banks immediately.

Mr. WILLIAMS. And in the case of these other institutions that have no use for it for investment purposes, what would they do with it?

Governor ECCLES. They, of course, would deposit the currency in the banks, which would increase the banks' deposits by the amount of the 55 percent of the Government bonds they hold.

As to the bonds held by the banks, it would increase their excess reserves by the amount of Government bonds they held but would not change their deposits.

Mr. WILLIAMS. It would possibly result in the entire amount of Government bonds going into currency being deposited in the banks, increasing their reserves?

Governor ECCLES. That is exactly what it would do.

Mr. WILLIAMS. That would create either one of two conditions. It would present a situation of unlimited inflation, unless——

Governor ECCLES. Unless the reserve requirements were raised by that amount.

Mr. WILLIAMS. It would raise the reserve by that amount, but you would not necessarily have to raise it to the full amount, would you?

Governor ECCLES. You have already over 2 billion excess reserves. You have enough excess reserves now to give you a large inflation; and, if you did not raise reserve requirements by the full amount, you would have additional excess reserves over the 2 billion now held.

Mr. WILLIAMS. Would the fact that the reserves were increased, we will say, to 5 billion, tend to create an inflationary condition? Would that help to make money more easy and induce people or institutions to borrow?

Governor ECCLES. I doubt that it would have any such effect. The rates now on bankers' acceptances and commercial paper, and short-term, high-grade bonds, and Government bonds are almost at the vanishing point, lower than at any time, I suppose, in the history of the country.

But I do not believe that increased reserves, beyond the present excess, would induce any more borrowing or any more lending.

If we begin to get recovery and private credit begins to expand, and the banks increase their investments in securities, and the funds go into the capital markets for building new capital facilities, by the time the banking system had used up their present excess reserves of 2 billion dollars, you would have a volume of money far in excess of anything that the banking system has ever had, and with that volume, with the income velocity that we had in 1927, 1928, and 1929, it seems to me you could have a great inflation, without using any of the increase in the reserves. I mean without using any of the increase in the reserves which would be brought about by retiring Governments through issuing currency.

Mr. WILLIAMS. In other words, the credit expansion potentialities, at least, are as great as you think they ought to be now?

Governor ECCLES. Yes; they are sufficiently great right now, I think, and it would be necessary to carry out open-market operations, or to raise the reserve requirements, before the present excess requirements were entirely used up.

Mr. WILLIAMS. I would like now to get down to section 202 of this bill, with reference to the admission of nonmember banks into the Federal Reserve System, about which you talked a great deal.

In the first place, the bill itself as proposed here provides that the Federal Reserve Board may waive the capital requirements for admission, with the understanding that within the time specified by them the bank admitted into the System makes up those requirements.

Governor ECCLES. That is right.

Mr. WILLIAMS. That is the provision of the bill.

Governor ECCLES. That is right.

Mr. WILLIAMS. As I understand it, the amendment offered by you—I did not understand that you presented any definite language.

Governor ECCLES. We have definite language. I did not submit it here, but I submitted this statement before the committee, and I will read it, if you desire.

Mr. WILLIAMS. I did not understand that you submitted definite language.

Governor ECCLES. Not here, but we are prepared to submit to the committee suggested language, if they desire us to do so.

Mr. WILLIAMS. That is exactly what I wanted to ask you about. I understood your general statement to be that they may waive this requirement and other requirements.

Governor ECCLES. This is what that meant. This provision with reference to the admission of insured nonmember banks is very short. It provides—

On the admission of insured nonmember banks, the Board shall have authority to waive not only capital requirements, but all other requirements for admission, and the Board shall be permitted to admit existing banks to membership permanently with capital below that required for the organization of national banks in the same places, provided that their capital is adequate, or is built up within a reasonable time to be adequate, in relation to liabilities to depositors and other creditors.

Your question was in relation to capital and all other requirements for admission.

Mr. WILLIAMS. What is meant by the waiving of all other requirements?

Governor ECCLES. I have in mind one particular situation. Quite a number of banks that closed during the bank holiday and wanted to reopen found it necessary to get waivers of a certain percentage of their deposits from their depositors. In getting those waivers the banks issued to the depositors certificates of claims for the amounts of the deposits which they waived, which were, of course, secondary to the deposits of the reopened banks, but senior to the stockholders' interest in the banks.

It has been construed by the counsel of the Federal Reserve Board that, under our present Federal Reserve Act, that claim of the depositors is a liability of the bank, and therefore that they cannot figure they have any sound capital so long as those claims exist, whereas those claims are secondary to the depositors' rights.

For all practical purposes, the depositors are as fully protected under that arrangement as they would be if the claim did not exist, and they are given that protection. That is the only case I have in mind at the moment; there may be others.

But we felt that we wanted the language of the bill broad enough to give the Reserve Board the power to get nonmember banks into the system; whereas if conditions were imposed that they could not meet, it would be undesirable, and that was not what the reserve organization felt should be done.

Mr. WILLIAMS. Is it your thought that these capital requirements should be waived permanently, or that they should be required to make them up after they get in?

Governor ECCLES. No, sir; it is our thought that they should be waived permanently, if the capital and surplus which they have is adequate in relation to the bank's liabilities.

Mr. WILLIAMS. And you would consider them solvent?

Governor ECCLES. Yes. For instance, a bank with $40,000 of capital and surplus combined and with a deposit liability of $250,000 has adequate protection for its deposit liability. That is as much protection, on the average, as the deposits have throughout the banking system, as a whole.

Mr. WILLIAMS. The thing that has disturbed me, and has disturbed me very much, is what we are going to do with the 8,500 nonmember banks.

Governor ECCLES. Seven thousand.

Mr. WILLIAMS. That is, the banks which during all these years have not seen fit to come into the Federal Reserve System, and now compelling them to come in if they are going to enjoy any of the benefits of the Insurance Corporation.

Governor ECCLES. Of course, that is not a provision of this legislation.

Mr. WILLIAMS. I understand that, but we are legislating on that subject.

Governor ECCLES. We are simply making it possible to liberalize the Federal Reserve requirements so that the legislation requiring their membership which was passed last year can be complied with without hardship to the nonmember banks.

Mr. WILLIAMS. You understand how it was passed?

Governor ECCLES. It was passed and is in the law; and of course I, personally, am very much in favor of it. I feel that this whole banking policy cannot be successfully carried out so long as you have a substantial part of your banking system not under the Federal Reserve System. The control over your reserves and the control over your money is reduced just to the extent that a substantial part of your banking system is entirely out of the Reserve System.

And, since the nonmember State banks came to the Federal Government in an emergency, the same as the banks under the direction of the Reserve System and/or the Comptroller of the Currency, and requested the benefits of the Reserve System and the Reserve System was rquired to lend to the nonmember State banks at the time of the bank holiday, I believe that in the interest of the nonmember State banks the legislation passed last year, with the amendment proposed, is very necessary and a very constructive thing to require.

I have met with a lot of nonmember State bankers, and I know that they feel that it is against their best interests to be members of the Federal Reserve System. That may have been true in the past, to the extent that they could carry their reserve balances in the city banks and get 2 percent interest, I think, or 1½ percent interest.

Today they get no interest whatever on their reserves in the city banks, and they would be just as well off to have those balances in the Reserve banks now as to carry them in the city banks, whereas that was not true until the time of the Banking Act of 1933.

Another advantage in becoming a member of the Federal Reserve System, that will exist if this legislation passes and that did not formerly exist, is that by the broadening of the eligibility features, it will give them a protection that they did not have before.

The CHAIRMAN. May I interrupt you right there? That means, of course, with the inducements that are offered to the nonmember banks to join the Federal Reserve System. There is not a nonmember bank in the United States that will object to entering into the Federal Reserve System that tends to induce them to come in. Some of them do not want to be forced in, and I do not think you have given all the reasons for it yet.

For instance, one is in connection with the matter of their right to charge for service rendered.

Governor ECCLES. Exchange.

The CHAIRMAN. Which, in the case of a small community bank with a small capital, goes a long way toward meeting their overhead.

And there is another reason. Nonmember banks come in contact with member banks, or the officials of nonmember banks come in contact with the officials of member banks, and they get from those contacts, in addition to what they gather otherwise, impressions as to the desirability of membership in the Federal Reserve System, and there has been unfortunately an accumulation of complaints on the part of national banks that were automatically taken into the Féderal Reserve System.

This question here, if I may say so, comes back to this proposition. It seems to me it must be considered separate and apart from the fundamental thought that enters into the policy that should be finally deermined as to the unification of the entire banking system; that is, our efforts to deal with the emergency that confronts us.

If we attempt to set up requirements of nonmember banks which they cannot meet—if such a provision is put into effect—they can have the benefit of deposit insurance; and I think it is generally conceded that would result in disaster, as a general rule, to small nonmember banks.

Governor ECCLES. It would be suicide for the Reserve Board to set up requirements that the small nonmember State banks could not meet, and thus force them out of the deposit insurance and force them to close. There would be nothing constructive accomplished by any such action as that.

The CHAIRMAN. I here and now register my complete acquittal of you as to any fear of that kind. But we cannot have you in control always. I wish you would live a hundred years, but you cannot.

Governor ECCLES. I do not wish that.

The CHAIRMAN. We do not know who will be Governor of the Federal Reserve Board 5 years from now.

Governor ECCLES. Or next month.

The CHAIRMAN. Or possibly next month.

What happened when we were faced with the complete collapse, or at least the complete closing—I guess it is fair to call it a collapse—of the entire banking system of the Nation in 1933? The bankers were desirous then of having Congress meet, and for once they were willing to meet with Congressmen and confer, and we did confer. We passed the Emergency Banking Act. You know how it was written, I assume.

Governor ECCLES. I read Huey Long's speech after he had voted for it.

The CHAIRMAN. Huey Long was not the only one who felt that way. The entire administration thought that way, and what happened was this—and that is what I was about to call attention to—that the controlling voice in framing that legislation did not come from nonmember State banks in the United States; and the result was that when member banks found they could not get currency enough to pay their depositors and keep their doors open, they arranged for currency to be printed on their assets and supplied to them.

Governor ECCLES. Clearing-house certificates.

The CHAIRMAN. Under the Emergency Banking Act of 1933, as originally passed, we provided for the issuance of Federal Reserve bank notes to member banks, but nonmember banks were not permitted to have that privilege under that act.

Under that legislation, a town of 10,000 or 20,000 population might have two banks, half of the business activity and life of the community being centered in one bank on one corner and the other half in the other bank.

With this situation affecting the Nation under that bill we provided relief for half of that community and its interest and its deposits in the member banks of the Federal Reserve System. And we said to the member bank, "Here is the way you may print money or get currency to take care of your deposits"; and we said to the people of the community interested in nonmember banks, "You take care of yourselves." Of course, that was finally corrected, but it took a struggle to do it.

They have that recollection before them; and there are a lot of just such experiences, not just exactly like that but experiences of that kind that influenced the nonmember bankers; and if we attempt to set up arbitrary standards to force them into the Federal Reserve System, I am not sure that we will not get into difficulties.

Governor ECCLES. If we had a unified banking system at the time you refer to, the question as to whether or not a bank could get the benefits of advances from the Federal Reserve bank and receiving therefor Federal Reserve bank notes would not have come up.

The question came up, because here was a system set up for member banks, and all banks had been invited to join the Reserve System from its very beginning. An emergency developed after a period of 20 years, and those banks that had not taken advantage of the opportunity to join wanted in the emergency, the benefits of a system of which they were not members.

I recognize that it was in the public interest to do just what was done.

The CHAIRMAN. What was finally done, but not what was done so long as we were moving under the counsel of one class of bankers.

Governor ECCLES. But I do think that the possibility of the recurrence of such a condition should be prevented by getting a unification of the banking system. I believe you will never have in this country a banking system that can withstand the pressure of periods of financial distress, and we will never have a sound, dependable banking system until we get a unified banking system. And neither do I think it will be possible to exercise through monetary policy the same control over the money system when a substantial number of banks which create money just the same as the member banks are subject in no way to the regulation or control of the authority that is responsible for monetary action.

I have been in the banking business for a period since 1913, a period of 22 years, up until the time I came over here a little more than a year ago.

My first banking connection was with about a million-dollar bank which joined the Federal Reserve System shortly after the Federal Reserve System was organized. It is a State bank. From that period a banking organization of over $55,000,000 was built up, operating over 25 banks, national and State, member and nonmember.

I found, as the result of experience, that it is in the interest of a bank to be a member of the Federal Reserve System, whether it be a small country bank or a substantial sized city bank; and I am stating here my honest conviction of what, as a result of experience and as a result of study for a period of years, I feel is in the public interest and in the bankers' interest.

And I believe that the great majority of the nonmember State banks, if they understood this problem, could be induced, in their own interest, to become members. I have found in talking, as I have upon many occasions, to nonmember State bankers, that invariably they can be sold upon the idea, and the difficulty today with very many of them is a lack of understanding and lack of information with reference to the problem.

The CHAIRMAN. I think one reason why they have not wanted to come in was because they did understand. When a bank becomes a member of the Federal Reserve System its other connections are practically terminated.

Governor ECCLES. You mean its other banking connections.

The CHAIRMAN. Yes; its other banking connections. So far as obtaining relief in an hour of need is concerned, those connections are terminated, and any small bank, a member of the Federal Reserve System, would be dependent upon its Federal Reserve bank for relief in the hour of difficulty, as a general proposition. I think that is undeniably true.

Governor ECCLES. Not altogether, because every bank carries usually an account or two with a city correspondent.

The CHAIRMAN. Sometimes they do, but they do not always do that.

I can point you to instances in my own district where a bank in a town of not over 20,000 population was allowed to close. I know the history of it.

I know that there were criticisms and faults to be found with the management, and its papers were not all desirable. But the bank came very near liquidating 100 percent to its depositors during this depression. The Federal Reserve turned them down and abandoned them.

That very institution, if it had not been a member of the Federal Reserve System, and had kept up the other connections that would have existed, in all human probability would have been able somewhere to have secured relief to tide them over their difficulties.

Of course, that is one instance that happened many times.

I want to say in that connection that I think the story would have been different if we had then the experience we have gathered since that time and had had the legislation now proposed and had it administered with some degree of common sense.

Governor ECCLES. I think that there was a lack of power for the Federal Reserve banks to extend the relief that they should have been able to extend; there is not any question about that.

The CHAIRMAN. In connection with what I said, I want to add this, that I have not the slightest doubt that this legislation, if it is administered as I think it will be, and I believe it will be in the light of our experience, with a more liberalized view of the situation to be reflected in the administration of the Federal Reserve System, will induce many State nonmember banks to join the Federal Reserve System voluntarily.

Governor ECCLES. There is not any question that the Reserve banks were extremely rigid in their credit extension, in their interpretation of eligible paper. As the depression proceeded and as deflation continued, the attitude and the action of the Reserve banks, based upon my experience, and I know upon the experience of thousands of other bankers, was to the effect that the Reserve banks became more rather than less restrictive.

I think the experience of the past has been a very salutary one, and I agree with Mr. Steagall that, if this legislation is passed and is administered with understanding and in the spirit that has motivated the legislation, a repetition of the banking catastrophes that we have had in the past would be impossible.

Mr. CAVICCHIA. The other day, Governor, I asked you if this bill aimed at a centralized banking system, or whether it was merely regulatory.

I notice this morning you used the word "unification." As I understand it, this bill aims at unifying the National and State banking systems under the Federal Reserve System; am I correct?

Governor ECCLES. No; this bill does not deal with that problem at all. That matter was covered by the legislation which was passed in 1933.

Mr. CAVICCHIA. In what sense did you use the word unification?

Governor ECCLES. I was simply stating that I thought a unification of the banking system was necessary, and according to the legislation that Congress passed in 1933 unification will be brought about by 1937, when the nonmember State banks will be required to become members of the Federal Reserve System in order to get deposit insurance.

Mr. CAVICCHIA. And your program is to unify the banking systems?

Governor ECCLES. No; that is the program which was passed, and which I am favorable to.

Mr. CAVICCHIA. The aim of the legislation we passed and that which we are now considering it to unify the banking systems, whether it be National or State?

Governor ECCLES. That is correct.

The CHAIRMAN. You mean this legislation was not designed to accomplish that purpose, but its purpose was of another nature, and you merely accepted the existing law with reference to unification.

Mr. CAVICCHIA. You still have the two systems.

Governor ECCLES. This legislation only facilitates the carrying out of the legislation which has been passed, without imposing unnecessary hardships on the nonmember State banks.

The CHAIRMAN. You might state your views to be that a proper interpretation and understanding of the proposed legislation is that it really liberalizes the requirements heretofore imposed in the act of 1933.

Governor ECCLES. Yes.

Mr. WILLIAMS. I want to ask whether or not you think that State legislation authorizing the creation of State banks ought to be entirely abolished, making it one system, sure enough.

Governor ECCLES. It is my personal belief that that may be desirable, but it is impracticable at the present time.

In practically every other country in the world they have one banking system; and, as the result of that, they have, I believe, avoided many of the banking troubles which we have had. But we are young, and I do not believe that we can make changes in our methods and habits too rapidly. We cannot go faster than the people of the country are willing to have us go.

Mr. WILLIAMS. It seems to me we are inevitably going to that, and I have the view in reference to the general philosophy of the legislation that we are certainly going in that direction.

If it is desirable, as you think—and I am not controverting that here—to have the entire system under a central control, so far as the monetary policy is concerned——

Governor ECCLES. That is what this would do, without eliminating the State banking departments.

Mr. WILLIAMS. Undoubtedly; but it brings them into the picture, subject to that policy.

Governor ECCLES. Not so far as the examination of banks is concerned, and not so far as the chartering of banks is concerned; but it does unify the System by placing State banks under the influence of monetary policy of changes in Reserve requirements and changes in discount rates.

Mr. WILLIAMS. If we are going to bring them into one system, I can see no reason at all for the further existence of State banks. I cannot see the necessity of having a separate examination of them.

Governor ECCLES. There is not any question but what there are many improvements that can be made in the banking system that the proposed legislation has not provided for. But I believe that banking legislation must be evolutionary and not revolutionary. We cannot expect in one session of Congress to get all the banking legislation we want, when we take into account the size of the country and the habits of the country, the adverse and diverse opinions. Therefore, what has been proposed here, it seems to me, is about as far as we could expect to go at this time with reference to banking legislation, and the question of other problems of banking legislation which have been discussed from time to time, such as the matter of unification, the examining problem which you raised, Mr. Williams, and the question of branch banking has come up a good many times here and it has come up in many State legislatures. All of those problems are problems which will come up from time to time for consideration. There is not any question about that.

Mr. CLARK. The Federal Reserve System as it has existed and has been administered, as Mr. Steagall pointed out, has not been sold for some reason or other to thousands of banks throughout the country that did not want to join, whether they understood the facts or not.

In title II of this proposed legislation, if it is passed, I think, personally, you have an article that will sell the System, if properly administered.

But why do you think it is necessary to use the F. D. I. C. as a club to force the sale of an article that ought to sell on its own merits?

Governor ECCLES. I think that membership in the F. D. I. C. should be confined in the future to member banks. In 1933 it was found that the Federal Reserve System was the only agency that could provide liquidity to the banking system and thus enable the banks of the country both member and nonmember banks, to reopen and to make available the depositors' money. This had to be done at that time by the Federal Government, even though it had nothing whatever to do with the chertering or the supervision of nonmember banks. The Government had the responsibility through the Reserve System of giving them the benefits and the protection of that system in the same manner in which it was accorded to member banks.

Now, I do believe that, in the public interest, after a reasonable time—and 1937 is a reasonable time—and after providing a liberalization of the requirements of membership, any bank which is being insured by the Federal Deposit Insurance Corporation should be required to become a member of the Federal Reserve System for better protection to the Federal Deposit Insurance Corporation. Although it is a bank mutual insurance plan, at the same time the moral obligation of the Federal Government is there; because the public looks to the United States Government to make that insurance company solvent if the banks cannot or do not.

Mr. CLARK. You think, that the insurance features of the F. D. I. C. are so closely involved with the entire banking system that it is good practice in this instance, whereas ordinarily it would not be, to use one agency as a club to force membership into another agency; that they are so interrelated and tied up that it is a fair thing to do.

Governor ECCLES. I agree with you. I do not like the use of a club at all in dealing with human problems. The F. D. I. C. and the Federal Reserve System are so closely interwoven that it is necessary in the public interest to require membership of insured banks; but I do not like to look upon the use of the F. D. I. C. as a club.

Mr. CLARK. That has been suggested several times while we were discussing title I, and that is why I used the term. I merely wanted to get your statement in the record because numerous State banks have written members of the committee raising that very question, stating, in effect, that they were being clubbed by a desirable institution into joining the System, which, as presently constituted, they do not like.

That is one reason why I wanted to get your views in the record so that we might have the entire picture.

Mr. HOLLISTER. With respect to section 210, which pertains to the lending power of national banks, are you going to mention that?

Governor ECCLES. That is just what I was going to refer to.

Mr. HOLLISTER. I was just going to bring that out.

Governor ECCLES. I wanted to put in the record a suggestion with reference to section 210, which is the provision dealing with real-estate loans, a section that has possibly been misunderstood as much or more than any other section, and a section which has been discussed here, possibly, as much as any other section.

I recommended before this committee that, instead of providing in the bill a specific maximum amount based on appraisal that could be loaned, a specific maximum period, and a maximum amount of time funds, that there should be more flexibility, and that the Reserve Board should be required to make rules and regulations governing the making of real-estate loans by member banks.

There are many reasons for that which I do not think it is necessary to review here. It has been suggested that it would be desirable, and that the proposal would be far more acceptable to the bankers in general, if there were a limitation of 60 percent instead of the 75-percent limitation placed in the legislation; that is, to permit the Board to make rules and regulations with reference to real-estate loans, with the limitation that no loan made after the passage of this legislation or after the promulgation of the Board's rules and regulations could exceed 60 percent of the appraised value of the property.

I see no objection to that. I do not believe the banks would loan more than 60 percent on the appraised value in any case.

My purpose in suggesting the 75 percent was not with the expectation that the banks in the future would loan 75 percent of the appraised value of the property; but it would enable them to carry the more than 2 billion of real-estate loans which they have, which, due to depreciation values, are in excess or 50 percent in many cases, possibly as high as 65, 70, or 75 percent in some cases. It would permit them to carry the loans they have and extend them over a long period with an amortized basis of payment, rather than to bring pressure on the borrowers because the examiners bring pressure upon the banks, to reduce these loans to the 50-percent limit, which would force the borrowers on to the Government, through the Home Owners' Loan and the Farm Credit Administration.

I would like to see the banks able to carry the real-estate loans they have, even though they are in excess of 50, or 60, or 70 percent, and to refund those loans.

But I think a 60-percent limitation is desirable in the case of making new loans in the future. I have no objection to it, and would like to recommend that, in connection with giving the Federal Reserve Board the authority to make rules and regulations, such a limitation be put upon that authority.

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The CHAIRMAN. We have concluded with Governor Eccles, and I want to thank you, in behalf of the committee for your faithfulness in attending these hearings, and for the very able presentation you have made of this legislation. All of the committee, I am sure, cannot agree with everything you have said, but we agree with you.

Governor ECCLES. I appreciate your courtesy and the patience which the members of the committee have accorded me.

Statement on National income, money, and income velocity, submitted by Gov. M. S. Eccles

	National income, Copeland [1] (billions)	National income, Department of Commerce (billions)	Money [2] (billions)	Income velocity based on Copeland (I÷III) (times per year)	Income velocity based on Department of Commerce (II÷III) (times per year)	Percentage change in income, Copeland	Percentage change in income, Department of Commerce	Percentage change in money	Percentage change in income velocity, Copeland	Percentage change in income velocity, Department of Commerce
	1	2	3	4	5	6	7	8	9	10
1921	56.8		21.7	2.62						
1922	60.3		21.5	2.81		+6.2		−1.2	+7.3	
1923	68.9		22.6	3.04		+14.3		+5.5	+8.2	
1924	70.2		23.1	3.04		+1.9		+1.8		
1925	74.5		24.6	3.03		+6.1		+6.7	−0.3	
1926	78.8		25.3	3.11		+5.8		+2.9	+2.6	
1927	80.9		26.0	3.11		+2.7		+2.8		
1928	83.3		26.4	3.16		+3.0		+1.3	+1.6	
1929	87.0	82.3	26.4	3.29	3.12	+4.4		+0.1	+4.1	
1930		75.8	25.4		2.98		−7.9	−3.8		−4.5
1931		63.3	23.8		2.66		−16.5	−6.3		−10.7
1932		49.7	20.5		2.42		−21.5	−13.9		−9.0
1933		46.8	19.9		2.35		−5.8	−2.9		−2.9
1929–33							−43.1	−24.6		−24.7

[1] Less imputed nonmonetary incomes.
[2] Deposits subject to check plus cash outside banks as of June 30.

MODIFICATION IN THE BANKING BILL OF 1935 PROPOSED BY GOVERNOR ECCLES IN HIS TESTIMONY BEFORE THE HOUSE BANKING AND CURRENCY COMMITTEE

1. SEC. 201. The governors and chairmen and vice governors of the Federal Reserve banks shall be approved by the Federal Reserve Board every three years rather than annually, so that their terms as governors would coincide with their terms as class C directors.

2. SEC. 202. On the admission of insured nonmember banks, the Board shall have authority to waive not only capital requirements, but all other requirements for admission, and that the Board be permitted to admit existing banks to membership permanently without requiring an increase in capital, provided their capital is adequate in relation to their liabilities.

3. SEC. 203. The pension provision shall be modified so that any member of the Board, regardless of age, who has served as long as five years, whose term expires and who is not reappointed, shall be entitled to a pension on the same basis as though he were retired at seventy. That is, he is to receive a pension of $1,000 for each year of service up to twelve.

SEC. 205. Authority over open-market operations shall be vested in the Federal Reserve Board, but that there be created a committee of five governors of Federal Reserve banks, selected by the twelve governors of the Federal Reserve banks, and the Board shall be required to consult this committee before adopting an open-market policy, a change in discount rates, or a change in member-bank reserve requirements.

5. SEC. 209. The Board shall not have the power to change reserve requirements by Federal Reserve districts, but only by classes of cities. For this purpose banks shall be classified into two groups: one comprising member banks in central reserve and reserve cities, and the other all other member banks. Changes in reserve requirements, therefore, would have to be either for the country as a whole or for the financial centers, or for the country districts.

6. SEC. 210. The conditions on which real-estate loans may be granted by member banks shall be left to the discretion of the Federal Reserve Board to be determined by regulation. No real-estate loan hereafter made shall exceed 60 percentum of the appraised value of the property; but this shall not prevent the renewal or extension of loans heretofore made.

7. It shall be the duty of the Federal Reserve Board to exercise such powers as it possesses to promote conditions making for business stability and to mitigate by its influence unstabilizing fluctuations in the general level of production, trade, prices, and employment, so far as may be possible within the scope of monetary action.

(Thereupon, the committee took a recess until 3 p. m., this day.)

AFTERNOON SESSION

The CHAIRMAN. Dr. Goldenweiser, you have heard the discussion that has taken place in connection with this bill, H. R. 5357. The committee would like to have you discuss the legislation, and I assume that it is to be desired that you give us the benefit of your judgment in the way of explanation of the legislation embodied in title II, in its technical aspects, so that all of us may have a clearer understanding of its mechanics.

Mr. GOLDSBOROUGH. Mr. Chairman, I do not know whether this suggestion is desired by Dr. Goldenweiser, but on various and previous occasions he stated that, in view of the fact that he was on the staff, he preferred not to give his opinion as to matters of policy.

The CHAIRMAN. I undertook to intimate to him that it is not desired to lead him into that field, but that he give us the benefit of his explanations of the mechanics and the technical part of this bill.

STATEMENT OF DR. E. A. GOLDENWEISER

Dr. GOLDENWEISER. Mr. Chairman, I would like to make a brief statement before you ask me questions, if I may. I have not prepared a written statement. One reason that Governor Eccles thought it would be desirable for me to testify was that I could make it somewhat clearer how the provisions of this proposed legislation have been developed out of the experience of the Federal Reserve System under the provisions as they are in the law today, and it is along that line that I should like to make my opening remarks.

I want to state for the record that anything that I say that is not purely factual expresses my own personal opinion, and I am not speaking for the Federal Reserve Board. In my opinion, this bill accomplishes two important purposes: One is to clarify and fix more definitely the responsibility involved in the administration of the Federal Reserve System; and the other is to improve the administration of the credit machinery that the System sets up.

The proposals do not involve as much change from existing law as has been intimated, chiefly in the comments and the general impression in the discussion of the bill outside of this room.

I should like, with your permission, to discuss in some detail a few of the sections of the bill on which I can, perhaps, add a little light, and then leave it to you to ask me such questions as you may desire.

The first section of the bill—and I am speaking entirely of title II of this bill, H. R. 5357—the first section is one that arranges for combining the offices of governor and chairman of the Federal Reserve banks, and to make the appointment of the person to occupy the position subject to the approval of the Federal Reserve Board. It has been explained to you just why it is necessary that the Board be consulted, and I shall not discuss that phase of it, but I would like to say a few words about the effect of this dual organization under which we have been functioning for 20 years, which has, in part, not proved entirely satisfactory, either to the banks or to the Board. In many cases it has worked very well. In the final analysis, it is all a question of personalities, but you are setting up a charter for the bank, and you ought to provide against the possibility of undesirable contingencies developing, rather than to depend on human qualities to be such as to result in smooth administration, even though the machinery be calculated to produce the reverse.

I do not want you to get the impression that in numerous cases it has worked in an unsatisfactory manner, but still there have been cases where it has worked in an unsatisfactory manner.

Under existing law and practice the Federal Reserve bank has two heads: The chairman of the board, appointed by the Federal Reserve Board, who is also a class C director and is also the Reserve agent and the Federal Reserve Board's local representative in the banks; and then it has the governor, who is appointed by the directors and is responsible entirely to them, except that his salary is subject to approval by the Federal Reserve Board and he is subject to removal for cause.

In most cases it has worked out that the governor has been the principal executive officer of the bank, although there have been cases where, as a matter of personal equation, the chairman has been the principal executive officer. It has been a question of personalities, as to which one has been dominant. It seems clear that it ought to be made perfectly plain in the law just who is going to run the banks, whether it is going to be the chairman or the governor, and the only way to do that, without defining their duties in very great detail, is to combine the offices.

We have had cases where the chairman and the governor did not get along, where the chairman might have used his prerogatives as chairman to try to keep the governor out of the meetings of the board of directors, which seems absurd, and there ought to be no legal possibility for such a situation. We have had cases where of two men one was first governor and then chairman, and then they reversed themselves and the one that had been chairman became governor, and vice versa, and they continued to be at cross purposes. Usually the Federal Reserve Board feels that it is desirable for it to communicate with the banks through the chairman of the board of directors, who is the Federal Reserve Board's representative on the premises. As it has worked in practice, in some cases it has been merely a matter of routing the mail to the governor, who is the executive head of the bank, through the chairman. In some cases, however, where the chairman happened to be jealous of the prerogatives of the governor, it has sometimes resulted in the Board's addressing the chairman and the information not reaching the governor, who has the responsibility for the running of the bank.

It has particularly happened in cases where the governor might be away and the deputy governor, while actively in charge of the bank, would not receive the information coming from the Board to the chairman, and yet the deputy would be the man whose responsibility it was to run the bank.

Now, those things will happen. They are bound to happen so long as we have a set-up where you have two heads responsible and performing different functions. It cannot be expected in all exigencies of daily life and personal equations for them always to be the kind who will talk it over and get along smoothly in their operations. In most cases, they have done that, but there have been cases where they have not.

This proposal will do away with this difficulty and, at the same time, will save the system a considerable operating expense, and will result, I think, within the banks, in smoother operation and also in smoother cooperation between the banks and the board.

The agent's department or the chairman's department in the bank has had several functions of the bank under its charge. It has had the examination division, and the bank-relations division, and the economic services, and while that has worked very well in many cases—you will forgive me for taking a particular interest in the economic services, with which I am connected, myself—the fact that they are connected with the chairman, who is not the executive head of the bank, has been an additional handicap in making those divisions function in a way so as to have the information that they collect, and the material which they assemble, finding its way into the hands of the operating officials, who would use it in formulating policies.

The only purpose of the economic services of the Federal Reserve System is to give the operating officials of the banks and their boards the kind of information that they require for their work, and anything in the nature of a hurdle between the economic services and the bank officials is a handicap to the effective working of the economic services, and I think it has seen that to some extent.

Those are the reasons, as I see them, for combining the offices. Those are the reasons that appeal to me, and the fact, as I said, that the combined officer needs to be approved by the Federal Reserve Board, it seems to me, almost goes without saying, because the Board is given the power to appoint the chairman, and it must naturally have the power of approval of the joint officer.

I have not anything to comment upon in the section that deals with the admission of insured banks into the Federal Reserve System. It seems to me that the Governor covered all of that, all that I can think of on the section.

In connection with the qualifications of the Federal Reserve Board, which this bill provides for, the principal thing in the way of their qualifications is, that instead of having it stated that they should be appointed with due regard to agricultural, industrial, and geographical interests, there is substituted a statement that they should be persons, who by training or experience or both, are qualified to formulate economic and monetary policies. It seems to me that that substitution is a very good one, because it states the qualifications of the members of the Federal Reserve Board in terms of the principal function which they have to perform, and because it does away with the idea that the board should consist of representatives of different groups of the population, this man representing agriculture, this man banking, this man trade, and so on. It is better that each member of the Reserve Board, as a matter of law, should feel that he represents the country as a whole, and the interests of the country as a whole, and his job on the Board is to be engaged in the formulation of national credit and monetary policies.

I think that the insertion of that qualification into the text of the law is recognition of the growing conviction on the part of the country that the Federal Reserve System's functions are much broader than was clearly understood at the time the Federal Reserve Board was organized. At that time, it was largely conceived that the Board should be a representative Board and that it should represent the different sections of the population, so that none of them would fail to receive equal consideration. Of course, that is important, and it will continue, but an explicit provision for a national, nonpartisan board, that has the sole objection of serving the interests of the people as a whole, with particular reference to those duties that deal with the quantity and cost of money is an advantage.

It is along the same line as the proposal which Governor Eccles has read to you, stating the objectives of the Federal Reserve System in terms of maintaining the stability of various elements of the business structure, that is, to have men on the Board who will devote their energy to maintaining that stability insofar as it can be maintained by monetary means, and men who should be qualified to formulate national policies.

I would like to say, in this connection, that the idea that the Federal Reserve Board has broader responsibilities than the mere accommodation of commerce and business and the serving of agriculture, trade, and industry, is an idea which has been forced upon the Federal Reserve System by actual experience and which has been gradually developed in the System.

The accommodation of commerce and business, which is the only objective that was mentioned in the Federal Reserve Act, is a vague phrase, and has all of the attributes of a statesmanlike pronouncement. It is vague, it is a glittering generality like the Declaration of Independence, and its content can be changed as circumstances change. It has, therefore, not served any very useful purpose, but has not done any particular harm.

It is now time, in the light of 20 years' experience, to substitute a more clearly defined objective than this vague phrase, which, to my way of thinking, held the place for a more definite objective throughout these years.

As I say, the objective which has been suggested by Governor Eccles and the one that you have clearly in mind, is one that has been gradually evolving. You know, Mr. Chairman, and the other members of the committee, that you have had a great many hearings on various bills for a number of years, and I remember particularly the hearings in 1928, when Congressman Strong, of Kansas, was recommending price stability as the objective of the Federal Reserve System.

The Federal Reserve System, at that time, opposed that particular objective, largely on the same grounds that Governor Eccles stated here he would oppose it as the sole objective now. At that time, former Governor Hamlin, of the Federal Reserve Board, submitted to the committee his alternative for that proposal, which, with your permission, I would like to read. What he suggested was this:

> The Federal Reserve System shall use all of the powers and authority now or hereafter possessed by it to maintain a stable gold standard and shall furnish credit facilities commensurate with the requirements of credit stability of agriculture, industry, employment, and the purchasing power of the dollar, so far as such purpose can be accomplished by monetary and credit policy.

I think, with some allowance for changes in fashions as to terminology and for the fact that, at that time, the gold standard was taken more or less for granted, that the objective that Governor Hamlin proposed in 1928 is very similar to the one that Governor Eccles is proposing now.

I call this to your attention in order to indicate that the proposals presented before you now have definite roots in the history of the Federal Reserve System; that they have been developed as part of the System's experience, and, for that reason they are hoped to be and expected to be well adapted to the more effective carrying on of those purposes for which the Federal Reserve System was organized.

The next section on which I should like to make a word of comment is the one that has to do with the open-market operations, and that is entirely in line with what I have been saying on the other sections.

The necessity of having a national body control changes in the cost and volume of money is almost too obvious to require explanation, or to need emphasis, because so far as I can gather, this committee is convinced of the necessity of national responsibility for this national function. The Federal Reserve Act, at the present time, provides that the Federal Reserve Board have power over the discount rate, and over reserve requirements, with the approval of the President. So that two of the powers of monetary control, or monetary regulation, are in the Federal Reserve Board, and it seems only logical that the third power should be vested in the same authority.

I might say a word here about the legal phase of it, on which I feel a little reticence, because I am not a lawyer, but it appears to me, after some consultation that the Federal Reserve Act, as originally drawn, was intended to give the Federal Reserve Board the power to initiate open-market operations. It did not say so anywhere in so many words, because, at the time it was written, open-market operations were a relatively minor matter; there were practically no Government securities outstanding, except those that were in back of the national-bank notes, and the open-market idea had not yet developed.

But the Board has the power to fix the discount rates. It has been argued by counsel that under the original act the Federal Reserve Board probably had implied power to order open market operations. The Board's having authority over the discount rate has been questioned. The law says that the rates shall be established by the Federal Reserve banks, subject to the review and determination of the Federal Reserve Board, but the Attorney General of the United States held in 1919 that that meant that the Federal Reserve Board could establish the discount rate, and on one occasion, at least, the Federal Reserve Board has done so.

Mr. HOLLISTER. May I interrupt? I know that is not your regular way of doing it, but do I understand you to say that the counsel of the Federal Reserve Board raised a law question as to the law giving it the right to compel all of the regional banks to enter the open market operations?

Dr. GOLDENWEISER. I do not like to speak for the counsel. If you will wait one second, I think I will make that clear. I meant to say that under the original Federal Reserve Act, prior to the Banking Act of 1933 it could be argued that the Board had the power.

I think that when the Banking Act of 1933 was being formulated, the intention was to strengthen the Board's authority, because that is indicated in more details that you would care to take the time to consider now. But they put in a separate section (12a), and they put this clause there, that no Federal Reserve bank shall engage in open market operations, except subject to the regulations of the Federal Reserve Board, the same language more or less which appeared in another section.

Similar things were done very frequently in the Banking Act of 1933, where the same powers are mentioned over again, in order to emphasize the will of Congress that they should be exercised, and I think it is a fair construction to say that it was intended to increase the powers of the Federal Reserve Board over open-market operation. But when that act was passed there was established a statutory open-market committee, which had previously been a voluntary committee, without any legal sanction, and it was given special powers over the open market, and then there was put in a separate section, which says that the Federal Reserve banks shall have authority to decide whether they shall participate or not. As a consequence, I think that there can be no question whatsoever that, under the law as it stands today, the Federal Reserve Board does not have authority to initiate open-market operations, or to see to it that they are carried out, even after the committee has recommended them and the Board has approved them.

It is proposed here to go back to the original Federal Reserve Act and to go a little further in clarifying what was probably authorized, and putting it into perfectly clear language, and placing perfectly clear-cut authority and responsibility on a national body, the Federal Reserve Board.

I suggest that, if you modify that and give actual voting power to the representatives of the Federal Reserve banks in the committee that is going to determine the open-market policy, in my opinion, you will not be restricting new, additional powers requested by the Board, but would be giving the regional banks more power in this matter than they have had since the establishment of the System; because, even under the existing law, the committee cannot move without the approval of the Board.

If the committee makes a recommendation and the Board disapproves it, they cannot carry it out, and the Governors have no vote on the Board in passing on these recommendations of the committee. So that, as a matter of fact, the committee that is actually proposed in this bill, which the Governor has suggested to modify, would give the Governors of the Federal Reserve banks more power in the determination of open-market policies than they have ever had. Rather than the Board getting more power by this proposal that is now before you, the proposal that is now before you would only clarify and make perfectly plain and clear the power which probably existed in the Federal Reserve Act prior to the Banking Act of 1933. Whereas a committee in which the governors participated in voting, would give them more power than they have ever had before.

The CHAIRMAN. Give them more power in the inauguration of policies?

Dr. GOLDENWEISER. Yes.

The CHAIRMAN. But that would take away from them the power to nullify the policies that had been inaugurated and later approved by the Board?

Dr. GOLDENWEISER. That is correct; yes.

Hr. HOLLISTER. Is there such a difference between an affirmative right and a negative right?

Dr. GOLDENWEISER. Yes; I think so.

Mr. HOLLISTER. This, for the first time, makes it perfectly clear that the regional bank may be compelled willy-nilly to participate in the open-market operations?

Dr. GOLDENWEISER. The clear-cut statement of the power is new; prior to that, it was an implied power and was not clear. I think, since 1933, the power has not existed, and I think now it is proposed to restore it and make it perfectly clear.

Whether you wish to do it or not is not for me to discuss, but I was trying to make clear that the alternative suggestions are in the nature of giving the governors more power than they have ever had before.

Mr. HANCOCK. May I ask you one question right there?

Dr. GOLDENWEISER. Yes.

Mr. HANCOCK. Do I understand that your suggested amendment to the act, as proposed by Governor Eccles, and discussed by him, that is, the open-market committee of the governors, would have any authority as far as formulating the policies is concerned?

Dr. GOLDENWEISER. The committee of the governors would be a consultative committee——

Mr. HANCOCK. In my understanding, from what he said, was that, under his amendment, this committee would be an advisory committee?

Dr. GOLDENWEISER. It would have no powers, other than to make recommendations to the Board. However, the Board would, under that amendment be required to obtain that advice before it took action, either open market or——

Mr. HANCOCK. And they would obtain advice on a policy which they had formulated, rather to receive, in the first instance, a policy formulated by the committee; is not that correct?

Dr. GOLDENWEISER. That is correct, except there is nothing to prevent that committee from recommending policies, if it chooses. It has no power to initiate them, but it has the power of recommendation and——

Mr. HOLLISTER. It has not any power at all?

Dr. GOLDENWEISER. The power of recommendation is the power that anyone may have to suggest something, but it has no statutory power other than to make recommendations.

Mr. HOLLISTER. There is no power except the power of suggestion?

Dr. GOLDENWEISER. That is right. I would like, on the subject of open-market operations, to say one or two other things in line with what the chairman mentioned, their mechanics.

We have had this system operating in the open market on a considerable scale for 13 or 14 years. When the system was first organized, it met the war emergency, and that was merely a matter of supporting the Government, and it was a matter of discounting paper secured by Government obligations in order to enable the Government to finance its war needs.

After the early period and after the liquidation of 1920 and 1921, the Federal Reserve banks found themselves with a very small volume of earning assets. There was in the market a large amount of Government securities, and so, quite naturally, in 1922, the Federal Reserve banks began to buy Government securities for the purpose of having enough earning assets to meet their expenses. That did not last very many weeks before it began to cause difficulties for this reason: That the market for Government securities and all securities, essentially, is in New York. So that when the Federal Reserve Bank of Kansas City—I am using that as an example—would, for instance, want to buy $10,000,000 of securities in the New York market, what it would do would be to draw a check in favor of a New York broker, the New York broker would deposit the check in a New York bank, and the New York bank would then get that much more gold through the gold settlement fund, put it to its account at the New York Federal Reserve Bank, and this bank would use that balance to extinguish that much of its indebtedness.

So that the consequence of the banks in the interior buying Government securities was to reduce the earning assets of the New York Federal Reserve Bank which was not, of course, particularly pleasing to the Federal Reserve Bank of New York, and which did not change the total earning assets of the Federal Reserve System. So that one bank would be increasing its holdings at the expense of another bank, and the aggregate earning assets would remain constant.

Furthermore, these purchases by the banks, the uncoordinated 12 Federal Reserve banks, were creating considerable disturbance in the Government bond market, and Parker Gilbert, who was Under Secretary at that time, was disturbed about that. It was not long before it was decided that open-market operations must be coordinated.

A committee of five Governors was appointed to coordinate those purchases. That committee, with rather narrow and limited purposes, one of which was to see that purchases do not unduly upset the Government bond market, functioned for about a year, and during that time the Federal Reserve System did a lot of hard thinking and saw a lot of things developing with which they had not had experience before. They noted that the purchases of Government securities resulted in decreased discounts and in no increase in the total earning assets of the Federal Reserve banks. The Federal Reserve Board suggested in the spring of 1923, and it was agreed, to reorganize the committee, and to create a Federal Reserve System Open Market Investment Committee, which would have the duty to make recommendations in regard to open-market policies; and at that time, the policy was established that those purchases should not be made with a view to earnings because the Federal Reserve System could not afford, and the country could not afford to have the Federal Reserve System run with the view to maintaining its earning capacity.

The Federal Reserve System's duties are entirely different; they relate to monetary control, and it is not their business to worry about earnings; they have to disregard them as a principle of their operation.

Now, in 1923, this open-market committee that was set up established the principle that the open-market policy should be on the same principle as the discount-rate policy, which at that time was the phrase which I referred to before, the accommodation of commerce and business, and with refernce to the general credit situation.

This language clearly had in mind the exercise of the right kind of influence on the business situation. The fact that they meant that is entirely clear from the kind of information on which decisions were based.

From 1923 and until 1930 or so, that committee functioned, and during that period the Federal Reserve engaged in a large volume of open-market operations. Those operations were undertaken in the light of information, in the collection and compilation and organization of which the Federal Reserve System had been the pioneer, and had collected the kind of information which had not been available anywhere before. That information was along lines of keeping track of the physical volume of industrial production, the movement of goods through the channels of trade to consumers, the movement of imports and exports, employment, pay rolls, commodity prices, retail prices, stock-market securities; all of those factors, in addition to changes in deposits and loans and investments, and the different kinds of loans and investments of the different banks, and also foreign exchanges and gold movements.

In other words, the Federal Reserve System based its decisions in open-market policies on a whole array of economic factors that were available, and that were made available by the efforts of the Federal Reserve System, to serve as a basis for these decisions.

The sort of information that the Federal Reserve System uses is indicated in this book of charts, of which every member of the Federal Reserve Board always has one on his desk, and which covers the subjects that I have just enumerated.

The reason I bring that out is to show that the policies and objectives and ideas, which are now incorporated in the objective that Governor Eccles proposed, are the same policies, the same objectives, and based on the same general factual material as that which has been gradually evolved in the Federal Reserve System through actual experience. In the securing of this information, the Federal Reserve System has played a pioneering part.

This committee functioned from 1923 to about 1930, and then in 1930 it was decided to modify it by including all of the governors of the Federal Reserve banks rather than just five. Instead of having a committee of five representing the governors' conference, it was decided that the matter was of sufficient importance, and one the repercussions of which were felt throughout the country sufficiently, so it would be desirable for the committee to bring together all of the governors into a committee called the "Open Market Policy Conference"; and that is the committee which, in the Banking Act of 1933 was made a statutory committee, under a somewhat changed name, "Federal Open Market Committee", a committee of 12 governors.

It does not say, in the law, that they have to be Governors, but it says they have to be representatives of the Federal Reserve banks. But, as a matter of fact, the Governors were selected.

When we speak about the period from 1923, say, to 1933, during which the Open Market Committee functioned, first, as a voluntary, and later as a statutory committee, I should like to say to you that the Federal Reserve System did pioneering work not only in obtaining the information and working out the relationships between these different economic factors in the situation—it did pioneering work also in the magnitude and boldness of its operations.

There has never been a banking system that did more in the way of carrying out the objectives which it is now proposed to write into the act than the Federal Reserve System did during that period.

The purchases which they engaged in, in 1924, were on a large scale partly for the purpose of moderating the business recession, but partly for the purpose of helping the establishment of stable money conditions throughout the world.

The same thing was done in 1927. Then, in 1928, when speculative expansion was so great that the Federal Reserve System proceeded to a policy of restraint through discount rates and open-market operations on a larger scale than had been done before. When business broke in 1929, the Federal Reserve System stepped in and bought a large volume of securities—not large in the sense we have gotten accustomed to thinking of now, but large in the light of what appeared in 1929 to be large—then in 1930, they bought $100,000,000 or more of securities, but they did not proceed as vigorously as may now seem to have been desired in the light of subsequent developments.

In 1931, the world went through a terrible contortion, with first one country and then another being subjected to runs, and, finally, in the autumn, England went off the gold standard. At that time, the United States lost, in a matter of 6 weeks, $700,000,000 of gold.

We had very large foreign balances in this country which were subject to withdrawal on demand; and the Federal Reserve System, in order to protect itself against continuous drains, followed the orthodox practice of raising its rates, and holding them at a higher level. It seems, in retrospect, that those rates were kept high longer than was desirable, and that is particularly true of the bill rates, which were held above the market rates for 3 or 4 months, during which time there was a rapid run-off of bills.

This should be viewed, however, in the light of the fact that, at that time, we still had a very large volume of foreign obligations subject to withdrawal on demand, and that the legislation under which the Federal Reserve System was functioning was such that the amount of gold, free gold, was beginning to be low. I would like to discuss that matter of free gold a little more, in connection with collateral requirements.

However, when the Glass-Steagall Act was passed, on February 27, 1932, and the Federal Reserve System's gold became available, the system began open-market operations on a scale that is very impressive. First, they decided to purchase securities for awhile at a rate of $25,000,000 a week, and then at a rate of $100,000,000 a week, so that the system's holdings of open-market securities increased from $750,000,000 to $1,850,000,000 in the course of a few months and they were held steady at that, except for seasonal fluctuations; and then, in 1933 they purchased another $600,000,000, so their total holdings now are more than $2,400,000,000. The chart shows this.

The reason I am emphasizing those facts is that I am a little restive under the wide-spread allegation that the Federal Reserve System sat supine and did nothing to combat the forces of the depression. It may be that the Federal Reserve System did not know, in 1929 and 1930 and 1931, as much of the magnitude of the catastrophe that the world was facing as it knows today; it may be that they did not have adequate information; and it is also unquestionably true that the system did not have the necessary legal authority which it has since acquired and which is going to be further increased, if this bill becomes a law. But in considering all of that——

Mr. GOLDSBOROUGH. And they did not ask for any increase of authority. They did not show any knowledge that any increase in authority was necessary.

Dr. GOLDENWEISER. Not until the early months of 1932, when they asked for the Glass-Steagall Act.

Mr. GOLDSBOROUGH. Up until 1932, we were told by the Secretary of the Treasury and the Governors of the Federal Reserve Board that they were doing everything that could be done by the Federal Reserve System.

Dr. GOLDENWEISER. Yes; and I think——

Mr. GOLDSBOROUGH. And they insisted that we stay on a rigid gold standard and no expansion should take place, and if it did, the country would go off like Germany. There was nothing indicated whatever that there was any vision on the part of the Secretary of the Treasury's office, or the Governors of the Federal Reserve Board, as to what was going on in the world, at all.

Dr. GOLDENWEISER. I do not wish to contradict that, but all I wish to say is——

Mr. GOLDSBOROUGH. No; but you did contradict it a few moments ago.

Dr. GOLDENWEISER. No; excuse me. I did not contradict it. I simply said it is a record of a great many things having been done; and as soon as it obtained, under the Glass-Steagall Act, the authority to release our gold, the Federal Reserve System engaged in open-market operations on an exceedingly large scale.

Mr. GOLDSBOROUGH. I will tell you what this committee, or a great part of it, thinks about the open-market operations that took place: This committee thinks that the Federal Reserve System did not want the Goldsborough bill passed, and for that reason it started only buying $25,000,000 a week, and they proceeded; and when the bill was about to pass the House, to increase the purchases, they did buy $100,000,000 a week, in order to indicate that this legislation was not necessary. We were told, time and time again, it was not necessary; and then just as soon as the Glass substitute to the Goldsborough bills was adopted by the Senate, the purchases were immediately stopped. It looked as if the purchases were tactical, instead of being economical.

Dr. GOLDENWEISER. I think, Mr. Goldsborough, that is a matter of opinion. My opinion is that you are all wrong about that; that there was nothing tactical in these purchases. I was in the Federal Reserve System in the fall of 1931, and in January and February 1932, when the question of the possibility of purchasing and relieving the situation was constantly under discussion, and when we were running up against the difficulty of the shortage of gold, and we went to Congress and got the authority and purchased $1,100,000,000 of Government securities in 6 months.

I think that this did represent economic convictions. The Glass-Steagall Act was passed on February 27, 1932, and after that the purchases were $1,100,000,000, and the Banking Act of 1933 was not passed until a year later.

Mr. GOLDSBOROUGH. I want you to understand that what I said is not intended as a criticism of you.

Dr. GOLDENWEISER. I understand that it is not personal, of course.

Mr. GOLDSBOROUGH. You were not engaged in formulating the policies of the Federal Reserve System, so it is no criticism of you.

Dr. GOLDENWEISER. I did not assume that. I think it simply is not the correct interpretation of the facts of the Federal Reserve System. If you have, on the subject, information that is not available to me, that is where the matter has to rest.

Mr. GOLDSBOROUGH. We have information given by the Secretary of the Treasury and the Governor of the Federal Reserve Board, who took the position that we should do absolutely nothing but allow conditions to remain the same and worry through the situation. That is what we were told.

Dr. GOLDENWEISER. I would like to say a few words, Mr. Chairman, on the matter of eligibliity. I know——

The CHAIRMAN. In that connection, I wish you would define to the committee what paper is eligible under the present law, so we may have a clearer idea of what we have been operating under heretofore and what would be involved in the change contemplated in the bill now under consideration.

Dr. GOLDENWEISER. Yes; Mr. Chairman.

Mr. HOLLISTER. Just one question before we leave the open-market operations.

Dr. GOLDENWEISER. Yes.

Mr. HOLLISTER. Now, if the acquisition by the Federal Reserve banks of Government obligations are directly from the Government, would that be a part of the open-market operations?

Dr. GOLDENWEISER. That comes under section 14 of the Federal Reserve Act, which is the open-market section.

Mr. HOLLISTER. What I am getting at is this: In the event that this bill becomes a law, so that the various Federal Reserve banks may be compelled to enter the open-market operation, may they then be compelled, against their will, to continue buying Government obligations directly from the Government—if not in the open-market—but directly from the Government?

Dr. GOLDENWEISER. I am not a lawyer.

Mr. HOLLISTER. I think that is a very natural thing which the committee ought to know.

Dr. GOLDENWEISER. Yes; and perhaps it would be better if you asked the counsel of the Board that question. As a matter of fact, that is a question which we have not discussed or considered at all.

Mr. HOLLISTER. That is very material—I mean the opinion that some of us have of this power, that it might be used by the Administrative Control Board to compel banks, very much against their will, to put their resources back to the continuous acquisition of Government bonds, even though it were clear that the Government had gone far beyond the necessity of demands of the case in issuing bonds.

Mr. WYATT. I am not prepared to render a definite opinion on this question, because it is something I have not thought about. The question was not raised or discussed while the bill was being drafted; but my off-hand view is that, under the bill as introduced, the Open-Market Committee could not compel the Federal Reserve banks to purchase bonds directly from the Government, because the committee is only given power over open-market operations.

Mr. HOLLISTER. You would not consider that open market then?

Mr. WYATT. Off hand, I would not say so; but I would like to call your attention to the fact that, under the Thomas amendment, there is already a specific provision for the direct purchase of $3,000,000,000 of Government bonds by the Federal Reserve banks from the Treasury. Moreover, the Thomas amendment provides means of coercing the banks to do so.

Mr. HOLLISTER. Yes; I know that.

Dr. GOLDENWEISER. Of course, Mr. Hollister, it is true that the Federal Reserve banks buy Government securities directly from the Government.

Mr. HOLLISTER. I realize that; but they are not compelled to, at the present time, however.

Dr. GOLDENWEISER. No; but they have authority, and usually they are short-term day-to-day certificates.

Mr. HOLLISTER. I understand that, but what worries me is the compulsory end of it.

Dr. GOLDENWEISER. I say the power of purchase does exist at this time, under the authority of section 14, which is the open-operation section, so that would be a question of legal interpretation.

Mr. HOLLISTER. In other words, if they are proceeding under any vague authorization whatsoever today, if they are not exceeding their powers in acquiring Government obligations, then the same provision of the law which says they are not exceeding those powers also makes it compulsory on them, in the future, to acquire Government securities, in the event that the Federal Reserve Board orders them to?

Dr. GOLDENWEISER. Yes; that would be my opinion, and I should think it would make very little difference, Mr. Hollister, whether they bought directly from the Treasury, or whether the Treasury first had to go through the form of selling them to some individual or some bank before passing them on to the Federal Reserve bank. The fundamental question you are interested in would not be really affected by it, substantially.

Mr. HOLLISTER. Except as a question of amount—I mean the open market might not provide the amounts and they would be compelled to take directly from the Government.

Dr. GOLDENWEISER. There are enormous amounts on the market, you know.

The CHAIRMAN. Before you leave that, the purchases shown by the chart you have just shown the committee, do not represent action directly as a matter of Government policy, but they represent the independent action of the different banks who are free to do as they please, and buy where they please. and decline to buy where they do not please?

Dr. GOLDENWEISER. I am very glad you brought that question up, Mr. Chairman, because I think——

Mr. SPENCE. A little louder.

Dr. GOLDENWEISER. I do not think that is an accurate statement, Mr. Chairman, because they did work through the open-market committee.

The CHAIRMAN. As long as they wanted to?

Dr. GOLDENWEISER. And the purchases were through the open-market committee.

The CHAIRMAN. I am not interested in how the purchases were made. My inquiry was this: Whether or not the purchases made by the banks represented the free action of the banks, or whether they represented the actions carried out as governmental policy?

Dr. GOLDENWEISER. I cannot answer that "yes" or "no."

The CHAIRMAN. The record is quite complete to the effect that the banks were free to act as they pleased.

Dr. GOLDENWEISER. Yes; that is correct; but I would like to add the statement that, while they had freedom to buy or not to buy, they agreed to act jointly through the open-market policy conference.

The CHAIRMAN. That is the very thing I am talking about. They agreed, and what they did represented an agreement on their part, but none of it was necessarily the result of governmental policy?

Dr. GOLDENWEISER. None of it was; no.

The CHAIRMAN. Nor did any governmental authorities have the power to direct and compel these actions?

Dr. GOLDENWEISER. None of it was compulsory.

The CHAIRMAN. And they opposed any move for governmental authority to require such action?

Dr. GOLDENWEISER. That is probably true, also.

The CHAIRMAN. I think the record will show that.

Dr. GOLDENWEISER. But the fact is, also, that the Federal Reserve Board, especially the governors of the Federal Reserve Board, were in constant touch with the members of the open-market committee, and the policies pursued were agreed upon by all of the participants.

The CHAIRMAN. This would, of course, be true—and I did not, of course, intend to invite you into a question of policy, but this is necessarily true, also, is it not: That, insofar as it affects general conditions, in putting into effect a particular policy of the Federal Reserve banks, the psychological effect would enter into the calculation, as well as the actual transaction?

Dr. GOLDENWEISER. That is correct.

The CHAIRMAN. And such effect would be quite different in the case of action by banks in their independent capacity, which represented simply the purposes of the banks, one at a time, putting in effect their own judgment, and what it would be if the action taken were known to the world to be the expression of policy on the part of the Government, which would be followed up consistently?

Dr. GOLDENWEISER. I think that is correct; absolutely. By "Government" you mean the Federal Reserve Board?

The CHAIRMAN. Oh, yes.

Dr. GOLDENWEISER. I think perhaps it is important to make the distinction.

The CHAIRMAN. Of course, I mean that, because that is the only authority at the time that could do it.

Dr. GOLDENWEISER. I think I have said——

The CHAIRMAN. I suggested that you define eligible paper under the existing law, so we may have in this record a clear definition of it, and thereby be enabled to know what we are doing by the changes involved in this bill.

Dr. GOLDENWEISER. The definition of eligible paper is a complex matter; it covers many pages of law and many pages of regulations, but I should like to have the privilege of reading a paragraph or two of an article that discusses that subject, which appeared in the Bulletin of July 1930, and, if the chairman pleases, I should like to insert these three or four pages into the record.

The CHAIRMAN. That is taken out of the law?

Dr. GOLDENWEISER. That is taken out of the Bulletin—the Federal Reserve Bulletin—and it is stated in terms understandable to the ordinary business man.

The CHAIRMAN. In other words, this will embody the information that I suggested?

Dr. GOLDENWEISER. I would like, however, if you wish, at this time, to read a paragraph of it.

The CHAIRMAN. Certainly.

Dr. GOLDENWEISER (reading):

Eligible paper is a term applied to credit instruments that are eligible for discount at the Federal Reserve banks under the terms of the Federal Reserve Act and the rulings of the Federal Reserve Board. The general principles of eligibility are clearly defined by the act and the rulings, but their application in particular cases is not always a simple matter.

In view of the fact that the Federal Reserve System was established for the purpose, among others, of creating an agency from which member banks can obtain credit for seasonal or emergency needs, the Federal Reserve Act provides in a general way that so-called "commercial paper" be eligible for discount with the Reserve banks.

The CHAIRMAN. I suggest you read all of it.

Dr. GOLDENWEISER (continuing reading):

Paper created in the process of financing the flow of commodities in production and trade arises out of loans that are ordinarily liquidated by the borrower with funds received in the natural course of events from the sale of goods underlying the transaction. In the majority of cases the rules and regulations relating to eligibility are consequently devoted to defining eligible paper by reference to the nature of the underlying transactions. The first question to ask, therefore, in the process of testing any piece of paper for eligibility, is: Did it arise from, or are the proceeds to be used for, the proper sort of transaction? Other questions, which are equally essential but comparatively easy to determine, are as follows: Is the maturity within the law and regulations? Does the paper meet the physical formalities prescribed? Has the legal limit of the aggregate of paper rediscountable for the particular obligor been reached?

In order to be eligible, paper must arise out of a transaction related to an agricultural, industrial, or commercial purpose; the paper must have been drawn or the proceeds used for producing, purchasing, carrying, or marketing goods. Paper is not eligible if the proceeds are used to finance fixed investments of any kind, or any investments of a purely speculative character, or carrying or trading in stocks and bonds except obligations of the United States, or to finance relending operations except relending by cooperative marketing associations and factors.

Because of the longer maturities for which agricultural paper may be rediscounted, it needs to be distinguished from other eligible paper. Agricultural paper arises out of activities of growers in connection with production, marketing, and carrying of agricultural products, including the breeding, raising, fattening, or marketing of livestock. In classifying paper, the purpose of original negotiation is determining throughout its life.

Some special points should be kept in mind with relation to bankers' acceptances. In respect to this type of paper, the law and regulations are somewhat more specific as to the purpose of negotiation or nature of transaction.

Purposes specifically enumerated are shipment of goods, including export and import, storage of readily marketable staples, and the creation of dollar exchange.

Eligibility versus acceptability.—The Federal Reserve Act, the regulations of the Federal Reserve Board, and the rulings of the Board define the tests that paper must meet in order to be eligible for rediscount. The Federal Reserve banks must observe these tests when taking paper, but to them is left the matter of passing on the desirability of paper from a credit standpoint. Paper may meet the technical tests of eligibility and yet fail to meet the credit requirements of any particular Federal Reserve bank. Moreover, each Federal Reserve bank is charged by the act in extending accommodation to any particular member bank to have "due regard for the claims and demands of other member banks."

Member bank collateral notes.—Member banks, in addition to raising funds from Federal Reserve banks by rediscounting, may borrow for 15 days on their own notes secured by obligations of the United States or for 90 days on notes secured by paper eligible for rediscount.

Indeed, more use has been made in recent years of this method of borrowing than of rediscounting; on December 31, 1929, for example, member banks were borrowing at the reserve banks $454,000,000 on their collateral notes, and their rediscounts at the reserve banks amounted to $193,000,000.

Summary tabulation.—The following pages give a tabular array of the chief points that need to be taken into consideration in testing any particular piece of paper as to its eligibility for rediscount. There are also included, by way of illustration, digests of rulings in connection with the eligibility of paper arising out of specific transactions.

These are the principles, and then the article proceeds to tabulate the kind of cases that come under these rules.

The CHAIRMAN. I suggest you insert that in your statement.

Dr. GOLDENWEISER. Yes.

(The matter referred to is as follows:)

SUMMARY OF ELIGIBILITY REQUIREMENTS FOR REDISCOUNT AT FEDERAL RESERVE BANKS, JULY 30

[Excerpt from Federal Reserve Bulletin for July 1930, pp. 401–406]

What nature of transactions give rise to notes, drafts, and bills of exchange eligible for rediscount at a Federal Reserve bank?

Eligible paper arises if drawn for or proceeds used for producing, purchasing, carrying, marketing goods in agriculture, industry, or commerce.[1]

Ineligible pape arises if drawn for or proceeds used for fixed investments or capital purposes of any kind;[2] relending[3] except for agricultural purposes by a coperative association[4] or by a factor exclusively to producers of agricultural products in their raw state:[5] investments of a purely speculative character;[6] carrying or trading in stocks and bonds except obligations of the United States.[7]

Specific transactions giving rise to eligible and ineligible paper according to published rulings of the Federal Reserve Board:

ELIGIBLE PAPER	INELIGIBLE PAPER
	Investment paper
Given by owner to contractor in actual payment for material and services.[8]	Made by owner—proceeds of which to be used by owner to pay for work of developing or building.[9]
Given by motor transport corporation to the seller of trucks.[9]	Made by motor transport corporation—proceeds to be used for purchase of trucks.[9]
Given by farmer for tractor—agricultural paper on the ground that a tractor is used for a current agricultural purpose.[10]	Given by farmer for purchase of silo.[12]
Given by farmer—proceeds to be used for draining farm lands when drainage is incidental to cultivation.[11]	
Given by water works company—the proceeds of which to be used for pay roll, purchases of coal, etc., if statement of borrower shows excess of quick assets over current liabilities.[13]	Given by public-service corporation, if cannot be liquidated within a short time out of current earnings.[14]
	Relending or finance paper
Drawn by factor the proceeds used for making advances exclusively to producers of staple agricultural products in their raw state (maturities up to 90 days.)[15]	Drawn by a finance company to finance another.[16]
Given by agricultural cooperative marketing associations (with maturities up to 9 months), when the pro-	Given by Federal land bank or joint-stock land bank, secured by farm loan bonds—proceeds used for relending.[17]

1 P. 226 (act, sec. 13); p. 129 (Reg. A, sec. I (b)); p. 130 (Reg. A, sec. II (a)).
2 P. 227 (act, sec. 13); p. 130 (Reg. A, sec. II (c)).
3 P. 130 (Reg. A, sec. II (b)).
4 P. 232 (act, sec. 13a); p. 133 (Reg. A, sec. VI (b)).
5 P. 226 (act, sec. 13); p. 129 (Reg. A, sec. I (b)); p. 134 (Reg. A, sec. VIII).
6 P. 130 (Reg. A, sec. II (d)).
7 P. 227 (act. sec. 13—see also act of June 17, 1929; p. 129 (Reg. A, sec. I (c)).
8 P. 40 (ruling no. 331).
9 P. 44 (ruling no. 501).
10 P. 32 (ruling no. 211).
11 P. 33 (ruling no. 214).
12 P. 44 (ruling no. 500).
13 P. 37 (ruling no. 314).
14 P. 37 (ruling no. 318).
15 P. 226 (act, sec. 13); p. 129 (Reg. A, sec. I (b)); p. 134 (Reg. A, sec. VIII).
16 P. 38 (ruling no. 324).
17 P. 39 (ruling no. 330).

ceeds are to be advanced by the association to any of its members for an agricultural purpose.[17]

Made by a manufacturer of pig iron secured by pig iron already manufactured, held waiting delivery under contract of sale. The sale has been made and the carrying of the material is not for speculative purposes.[19]

Paper drawn for investments of a purely speculative character

Note, proceeds of which are used for holding grain for a higher price.[20]

AGRICULTURAL OR COMMERCIAL PAPER

Agricultural or livestock and eligible

Given by a farmer for purchase of agricultural implements (replaceable in a comparatively short time).[21]

Drawn by a dealer on farmer in payment for agricultural implements.[22]

Given by farmer to an irrigation company for water used for crops.[24]

Given by a farmer to raise funds for fattening cattle.[25]

Made by farmer in payment for mules.[27]

Made by agricultural cooperative marketing associations for the purpose of obtaining funds with which to make payments to members, or to finance marketing of agricultural products.[28]

Commercial and eligible

Given by a dealer for agricultural implements to resell to a farmer.[22]

Given to a farmer in payment for agricultural products grown by him.[23]

Given by an irrigation company, in its business of furnishing water to farmers.[24]

Given by a packing company—the proceeds used to purchase livestock.[26]

Made by mule and cattle dealer.[27]

Covering such food products as butter, cheese, eggs, poultry, frozen fish in cold storage under negotiable warehouse receipts.[29]

WHAT MATURITY MAY REDISCOUNTABLE PAPER HAVE?

Ninety days in general, including factors' paper created to make advances to certain agricultural producers.[30]

Nine months in case of agricultural paper including livestock paper.[31]

Indefinite maturities are ineligible except for sight bills which grow out of the domestic shipment or exportation of nonperishable, readily marketable agricultural or other staples and secured by shipping documents. Such bills may not be held for the account of a Federal Reserve bank for more than 90 days.[32]

HOW MUCH PAPER OF ONE BORROWER MAY BE REDISCOUNTED BY A MEMBER BANK WITH A RESERVE BANK?

An amount not in excess of that which may be loaned by a national bank to one person; i. e., 10 percent of such bank's capital and surplus subject to a number of important exceptions.[33]

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[17] P. 232 (act, sec. 13a); p. 133 (Reg. A, sec. VI (b)).
[19] P. 35 (ruling no. 302).
[20] P. 36 (ruling no. 312).
[21] P. 31 (ruling no. 204).
[22] P. 33 (ruling no. 215).
[23] P. 27 (ruling no. 100).
[24] P. 40 (ruling no. 333).
[25] P. 32 (ruling no. 208).
[26] P. 32 (ruling no. 209).
[27] P. 31 (ruling no. 203).
[28] P. 232 (act, sec. 13a); p. 133 (Reg. A, sec. VI (b)).
[29] P. 38 (ruling no. 321).
[30] P. 227 (act, sec. 13); p. 129 (Reg. A, sec. I (a)).
[31] P. 231 (act, sec. 13a); p. 129 (Reg. A, sec. I (a)).
[32] P. 227 (act, sec. 13); p. 129 (Reg. A, sec. I (a)); p. 134 (Reg. A, sec. VII; see also amendment of May 29, 1928.
[33] P. 227 (act, sec. 13)—see also amendment of sec. 13 by act of Apr. 12, 1930; p. 352 (sec. 5200 of U. S. R. S.).

WHAT TECHNICAL FORMALITIES MUST THE PAPER MEET?

Must be promissory note, draft, or bill of exchange, including bankers' and trade acceptances.[34]

Must be negotiable.[35]

Must be endorsed by a member bank.[36]

The name of one of the parties to underlying transaction must appear upon it as majer, drawer, acceptor, or endorser.[37]

May be secured by the pledge of goods or collateral of any nature, provided the paper is otherwise eligible.[38]

WHAT PHYSICAL EVIDENCE OF ELIGIBILITY MUST BE SUPPLIED BY DISCOUNTING MEMBER BANK?

Application for discount must certify—

Member bank's belief in eligibility.[39]

Paper, not acquired from nonmember bank, unless member has permission to rediscount for nonmember banks.[39]

If offering bank is a State bank, that borrower is not obligated for more than he could be to a similar national bank.[40]

If paper is a promissory note, whether a financial statement of borrower is on file. A Federal Reserve bank may in any case require the financial statement of the borrower to be filed with it. Such statement must be on file if the note was discounted for a nonmember bank or a nondepositor, and in all other cases unless secured by warehouse receipt, prior lien on livestock, or obligations of the United States; or the aggregate obligations of borrower offered for discount is less than 10 percent of capital of bank and is less than $5,000.[41]

A draft, bill of exchange, or acceptance should be drawn so as to evidence the character of the underlying transaction. A stamp or certificate may accomplish this.[42]

BANKERS' ACCEPTANCES

(Certain respects in which the law and the regulations governing eligibility are more specific with reference to bankers' acceptances than with reference to other types of paper are detailed below.)

Nature of transactions giving rise to eligible acceptances:

Shipment of goods in foreign trade, including shipments between two foreign countries.

Shipment of goods within the United States—shipping documents must be attached at time of acceptance.

Storage in the United States or in any foreign country of readily marketable staples, must be secured at time of acceptance by warehouse receipt and acceptor must be secured through life of acceptance.

Creation of dollar exchange.[43]

Maturity of eligibile acceptances: Ninety days in general,[44] 6 months, if drawn for agricultural purposes and if secured at time of acceptance by warehouse receipts covering readily marketable staples;[44] 3 months if arising from the creation of dollar exchange.[45]

Aggregate of acceptances of one customer rediscountable for a particular member bank: Ten percent of capital and surplus of accepting bank, unless acceptance is secured throughout life by documents growing out of same transaction.[46]

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[34] P. 226 (act, sec. 13) ; p. 228 (act, sec. 13).
[35] P. 130 (Reg. A, sec. II (a)).
[36] P. 226 (act, sec. 13) ; p. 231 (act, sec. 13a) ; p. 129 (Reg. A, sec. (e)).
[37] P. 130 (Reg. A, sec. II (a)).
[38] P. 130 (Reg. A, sec. II (e)).
[39] P. 131 (Reg. A, sec. III)).
[40] P. 217 (act, sec. 9) ; p. 131 (Reg. A, sec. III).
[41] P. 131 (Reg. A, sec. IV (b)).
[42] P. 132 (Reg. A, sec. V (b)) ; p. 137 (Reg. A, sec. XIII).
[43] P. 135 (Reg. A, sec. XI).
[44] P. 228 (act, sec. 13) ; p. 137 (Reg. A, sec. XII).
[45] P. 230 (act, sec. 13) ; p. 137 (Reg. A, sec. XI).
[46] P. 136 (Reg. A, sec. XI).

DEFINITIONS

NOTE.—Unconditional promise, in writing, signed by the maker, to pay in the United States, at a fixed or determinable future time, a sum certain in dollars to order or to bearer.[47]

Draft or bill of exchange.—Unconditional order, in writing, addressed by one person to another, signed by the person giving it, requiring the person to whom it is addressed to pay in the United States, at a fixed or determinable future time, a sum certain in dollars to the order of a specified person.[48]

Trade accepance.—A draft or bill of exchange, drawn by the seller on the purchaser of goods sold, and accepted by such purchaser.[48]

Bankers' acceptance.—A draft or bill of exchange, whether payable in the United States or abroad and whether payable in dollars or some other money. of which the acceptor is a bank or trust company, or a firm, person, company, or corporation engaged generally in the business of granting bankers' acceptance credits.[49]

Agricultural paper.—Note, draft, or bill of exchange issued or drawn, or the proceeds of which have been or are to be used for agricultural purposes, including the production of agricultural products, the marketing of agricultural products by the growers thereof, or the carrying of agricultural products by the growers thereof pending orderly marketing, and the breeding, raising, fattening, or marketing of livestock.[50]

Goods.—Include goods, wares, merchandise, or agricultural products, including livestock.[51]

Readily marketable staple.—An article of commerce, agriculture, or industry of such uses as to make it the subject of constant dealings in ready markets with such frequent quotations of price as to make (*a*) the price easily and definitely ascertainable and (*b*) the stable itself easy to realize upon by sale at any time.[52]

Rulings have held these to be readily marketable staples.—Cotton yarns, flour, cotton, potatoes, cattle, sugar in bond, wool, coal, cottonseed. These have been held not to be such marketable staples: Automobiles, automobile tires, whisky, or sacramental wine in bond.[53]

NOTES

The foregoing article is based on the Federal Reserve Act and on the rulings and regulations of the Federal Reserve Board as published from time to time in the Federal Reserve Bulletin, and summarized in the so-called "Digest of Rulings" (described on p. 401). The numbered citations refer, except as indicated below, to pages of the digest, with parenthetical reference to the act (by sections), to the regulation (by letter and section), and to the rulings (by number, all numbers cited being those of rulings given in the digest under the general heading XIII-C).

Mr. BROWN of Michigan. You have just mentioned 90-day paper——

Dr. GOLDENWEISER. Yes.

Mr. BROWN of Michigan. There are cases that are running 9 months, at the present time; are they eligible?

Dr. GOLDENWEISER. Yes; but 90 days is the limit on member banks' collateral notes, unless they are renewed. Eligible paper, that is, rediscounted paper, Mr. Brown, may run 9 months for agricultural or livestock paper, but when a bank borrows on its own promissory note, the limit is 90 days.

[47] P. 131 (Reg. A, sec. IV (a)).
[48] P. 132 (Reg. A, sec. V (a)).
[49] P. 135 (Reg. A, sec. X).
[50] P. 132 (Reg. A, sec. VI (a)).
[51] P. 130 (Reg. A, sec. II (a), footnote).
[52] P. 136 (Reg. A, sec. XI, footnote).
[53] P. 74 (ruling XIII-E, no. 460).

Mr. Brown of Michigan. As far as time is concerned you have your 90-day paper, your 6-months paper, and your 9-months paper, but those are the maximums?

Dr. Goldenweiser. Yes, sir.

Mr. Brown of Michigan. You do limit them to one renewal, do you not?

Dr. Goldenweiser. I think that is a matter of practice. There is no regulation about one renewal. I think that is a matter for the individual bank——

The Chairman. If there is, it never was followed, I do not suppose?

Dr. Goldenweiser. No, sir; there is no absolute rule, Mr. Brown.

I do not think I need to say anything about eligibility, except that it has been suggested, in discussing this bill—I do not know whether it is in this room or in the press—that it would result in looseness of operation, or inflationary danger.

I think, myself, that the proposed bill introduces into the Federal Reserve Act, for the first time, the term "sound assets." As the law stands now, eligibility is defined by technical requirements, maturity, the nature of the underlying transactions, and other rigid rules, which the Federal Reserve Board had no authority to disregard in formulating its regulations, and the Federal Reserve banks have no authority to disregard in making their loans or advances to member banks. But there is nothing said in the Federal Reserve Act about the fact that assets must be sound.

Of course, that is something that any bank understands, and I do not mean to imply that the assets that the Federal Reserve banks have acquired were not sound, but I mean to say that the proposed bill substitutes for the rigid technicalities the fundamental principle that the assets must be sound, and beyond that leaves the actual regulations to the Federal Reserve Board, so that they can be adapted to different conditions that prevail in the country, and to different developments that arise at a time when Congress, perhaps, may not be in session.

That is what happened in 1932. We had banks failing very rapidly. There was a large number of banks that did not have eligible paper to present to the Reserve banks. The banks may have had sound assets and the Federal Reserve was unable to help them, and the banks were unable to get help from the Federal Reserve until the emergency bill was passed, which authorized them, under certain restrictions, to obtain relief from the Federal Reserve banks on other than technically eligible paper.

The Chairman. Did not that act employ the language "sound"?

Dr. Goldenweiser. No; it said any security satisfactory to the Federal Reserve banks.

The Chairman. And we even went to the extent of making it a form of emergency relief available to the nonmember banks?

Dr. Goldenweiser. Yes; you did, about a year later——

The Chairman. No; I beg your pardon. It was not a year later.

Dr. Goldenweiser. The Glass-Steagall Act was passed in February 1932, and the other provision was in the Emergency Banking Act passed in March 1933.

The CHAIRMAN. Yes; you are quite correct. What we did was to amend immediately, first, the Federal Reserve Act as to the privilege of obtaining currency.

Dr. GOLDENWEISER. Yes; you did that.

The CHAIRMAN. On Federal Reserve bank notes, and then to extend that privilege to nonmember banks.

Dr. GOLDENWEISER. Yes.

Mr. HANCOCK. In that connection, what is the total amount of discounts held by the Reserve System today, and what are the classes involved?

Dr. GOLDENWEISER. Mr. Hancock, the total discounts of the Federal Reserve, held today, are $6,000,000, and in view of the fact that it is a small figure, I do not know what it consists of.

Mr. HANCOCK. I do not think it is very important.

Dr. GOLDENWEISER. You see, with excess reserves of $2,000,000,000 the banks are not borrowing from the Federal Reserve banks.

The CHAIRMAN. What proportion of the present holdings of the banks is regulated by paper that might be classed as eligible?

Dr. GOLDENWEISER. You mean what is held by the member banks, themselves?

The CHAIRMAN. Yes, sir; that is what I mean.

Dr. GOLDENWEISER. About $2,000,000,000.

The CHAIRMAN. That might be classified as eligible?

Dr. GOLDENWEISER. That is classified as eligible, by their own classification.

The CHAIRMAN. What portion of their investments does that cover?

Dr. GOLDENWEISER. That is about 8 percent.

Mr. HANCOCK. What are the total assets of the Federal Reserve banks today, about $7,500,000?

Dr. GOLDENWEISER. They total $8,700,000,000.

Mr. BROWN of Michigan. Following the chairman's question, it seems to me that we ought to know what changes are contemplated by the addition of the new paragraph at the end of the present section 13, giving power to the Board to establish regulations for the rediscounting of commercial, agricultural, and industrial paper. What can you do under that provision that you cannot already do under the present section 13; what classes of paper will you add?

Dr. GOLDENWEISER. What we will add I do not know. That is a matter for the Board to decide. You questioned Governor Eccles about his opinion on this subject. My opinion would not be worth anything.

Mr. BROWN of Michigan. I am sure this committee thinks it would be.

Dr. GOLDENWEISER. The Federal Reserve Board would have authority to admit as collateral for member bank notes any asset that was sound, whether it was a commercial loan or bond or stock or real estate or farmer's paper, for the purchase of machinery. All of those long-term loans are completely barred, as the law stands today here, but would be made admissible under the new law.

The CHAIRMAN. And all of those same loans, which are now admissible because of their maturity, would also be admissible under the change?

Dr. GOLDENWEISER. Yes, sir.

Mr. BROWN of Michigan. That does not change the present status any?

The CHAIRMAN. That is what I am talking about.

Mr. BROWN of Michigan. The present statute remains as it is, and there are additional paragraphs giving the Board additional powers to make loans.

Dr. GOLDENWEISER. Mr. Brown, I think that is a matter of draftsmanship, and I think that the proper way to handle that is when this law is actually being drafted by your drafting forces to repeal all of those sections of the law and substitute this one section.

Mr. BROWN of Michigan. Might I say that if every limitation that we have heretofore had as to the time for which paper may be rediscounted is still in the law——

Dr. GOLDENWEISER. But that is repealed, Mr. Brown, by the proposed amendment, but I think it would be more effective to repeal it in so many words.

The CHAIRMAN. Well, the repeal would be conditioned upon the rules and regulations promulgated in order to put the change into effect?

Dr. GOLDENWEISER. That is right.

The CHAIRMAN. Otherwise they would proceed as they do now?

Dr. GOLDENWEISER. That is right.

The CHAIRMAN. That we do not know; but, if I understand the situation right, it is that you will continue to operate just as you are operating now, and if conditions were to improve and business got better and it was no longer deemed necessary to inaugurate new methods of meeting the situation, we might continue to operate as we are; but we are giving authority to liberalize?

Dr. GOLDENWEISER. Yes, sir.

Mr. HANCOCK. Under the present language of the act that we have before us now, as I understand it, you could not—the Federal Reserve System could not rediscount any paper with security longer than 9 months?

Dr. GOLDENWEISER. You mean under the proposed amendment?

Mr. HANCOCK. Yes; that is what I mean.

Dr. GOLDENWEISER. I think you are mistaken about that. I think, under the proposed amendment, the Federal Reserve banks could discount any paper that was sound. Is that not so?

Mr. BROWN of Michigan. I agree with Mr. Hancock to a certain extent. I think the authority is somewhat clouded, unless section 13 was repealed, as Dr. Goldenweiser suggested, in its entirety, and section 206 of the proposed bill substituted for section 13 of the law.

Dr. GOLDENWEISER. The counsel, I believe, has drafted a form by which that will be accomplished, and my personal recommendation would be that it should go into the law, because I know, positively, that it is the intention of the proponents of this bill that it should, in effect, take the place of existing section 13—I mean the parts of it dealing with eligibility.

Mr. BROWN of Michigan. Do you not think that the authority is somewhat clouded if section 13 remains as it now is?

Mr. WYATT. No; I do not think so. I think the broad authority given by the later statute, which would be construed as repealing by implication the restrictions contained in the old law. Certainly, there would be nothing in this statute that would prevent making advances on any sound assets. That is distinct from rediscounting. They could make advances on any sound assets, subject only to such regulations as the Board might prescribe. As a matter of fact, that is the way the banks would do it. They prefer to borrow on their own promissory notes secured by collateral, because that is less trouble than rediscounting.

Mr. HANCOCK. Under that language, it seems to me you could make advances on any sound assets for longer than 9 months; whereas if you discounted the paper, you would have to limit it to 9 months.

Mr. WYATT. That is not important, because if this goes through, the chances are that nearly all of the borrowing would be done on a promissory-note basis.

Mr. BROWN of Michigan. But your new section 206 speaks of assets—speaks of discounts as well as advances, and it seems to me there will be some complication between the paragraph we added this bill and the present law. Have you an amendment drafted to take the place of section 206?

Mr. WYATT. Yes. You cannot repeal all of section 13, because there are some other things in that section. What you really have to do in order to repeal the provisions which would be made obsolete by this amendment, is to repeal all of section 10 (a), all of section 10 (b), several paragraphs of section 13, several paragraphs of section 13 (a), and then amend several of the other paragraphs in sections 13 and 13 (a). We have it written out, and it takes 5½ typewritten pages to do it; but we can give it to you, if you want it.

Dr. GOLDENWEISER. Mr. Chairman, there is only one other subject on which I should like to have just a word to say, and that is the proposed repeal of the collateral requirements against the Federal Reserve notes. That is a technical subject and one that has given rise to a good deal of misunderstanding.

I would like to say, in the first place, that there is nothing in this proposed amendment that would, in any way, change the security back of the Federal Reserve notes.

The Federal Reserve bank holds certain assets, and against these assets it has its liabilities, principally the liabilities to the public in the form of notes and deposits.

There is one reservoir of assets and there are two kinds of claims against it. The present law provides that you take that reservoir of assets and pick certain ones out that are made eligible for that specific purpose by law, and put them in another box and call it collateral for Federal Reserve notes, and leave the rest as security against the deposits. All this bill proposes to do is to do away with that separate box and call the entire box of assets security against all of the liabilities. You are not changing the quality of the security in any way, you are simply doing away with an expensive and unnecessary segregation; and since Federal Reserve notes, by the terms of law, are prior liens and continue to be prior liens, they have as security the best part of the assets, so that the note holders would have to be satisfied before the claims of the deposit holders could be satisfied.

There is absolutely nothing in this proposal that changes the quality of Federal Reserve notes in any way whatsoever. It does not repeal the reserve requirements; it does not change the quality of the assets back of them; it merely does away with the segregation. I think that very simple point is one that has been very frequently overlooked.

There are just a few more things about this collateral that I would like to say.

Mr. WILLIAMS. Right in that connection, if I may, under the present law, there is a certain part of the assets that are segregated; is that correct?

Dr. GOLDENWEISER. That is correct; yes.

Mr. WILLIAMS. And back of each note issue?

Dr. GOLDENWEISER. No; against all of the notes. They are not earmarked for any particular note issue.

Mr. WILLIAMS. Under this law, do not the banks, in case they need notes, make application to the Federal Reserve agent?

Dr. GOLDENWEISER. Yes.

Mr. WILLIAMS. And offer certain classes of assets, and he receives them, and they are placed in a separate box, as you say, or a separate place, as the paramount security on any notes that are issued at that time?

Dr. GOLDENWEISER. The Federal Reserve agent holds all of the assets that have been pledged with him. The Federal Reserve agent gets collateral for all of the notes that he pays out to the Federal Reserve bank, but I do not think he holds any particular batch against any particular batch of notes.

Mr. WILLIAMS. Is not there also a provision in there which authorizes a bank to take down and substitute other ones for ones which have already been put up?

Dr. GOLDENWEISER. That is right.

Mr. WILLIAMS. And is there not also a further provision which permits the board to require a bank to put up additional security?

Dr. GOLDENWEISER. Yes; all that is correct, but all that applies to the entire collateral that the agent holds against the entire note issue, and not any particular note issue.

Mr. WILLIAMS. I was under the impression it was the other way.

Dr. GOLDENWEISER. Excuse me. That is correct, is it not, Mr. Smead?

Mr. SMEAD. That is correct.

Mr. WILLIAMS. That was not my understanding of the way the language reads.

Dr. GOLDENWEISER. That is the way it has always read, Mr. Williams. For instance, they have never taken a particular batch of Government securities and held them against those particular notes, because it would be almost impossible to do that. If the bank returns notes and wants to have a corresponding amount of collateral released, it asks for the collateral it wants.

Mr. WILLIAMS. In that event, that makes the assets of the bank be prime and paramount lien as to the payment of the notes?

Dr. GOLDENWEISER. They continue to be under the proposed law.

Mr. WILLIAMS. And they are now, and in that respect the law is not changed?

Dr. GOLDENWEISER. That is correct.

Mr. WILLIAMS. In other words, the redemption of the notes would come first, over the depositors of the bank?

Dr. GOLDENWEISER. Yes.

Mr. WILLIAMS. They are the first paramount liens?

Dr. GOLDENWEISER. Yes; that is right, and that is continued in the law.

Mr. WILLIAMS. Now, while I am asking questions, may I continue on another subject?

Dr. GOLDENWEISER. Yes.

Mr. WILLIAMS. The question of reserves, as I understand, the reserves under the present law, are fixed at a certain percent?

Dr. GOLDENWEISER. Which reserves do you mean, of the member banks?

Mr. WILLIAMS. Yes; depending upon their locality?

Dr. GOLDENWEISER. That is correct.

Mr. WILLIAMS. I also understand that is still left in the law?

Dr. GOLDENWEISER. Yes, sir.

Mr. WILLIAMS. Well, in addition to that, we have this provision in this new law, which gives the Federal Reserve Board complete and entire authority and jurisdiction over the fixing of those reserves?

Dr. GOLDENWEISER. Yes; it gives them authority to change them.

Mr. WILLIAMS. Well, now, if we are going to have that, why not repeal this fixed limitation in the law?

Dr. GOLDENWEISER. I think the theory of that is, Mr. Williams, that the reserves shall not be disturbed, and shall continue as they are, but if there is danger of expansion—I do not remember exactly what the language is—injurious expansion or contraction, and a change becomes desirable, the Federal Reserve Board can act and change it, but otherwise the reserve requirements continue as they are; and the banks must continue to keep their reserves at a certain ratio, unless action is taken by the Federal Reserve Board.

Mr. WILLIAMS. That is the law now, is it not?

Dr. GOLDENWEISER. But at the present time, the Federal Reserve Board has no authority to raise the requirements.

Mr. WILLIAMS. That is in case of emergency?

Dr. GOLDENWEISER. No, sir; they cannot raise them. They may suspend them, but they cannot raise them.

Mr. HANCOCK. You can only do that with the consent of the President?

Dr. GOLDENWEISER. Excuse me. What I meant to say is, that under the original Federal Reserve Act they had no power to change reserve requirements. This particular amendment in the bill does not do anything more than to clarify the section that was in the so-called "Thomas amendment", passed in 1933, which does give the Board, with the President's approval, authority to make the change. I was talking about the original Federal Reserve Act at the moment. This proposed amendment simply clarifies the existing amendment and extends it somewhat.

The CHAIRMAN. What was the language of the Thomas amendment?

Dr. GOLDENWEISER. The language of the Thomas amendment, quoting from memory, is that in case of emergency——

Mr. WYATT. Would you like for me to read it?

The CHAIRMAN. Yes.

Mr. WYATT. The Thomas amendment added this paragraph to section 19 of the Federal Reserve Act:

Notwithstanding the provisions of this section, the Federal Reserve Board, upon the affirmative vote of not less than five of its members and with the approval of the President, may declare that an emergency exists by reason of credit expansion and may, by regulation during such emergency, increase or decrease from time to time, in its discretion, the reserve balances required to be maintained against either demand or time deposits.

Mr. WILLIAMS. The power is there?

Dr. GOLDENWEISER. That emergency power exists, but it is quite illogically worded, because it says the Board could either increase or decrease the reserve requirements, if an emergency arises because of credit expansion. Now, you would not want to decrease the requirements if an emergency arose from credit expansion, so that, literally, you could never decrease them, because of the way the provision is worded. The bill proposes a clarification and extension of that power, and removes from the President the necessity of approval and the requirements of a vote by five members of the Board.

Mr. WILLIAMS. This simply gives the board power to change when they think it is necessary?

Dr. GOLDENWEISER. That is right, sir.

Mr. WILLIAMS. In order to prevent undue expansion or contraction of currency, to regulate the reserve requirement?

Dr. GOLDENWEISER. That is true.

Mr. HANCOCK. And under the act, it could be done, without declaring such an emergency exists?

Dr. GOLDENWEISER. Without declaring there is an emergency, yes; and it also gives them the power to do that for financial centers, alone, or for the country districts, alone, or for the country as a whole, depending upon the circumstances, which the present amendment does not give.

Mr. WILLIAMS. I just wanted to clear that up in my mind.

Dr. GOLDENWEISER. I was not trying to mislead you for a moment. My mind slipped.

Now, if I may make a few more remarks about the collateral requirements, I would like that to conclude my statement.

I think I made it clear that Federal Reserve notes continue to be prior liens, that there is nothing in the law that, in any way, weakens the Federal Reserve note whatsoever. At the same time, the existence of those collateral requirements is not merely a matter of economy that we are asking you for, although it is economical, but it also has created many complications. The fact that we required that collateral made it necessary to have assistant Federal Reserve agents, or else have a lot of issued notes in the hands of the branches, and that created a lot of difficulty, because nobody could issue notes except the Federal Reserve agent, or his assistant, and you would have a large supply of issued notes and collateral, which would not be necessary, because they were not in the home office where there was an agent, you had to carry them as issued notes, or else you had to have an assistant agent, and have a high corresponding salary, to be on the job in the branch.

So that it has created a whole lot of unnecessary, purposeless difficulty and expenditures. In addition to that, it has created, sometimes, a very bad situation.

In the early months of 1932, a very large amount of gold had flowed out of the country. The Federal Reserve banks had bought a good many Government securities, because there was an awful deflation going on and it was necessary to keep down the indebtedness of the member banks to the Federal Reserve bank, in order to stop the deflation. And so the eligible paper in the hands of the Reserve banks was relatively small in amount. Since they had to put up against their Federal Reserve notes outstanding enough eligible paper or gold to make up 100 percent, and since the eligible paper was in a small amount, they had to put up a whole lot of gold, with the consequence that, at that time, the Federal Reserve banks, though they had $1,400,000,000 of gold in excess of their reserve requirements of 40 percent against notes, and 35 percent against deposits. had to put up $1,000,000,000 of that $1,400,000,000 as collateral against the Federal Reserve notes, where it could not be gotten out except by selling Government securities, and putting the banks in debt again. And they only had about $400,000,000 of "free gold" available to meet a foreign demand.

A liberal open-market policy could, therefore, not be undertaken until Government securities could be substituted for the eligible paper or gold with the Federal Reserve agent.

So we came to you, gentlemen, and asked you to give us that authority, and that authority was given, and has since been extended, and the President has now extended it for 2 more years.

That is the kind of thing that happened and, in logic, is apt to happen again, because when we want to exercise immediate restraint that is usually the time when the banks are heavily in debt, and going further in debt, and at that time there will be plenty of collateral, so it will not act as a restraining influence at a time when you want to restrain, but at a time when business is going flat and contraction is going on, if you buy Government securities in order to help out the banks, that is the time when you are going to be short of collateral and you find that your collateral requirements will be pinching.

This requirement always works against the interests of the country, and against the interests of the credit policy pursued by the Federal Reserve System. In 1932 we were up against it, with nothing but $400,000,000 available, with $1,000,000,000 or more of foreign short-term bonds in this country that could be withdrawn on demand in gold, when the Federal Reserve System was unable to pursue a policy of monetary ease, which was clearly indicated by all of the elements of the situation. Congress then passed an emergency measure to relieve the situation.

Now, it is requested and proposed that you do away with this obsolete and useless, expensive and dangerous provision altogether.

There is just one other thing I would like to say, and that has not any direct bearing on the collateral, but it has an indirect bearing on it, and that is, the question of demand for currency and the ability of the Federal Reserve banks to issue currency without any collateral, which question has been raised.

I have gone through the problem of what is back of the notes already, and Governor Eccles has discussed that in some detail, but I would like to make it clear that, in our banking and credit system, currency is the small change of business. Currency is not a big element in our means of payment.

Currency fluctuates in response to certain influences. In normal times, it fluctuates chiefly in response to certain parts of our economy that are still handled by cash payments, principally retail trade and pay rolls.

During a long period there was a trend, gradually, from year to year, for a decline in the amount of currency, because more and more business corporations were adopting the policy of paying their pay rolls by check, partly for the purpose of avoiding hold-ups, and partly because it is more convenient, and the habit of depositing checks was spreading throughout the country.

That particular trend has been reversed recently, because of the tax on checks, because of the service charges, because of the fact that communities are left without banks in many cases. But in general, the level of money, cash money, has remained reasonably steady, except for seasonal fluctuations. Its elasticity is indicated by the fact that it goes up $100,000,000 over the Fourth of July, and goes up again over Labor Day. Whenever people go away from home, they get a little more currency, and currency goes up for a few days, but then goes right down again.

Mr. HANCOCK. It goes up around Christmas time?

Dr. GOLDENWEISER. Yes; but it goes back down again in January. But those are seasonal fluctuations, and the year-to-year fluctuations are relatively minor.

The fluctuating element in our banking system is not cash but deposits. The reason I put it that way is that the elasticity of our currency rests on the habits of the people and the customs of the banking system. No one carries in his pocket more money than is needed for such small cash payments as he is in the habit of making. Possibly he pays for his gasoline in cash, he may pay for his lunch in cash, and carfares, and a few things like that. People are in the habit of keeping in cash a certain amount of money out of their pay checks, and the rest of it they deposit in the banks.

When they deposit it in the banks, the banks do not keep it in their vaults, either, because it is a dead asset in their vaults and involves unnecessary risk from burglars. So they immediately take it to the Federal Reserve bank, where it is added to their reserve and gives them a basis of expansion.

Mr. HANCOCK. How much money is in circulation, in pocket change, so to speak?

Dr. GOLDENWEISER. I could not tell you how much is actually in pocket change, but I think the amount that is outside of the banks, the Treasury, and the Federal Reserve banks is around $5,000,000,000.

Mr. HANCOCK. I mean the amount that is outstanding usually and not in the Federal Reserve or member banks or any bank.

Dr. GOLDENWEISER. About $5,000,000,000. Now, I would like to add this: That is the usual relationship between the seasonal fluctuation in currency, with no sensational changes, and with gradual declines occasionally. When the banking system began to crack, all this changed, because people began to want money, cash money, not for change but as a matter of safety. They lost their confidence in banks. There is one other chart here that I should like to show you, if you will bear with me. This shows the amount of money in circulation—and that is a technical term—I mean outside of the Treasury and the Federal Reserve.

Mr. WILLIAMS. Right there I want to ask a question: What do you mean by money in circulation?

Dr. GOLDENWEISER. I mean all of the money issued, outside of the Federal Reserve bank and the Treasury. That does include the banks' money, the money in the vaults of the member banks——

Mr. HANCOCK. You say it does include that?

Dr. GOLDENWEISER. It does include that; yes.

Mr. HANCOCK. And does it deal with money in the nonmember banks?

Dr. GOLDENWEISER. This includes all of the money outside of the Treasury and the Federal Reserve banks. I want to show you—here is 1929, a year of great prosperity, and money in circulation is $4,800,000,000.

Then in 1930 came along a time when the pay rolls went down and prices went down, and currency went down a little in the early part, a little more than seasonal; you can see it was moving below 1929, until about November, when the Bank of the United States in New York and the Bank of Kentucky failed, and hoarding began, and it shot up. That was the first appearance of hoarding on a large scale.

Then in 1931, first we had the seasonal liquidation, and then things continued fairly evenly. Then in the latter part of 1931, when all of these events all over the world were happening—first the run on Germany, then the one on England—and our banks were failing, we had a tremendous increase in hoarding.

Then in 1932 that level was the same, no particular increase in hoarding and no decrease until the middle of the year, and then there was another lot of bank failures in the Chicago district; and it rose again, and stayed at that level. That is the way we ended in 1933.

Then when the panic began, the currency in circulation shot up a couple of weeks by $2,000,000,000, to $7,500,000,000.

Mr. HANCOCK. That was in February?

Dr. GOLDENWEISER. That was in February, toward the very end of February 1933 and early in March.

Mr. HANCOCK. We were experiencing a money boom?

Dr. GOLDENWEISER. Yes; you can call it that if you wish. There was a terrible panic. And then when the President ordered the banks reopened and said that only sound banks would reopen, people's confidence was restored, and as soon as the banking bill was passed and the banks reopened, the people found they could have their money, and they did not want it, and the money came right back in the course of a few months, and we were getting back to the level at the beginning of the panic. But even yet, even right now, in 1935, there is still a whole lot more currency outstanding than there was in 1929, because when money finds its way into hoards, being hidden away under mattresses and in tin cans, it is likely to take it some time to come back.

And while those things that Governor Eccles mentioned about service charges, taxes on checks and communities without banks, are all factors in the situation, there is also a very considerable amount of hoarding, because we find that it is the very large denominations that are held out, and large denominations are not used by people in paying their bills.

The CHAIRMAN. I note that your chart makes no reference to postal savings, but postal savings are exclusive of the funds in the banks and in the Treasury?

Dr. GOLDENWEISER. This is exclusive of that; yes. Postal savings also went up.

The CHAIRMAN. How do you classify postal savings?

Dr. GOLDENWEISER. That is just the cash, the currency. This is not the deposits.

The CHAIRMAN. You do not figure the postal savings in this, at all?

Dr. GOLDENWEISER. No, sir; that was another method of protecting themselves, and it went up from $300,000,000 to above $1,000,000,000.

Mr. HANCOCK. I understand it went up to almost $700,000,000. How much money was there in existence at that time?

Dr. GOLDENWEISER. The amount of money in existence does not mean anything, because the reserve banks could print any amount they wanted to. There was any amount printed available to pay out, if there was any demand. The amount of money in existence——

Mr. WILLIAMS. I understood you to say this represented all the money, except what was in the Treasury and the Federal Reserve bank?

Dr. GOLDENWEISER. Yes; but the Federal Reserve bank had many billions of money available in case the panic continued and people wanted more.

Mr. WILLIAMS. But they did not issue it?

Dr. GOLDENWEISER. No, sir.

Mr. WILLIAMS. What I meant was, What was the outstanding issue of money?

Dr. GOLDENWEISER. That is all that was issued, because what is in the Federal Reserve banks and the Treasury is more or less like a book of blank checks; it does not mean anything. The only money that means anything is in your pocket, or money that has been paid out. The money that the Federal Reserve banks have printed is kept in case somebody wants it—it does not become money until it is paid out. The money that was available—I could not give you the exact amount, but it was billions of dollars of cash money that had been printed and was available in case it was needed.

Mr. WILLIAMS. Undoubtedly so, but does that represent all of the money that was issued at that time?

Dr. GOLDENWEISER. I do not quite get your point, Mr. Williams.

Mr. WILLIAMS. I want to know whether it represents all of the money there was?

Dr. GOLDENWEISER. It represents all of the money that had been paid out; yes.

Mr. WILLIAMS. When it was down here to $5,000,000,000, for instance, where was the balance of that money then?

Dr. GOLDENWEISER. Some of it may not have been printed, and what had been printed was lying in the Treasury or Federal Reserve banks. I get word from the Chief of the Division of Banking Operations that the Federal Reserve banks at that time had $5,000,000,000 of money printed, ready to issue in case the public wanted it. I am trying to explain exactly what the situation was.

Mr. WILLIAMS. I am trying to find out the money that was issued at that time.

Dr. GOLDENWEISER. This is all of the money that was issued at that time.

Mr. WILLIAMS. Does that line represent—whatever it is, whether it is $7,000,000,000 or $5,000,000,000—the amount of money that was issued at that time?

Dr. GOLDENWEISER. That is all of the money that has been issued and has not been retired; yes.

Mr. KOPPLEMANN. If money is put in a country bank, is it retired?

Dr. GOLDENWEISER. Not at that stage; but the country bank is likely to send it to a Federal Reserve bank, and it will then be retired. All the money outside of the Reserve banks and the Treasury is on this chart.

Mr. WILLIAMS. Then it is all on there.

Dr. GOLDENWEISER. All of the money—that is, the actual currency—is in there; yes.

The CHAIRMAN. How much was that?

Dr. GOLDENWEISER. $7,500,000,000.

Mr. WILLIAMS. That represents all of it? I did not have that impression.

Dr. GOLDENWEISER. That is all of it; yes.

Mr. WILLIAMS. What is the low ebb of it?

Dr. GOLDENWEISER. It gets as low as $4,400,000,000.

Mr. WILLIAMS. That represents all of the money that was issued at that time?

Dr. GOLDENWEISER. All of the cash money.

Mr. WILLIAMS. And when it got up to $7,500,000,000 it represented all of the money that was issued at that particular time?

Dr. GOLDENWEISER. Yes.

Mr. FORD. And suppose the Patman bill passes, what would happen to that chart?

Dr. GOLDENWEISER. That chart would not change, except for a very short time. You would pay out $2,000,000,000 of currency, but it would be immediately redeposited in the Federal Reserve banks, and the so-called "money" in circulation would not change. All of that money——

Mr. HOLLISTER. The only change would be in its purchasing value?

Dr. GOLDENWEISER. Well, its purchasing power—it is a complex question whether it would change or not. The only time that money in circulation would be likely to increase very rapidly would be when the people again lose confidence in the banks. That is the only thing that makes it go out.

Mr. KOPPLEMANN. Then what is the relationship between money and wealth?

Dr. GOLDENWEISER. You mean cash money? If you mean cash money, there is no relationship.

Mr. KOPPLEMANN. No relationship?

Dr. GOLDENWEISER. No relationship whatsoever. Mr. Chairman, that is all I wish to say, on my part, and if you wish to ask questions——

Mr. HANCOCK. On the question Mr. Hollister asked you, it does not follow as a point of logic that the purchasing power of the dollar would be changed, does it?

Dr. GOLDENWEISER. Not necessarily.

Mr. HANCOCK. If funds were released of currency——

Dr. GOLDENWEISER. Not necessarily, unless that action resulted in the people losing confidence in currency, or losing confidence in the Government, in which case the repercussions are very difficult to deal with.

Mr. HANCOCK. The obligations of the Government would be the same?

Dr. GOLDENWEISER. The Government would have outstanding a large amount of non-interest-bearing debt, instead of interest-bearing debt.

Mr. HANCOCK. Which would have to be redeemed at some time?

Dr. GOLDENWESIER. That raises a question of redemption, which at the present time, is in abeyance.

Mr. HANCOCK. Both of which would have to be paid off at some time?

Dr. GOLDENWEISER. Not necessarily.

Mr. HOLLISTER. How are you going to pay off the non-interest-bearing paper, behind which there is nothing?

Mr. HANCOCK. There is only one way you can pay any obligation of the Government, and that is through taxation, is it not?

Dr. GOLDENWEISER. Actually, the Government can reduce its indebtedness by one of three ways, but your answer is really exactly right; the only real way is taxation. Another way is repudiation, and the third way is what I recently more or less facetiously called "evaporation." That is what happened in Germany when they did not repudiate it, and they did not raise taxes, but they made the mark so completely worthless that it just evaporated.

Mr. HANCOCK. I am speaking of honest obligations?

Dr. GOLDENWEISER. Yes; you are right.

Mr. WILLIAMS. What did you call the German system, Doctor?

Dr. GOLDENWEISER. I do not really think it is fit to repeat.

The CHAIRMAN. All right, gentlemen, Mr. Hancock moves that we adjourn.

We thank you very much, Dr. Goldenweiser.

We will meet again tomorrow at 10:30 o'clock.

(Thereupon, a recess was taken in the hearing until 10:30 a. m. Thursday, Mar. 21, 1935.)

BANKING ACT OF 1935

THURSDAY, MARCH 21, 1935

House of Representatives,
Committee on Banking and Currency,
Washington, D. C.

The committee met at 10:30 a. m., Hon. Henry B. Steagall (chairman) presiding.

The Chairman. Gentlemen, we have with us this morning, Mr. Coolidge, the Under Secretary of the Treasury, who will discuss the bill H. R. 5357.

Mr. Coolidge has prepared a brief statement which he would like to read to the committee, after which he will be glad to answer any questions members of the committee may desire to propound.

Mr. Coolidge, you may proceed.

STATEMENT OF T. JEFFERSON COOLIDGE, UNDER SECRETARY OF THE TREASURY

Mr. Coolidge. Mr. Chairman, I have a brief statement covering only title II of the bill.

The Chairman. I presume you desire to address yourself to title II of the bill, and that is really what the committee would like to hear you about.

Mr. Coolidge. Title II is the part of the bill which is of most interest to the Treasury Department, because in that portion of the bill it is proposed to amend the Federal Reserve Act.

When the Federal Reserve System was formed conditions were very different from those of today. There were practically no Government securities in the market. The reserve requirements of the System were based on the amount of gold that was in the country and there was no insurance of bank deposits by any agency. The adjustment of money rates was largely automatic and only partially a matter of judgment. Should gold leave the country it became necessary for the banks to borrow to replenish their reserves. The same was true when there was a demand for currency or for an extension of loans. When either of these situations arose it was almost axiomatic to raise the rediscount rates to discourage further borrowing or to replenish the gold stock.

These conditions are very different today. The gold in the country is in excess of any normal legal reserve requirements; Government securities are obtainable for liquidity in large quantities, whereas commercial paper is small in amount compared with previous times, and bank deposits have largely been insured by the Federal Deposit Insurance Corporation. The proposed bill attempts to adjust the banking laws so that these new conditions can be met in a suitable manner.

In that portion of the bill covering amendments to the Federal Reserve Act, I want to take up the proposed change in the method of appointing the governors and vice governors of the individual Federal Reserve banks; the proposed change in collateral requirements for loans from the Reserve banks; the proposed change in restrictions on real-estate loans; and the proposed method of open-market operations together with the power of the Fedral Reserve Board to change reserve requirements.

It seems incongruous to have a governor appointed by the directors of the local bank and a chairman of the board by the Federal Reserve Board at Washington. Under the bill, the directors of the local Federal Reserve bank choose a governor who shall be chairman of the board and a class C director, and their choice is subject to the approval of the Reserve Board at Washington. The approval of the Board should, I believe, make for harmonious relations between the banks and the Federal Reserve Board, while at the same time not deprive the local directors of any of their proper responsibility in the choice of the officers.

At present the Federal Reserve banks are restricted in their loans to member banks, being able to loan only on specified types of assets. This bill will permit them in their discretion to loan a member bank on any of its sound assets when in their judgment it is a wise thing to do. At the present time this may seem unnecessary as the member banks have great quantities of funds; nevertheless, should there be an unwarranted flow of funds from an individual bank or from certain parts of the country, the banks under the bill could be given proper support by the Federal Reserve banks should their general condition justify it and unnecessary liquidation be prevented.

It is proposed that the existing restrictions on real-estate loans be somewhat liberalized. I personally believe that banks should be permitted to work out their old loans without restriction, while in the case of new loans 60 percent of an appraised value should be high enough. The Federal Reserve Board could properly be given further authority to make regulations within this limit of 60 percent.

Our control of money rates has passed from the automatic stage, because of the great amount of excess reserves, into a condition where automatic standards cannot, I believe, be improvised which can be expected to work under the conditions of the present or immediate future. It would seem that this control must be entrusted to a group of men, and, presumably, will be exercised by open-market operations in Government securities, by a change in the reserve requirements and in rediscount rates, or by a combination of the three.

I would like to state that there are no important conflicting interests in regard to the proper rate for short-time money. Everyone's interest is best served by the proper rate to help make business stable and prosperous. There may be differences of opinion between men or groups of men as to what is the rate most suitable under the conditions of the time, and the best methods of obtaining the desired results. The Treasury has, of course, great powers in influencing the rates for money and it is most important that it cooperate with those to whom like powers are committed. It is not important to choose men from any particular group to perform this important function, but it is essential that wise men experienced in the effect of money policies be chosen and that they not be influenced by unwise demands of special groups.

For this purpose the bill sets up an open-market committee, three to be chosen by the Federal Reserve Board from their members and two to be chosen by and from the governors of the Reserve banks. It is contemplated that these five men have the responsibility of the difficult and delicate job of buying and selling acceptances and Government securities with Reserve bank money for the purpose of furnishing to the country a proper supply of funds at proper rates to the extent that it is advisable to use this method for the purpose. With conditions as uncertain as they are and with the vast amount of gold in the country this power of buying and selling acceptances and Governments may be insufficient to insure proper control and in ths bill the Federal Reserve Board is given power to change legal reserve requirements of member banks. A raise of legal reserves would impound the idle money of the member banks, thus raising rates; or a reduction of reserve requirements would give the member banks additional funds. These two methods used in combination will equip the Federal Reserve System with supplemental control devices to be available for use when required, although it is to be expected that the need to change legal reserves will occur very seldom.

The CHAIRMAN. Mr. Coolidge, the Treasury favors the enactment of this bill?

Mr. COOLIDGE. The Treasury favors the enactment of this bill and the purpose for which it is intended. The question of changes that may be made, or the methods of accomplishing the purposes is entirely a question for this committee, and there is no reason why the bill should not be considerably modified to carry out the purpose for which it is submitted, so far as the Treasury is concerned.

Mr. GOLDSBOROUGH. The Treasury is in favor of the bill; is that correct?

Mr. COOLIDGE. That is correct.

The CHAIRMAN. That is what I wanted to ask you.

Mr. GOLDSBOROUGH. Under the bill, the directors of the Federal Reserve banks would still elect their governors, subject to the approval of the Federal Reserve Board, and the majority, that is, 6 of the 9 directors are bankers?

Mr. COOLIDGE. That is note quite correct. Six of the nine are elected by the stockholders who are the banks, but only three may be bankers. I think I am correct in that statement. So the other three would not be bankers.

Mr. HANCOCK. The three appointed by the Federal Reserve Board must be bankers, which would mean——

Mr. GOLDSBOROUGH. I mean the six would either be bankers or would be members appointed by bankers, which, in my judgment, amounts to the same thing.

Mr. HOLLISTER. You have stated that the bill in its present form is satisfactory to the Treasury. Are you aware of the suggested changes that Mr. Eccles presented to the committee in his testimony?

Mr. Coolidge. When you say in the suggested form, I would like to make clear that the purposes and general form of the bill are favored by the Treasury. The exact form is not of particular consequence, or the particular business of the Treasury.

Mr. Hollister. Of course, inasmuch as the bill itself does not state what is purposes are, some people might read different purposes in the bill than others.

Mr. Coolidge. My only point is that I do not want to approve every dot on every " i " and every cross on every " t." I do not feel that I am in a proper position to do that, because I have not spent the time that Governor Eccles has spent on the subject.

Mr. Hollister. You have not looked over the memorandum of several pages which Governor Eccles submitted to the committee?

Mr. Coolidge. I have seen the changes proposed, but I am not prepared to state that the Treasury is back or is not back of those changes. I will be glad to have you enumerate the changes and to say what I feel about them.

Mr. Hollister. I have not that memorandum before me, but there are several of the changes that I can remember.

One, particularly, is this. As I understand it, Mr. Eccles has changed his views with respect to this open-market committee of five, and suggests that it would be much better that the Federal Reserve Board have complete control over the open-market operations, with a committee consisting of the governors of the various regional banks, with which a member would be compelled to advise prior to taking any action.

Mr. Coolidge. I do not think I would be personally prepared to back that particular recommendation. I think the committee should be composed of a combination of the two.

Mr. Ford. Was that the testimony given before the committee by Mr. Eccles? I do not remember that that was brought up before the committee; I thought it was suggested that it be composed of two from the Federal Reserve banks and three from the Board.

Mr. Hollister. That is in the bill, and as I understood Mr. Eccles' suggestion, he thought it would be much better to have the Federal Reserve Board have complete control.

I questioned Dr. Goldenweiser yesterday when he was before the committee concerning the statement that the power was left in the regional banks to control in some way the open-market operations, and he finally admitted that the only power given was the power to advise; that there was absolutely no power whatsoever either to initiate or to compel action, or to veto. The full power, under Mr. Eccles' suggestion, would be in the Federal Reserve Board to compel the Federal Reserve banks to enter upon open-market operations.

Mr. Hancock. I think Mr. Coolidge should be informed about the suggested amendment before he undertakes to answer that question.

Mr. Coolidge. I have seen the suggested amendment, and what I say is——

The Chairman. He thinks that the provision of the bill is more desirable.

Mr. Hancock. Mr. Hollister failed to state that under the Governor's suggestion, an advisory committee would be appointed from the governors to advise with the Federal Reserve Board before any such power became effective.

Mr. COOLIDGE. I understand that, and I do not wish to make a great point of it. But my personal feeling is that the money is owned by the Reserve banks, and that some Reserve bank governors should be on the committee investing those funds.

Mr. HOLLISTER. There are two purposes, I suppose, for which open-market operations can be carried on. One is the easing or tightening of credit or money. That is the chief purpose, so far as I understand it, of the whole theory of open-market operations.

Is it not also true that if full compulsory powers are given with respect to open-market operations, we will say to the Federal Reserve Board, or even to a committee which the Federal Reserve Board controls, that also this power might very well be used to compel the Federal Reserve banks to acquire securities directly from the Government, in the event that the Government has the securities it wishes to sell, and there is no other way of selling them?

Mr. COOLIDGE. That, presumably, would be within the power of the proposed committee if they so wished to use it.

Mr. HOLLISTER. That is something new in the law?

Mr. COOLIDGE. The same powers can now be exercised, only in a more complicated manner. The committee and the Reserve Board combined have the use of the same powers that is now proposed to concentrate in this committee.

Mr. HOLLISTER. But at the present time no reserve bank may be compelled to enter open-market operations if it decides it does not want to.

Mr. COOLIDGE. I think that is true.

Mr. HOLLISTER. Whereas under this bill, if it is passed, the Federal Reserve banks could be compelled by whatever body we decide upon, whether the committee or the Federal Reserve Board, after consultation with the advisory committee, to acquire bonds.

Mr. COOLIDGE. To both buy and sell; that is the intent.

Mr. HOLLISTER. The thing that worries me chiefly about the bill is the compulsory feature, the fact that the credit resources of the country might be compelled, notwithstanding what the great majority of good bankers might think as to the advisability of it—the great credit resources might be compelled to be used in the handling of bond issues, in the event that the Government continued to pile up deficits, and I would like to ask you whether you think that is a wise power to put in any board which is, to some extent, if not entirely, under administration control.

Mr. COOLIDGE. I would like to answer that very directly. I think the power is going to exist somewhere. I think it is rather unfortunate to have the power wielded by 12 separate banks.

I think the power should exist in a board, and that the board should be very carefully selected. The power is going to be somewhere.

Mr. HOLLISTER. The affirmative power to compel the regional banks to cooperate in acquiring, and you say also in selling—and I am worried about the acquiring end of it—in acquiring Government securities.

Mr. COOLIDGE. It seems to me, otherwise a regional bank may act on its own and interfere with the action of others, and then you have the picture of 12 regional banks, each with the power to do what you say you do not like to see concentrated.

Mr. HOLLISTER. Of course, if a majority vote of the regional banks could settle it, that would be one thing. But here would be the power in a board outside of the regional banks, and even if the regional banks unanimously thought that was a mistake, under this power they could be compelled to go into these open-market operations.

Mr. COOLIDGE. Your suggestion would be that the regional banks be given a veto over the open-market operations——

Mr. HOLLISTER. Yes; or a majority of the committee.

Mr. COOLIDGE (continuing). Of the committee.

Mr. HOLLISTER. What the open-market committee proposes that might not be wise, and it seems to me there should be some way in which the mass opinion of the bankers of the country might be able to check what they might consider as dangerous administration policies.

Mr. COOLIDGE. You have there a question as to the best method to attain the end.

Mr. HOLLISTER. Yes.

Mr. COOLIDGE. I am not prepared to recommend any method as the best possible.

The CHAIRMAN. As a matter of fact, Mr. Coolidge, under the present plan 11 of the banks might agree upon a policy which might be approved by the Board, and the entire 11 banks might desire to carry it out; but it would be in the power of one bank, if it was sufficiently strong in resources, practically to nullify a policy that might be desired and determined upon by all the other banks of the System.

Mr. COOLIDGE. That is the present situation.

The CHAIRMAN. That is the situation now.

Mr. COOLIDGE. It is that situation that we desire to correct.

The CHAIRMAN. And the truth is, as the matter now stands, instead of having control in the 12 banks, we have control in a very small minority of the banks in number. That is the practical situation. The whole truth is, the power is in one bank to dictate the policy of the Reserve System.

Perhaps you do not care to say that, and I will put it in the form of a statement instead of a question. That seems to be the situation.

Mr. HOLLISTER. I do not consider the present situation satisfactory at all, and I only feel we are going too far in this bill in taking all powers whatsoever away from the regional banks except the advisory power.

Mr. HANCOCK. Mr. Coolidge, I assume that both your position and the attitude of the Treasury Department is that, since you are to a large degree charged with the responsibility of furnishing the Nation with an adequate supply of money at fair cost, the present law should be changed so that you may have the control or power necessary to carry out that responsibility.

Mr. COOLIDGE. I see a situation which is proposed under this bill with great powers of control vested in the open-market committee and the Reserve Board and other types of control in the Treasury, and I see a great need of cooperation between those two. But they are independent parties; one is not dominated by the other.

Mr. HANCOCK. Under the open-market plan suggested in the bill, would it not be possible, under certain circumstances, for the will of the Federal Reserve Board to be thwarted in the event that one member of the Federal Reserve Board out of 8 members serving on this committee, together with 2 of the governors, also serving on this committee, should agree on a policy contrary to the known or expressed view of the entire Federal Reserve Board? I hope I make myself clear.

Mr. COOLIDGE. I do not quite follow that. The Federal Reserve Board can elect 3 members, although 1 must be the Governor. They can choose which three members they desire to sit on the open-market committee. I do not vision an alignment where special parties are going to line up against other parties. I visualize them as a group of men who meet to discuss conditions, and I do not think there are 2 against 3 in the matter.

Mr. HANCOCK. I am just wondering whether that situation might not exist, in view of the fact that there have been conflicts heretofore due to the lack of coordinated effort on the part of all the parties interested. That suggestion was made by Mr. Eccles, I think, as the basis for the suggested change in one of his amendments. He recommended that the powers should vest in the Board as a whole rather than in a joint committee as the bill provides.

But if you do not care to make any further expression on that point, it is all right. It is vitally important, however, in my judgment.

Mr. COOLIDGE. I think that is a matter of opinion. I personally feel that there should be governors of Reserve banks on the open-market committee.

Mr. HANCOCK. In Mr. Eccles' statement before the committee he referred to certain language used by President Woodrow Wilson in his address to the joint session of Congress on June 23, 1913. I am wondering whether you subscribe to Mr. Wilson's idea and conception of the control of banks. Here is what he said:

> The control of the system of banks of issue must be vested in the Government itself so that the banks may be the instruments, not the masters, of business and of individual enterprise and initiative.

Is that your conception?

Mr. COOLIDGE. I want to be rather certain; I am not quite sure of the meaning of his conception. He set up the Reserve System, and whether that was his idea of control by Government, thinking of the Federal Reserve Board as exercising that control, would be a question. I certainly feel the Reserve System is an instrument, not a necessity, of business.

Mr. HANCOCK. Of course, I do not know exactly what was in his mind, but it is my own personal idea that he would have been disappointed in the operations of the Federal Reserve, based upon my interpretation of his conception of the right kind of banking system that would function in all conditions for the welfare of the Nation, rather than for a few small parts of it.

Mr. COOLIDGE. The control has to exist somewhere, and the control should exist, in my opinion, in some rather independent body of men.

Mr. HANCOCK. Do you think it would be better to vest control in the Government, or vest control of the note issuing power of the Nation in an independent body, which might be called the "supreme court of finance", that would be insulated against direct Government or political influence and commercial banking influence at the same time?

Mr. COOLIDGE. I think that the banking system grows rather slowly. I do not see, off-hand—I am not an expert on these things—I do not see a final solution. I see this bill tending toward certain concentration of power, and I do not feel qualified to state what is the final solution of our banking situation, but I believe it is a long way distant.

Mr. HANCOCK. Mr. Coolidge, I assume you have read in the papers about the number of suggestions from the different organizations that seem to oppose very vehemently title II (and perhaps sincerely), and as a result of their attitude they are suggesting that a comprehensive study of banking and monetary matters by a national commission of appropriate character should be undertaken, rather than for Congress to proceed further with the consideration of this bill.

Is it the attitude of the Treasury that a commission of that character is necessary at this time?

Mr. COOLIDGE. I do not think I can express the Treasury attitude on that very well. I do not think the Treasury has taken any attitude on that question.

Mr. HANCOCK. But you say the Treasury does favor the main purposes of this bill and want them enacted into law, is that correct?

Mr. COOLIDGE. Yes.

Mr. GIFFORD. You have said that the Treasury favors this bill. Is not that because of the necessities of the situation, in connection with the financial deficits of the Government?

Mr. COOLIDGE. I personally favor it, to give some control over the money market. In my opinion the control does not exist today in proper form.

The Treasury is able to finance at very low rates, and I do not see that we need this in order to finance the Treasury operations.

Mr. GIFFORD. The Treasury does not attempt to advise Congress as to its expenditures, perhaps; but you think now that the banks are holding an undue amount of Government securities?

Mr. COOLIDGE. I do not say that. The banks have the Government securities because they wished to have their earning power.

Mr. GIFFORD. Is that not a rather temporary situation?

Mr. COOLIDGE. It may be temporary; someone else may buy them later. I feel that the whole situation is a very involved one, and it is difficult to forecast.

Mr. GIFFORD. Have you made a survey of the probable deficits that are going to be created by this Congress?

Mr. COOLIDGE. I have not.

Mr. GIFFORD. Is not that a matter of great concern to the Treasury, if they have to finance those deficits?

Mr. COOLIDGE. The problem of the Budget is important to the Treasury.

Mr. GIFFORD. After Congress passes these measures, bringing the deficits up to 10 or 12 billion dollars, does not it follow then that the Treasury will be quite interested as to how they are going to finance them?

If you were the treasurer of an organization, as a rule, you would be glad to inform the members of the organization, and even the president of the organization, of the situation regarding the treasury and the dangers, perhaps, involved in making great expenditures. That would be the ordinary procedure, would it not?

Mr. COOLIDGE. I think you have really gotten me a little bit out of my depth. The President has submitted a Budget, and that is before Congress.

Mr. GIFFORD. What I am getting at is this: The Treasury does not feel that they should advise the President of the dangers of the financial situation or the financial deficits, or even advise Congress of the danger of the financial deficits. Is it not the duty of the Treasury to suggest that they may have difficulty in financing the deficits, if they go over a certain amount?

Mr. COOLIDGE. The Treasury has expressed its views in the Budget, and what Congress will do is a matter of your knowledge rather than mine.

Mr. GIFFORD. The Treasury does not feel like even suggesting to Congress that it is all right to spend 10 or 12 billion dollars this year above ordinary expenses, and that you can handle it all right?

Mr. COOLIDGE. I think I would really rather have you ask the Secretary questions on matters of general policy. I trust there will be no such deficit.

Mr. GIFFORD. I do not know whether you want to express any personal opinions, but you are here representing the Treasury. Somebody must represent the Treasury when they come here, and I think we are entitled to the views of the Treasury Department relating to the dangers and difficulties of financing deficits.

You and I come from a section of the country where we once heard a voice say this, which illustrates what I have in mind, that if the bankers lend too much money to their Government they will not have enough left to lend to the people.

Under this theory of financing, there would not be any limit to the amount that the member banks are allowed to rediscount all the time and loan back again.

I am getting back to this point, which I would like to impress upon you, and that is this: Do not the necessities of the times in connection with these vast expenditures of the Government, bring about the actual necessity of this legislation, and is not that the purpose of it?

Mr. COOLIDGE. I cannot agree with that. This legislation, in my mind, is to control the rate for money. From the point of view of Treasury financing, we do not need this legislation in the least.

Mr. GIFFORD. Not if we appropriate $12,000,000,000 in Congress this year?

Mr. COOLIDGE. The effect may be very bad, but from the point of view of Treasury financing I do not feel that we need this legislation in the least.

Mr. GIFFORD. Temporarily, not. But suppose business should decide to go ahead; will not business need this money?

Mr. COOLIDGE. To my mind, the money available, without changing the law, is of an enormous amount, ample for business as well as for proper expenses of Government.

Mr. GIFFORD. That is because of the amount of gold we have in the Treasury.

Mr. COOLIDGE. Yes; and from the point of view of Treasury financing I can see no need for this bill.

Mr. GIFFORD. You can take care of the $12,000,000,000 deficit this year?

Mr. COOLIDGE. I am not prepared for one moment to say that.

Mr. GIFFORD. You will have to be prepared, will you, if we pass appropriations causing a $12,000,000,000 deficit, appropriations calling for that amount of money?

Mr. COOLIDGE. That is a subject which is beyond this banking bill, it seems to me, and it is a broad subject.

Mr. GIFFORD. It is so broad that it seems that it is desired to pass this political bill.

Mr. COOLIDGE. I do not follow that.

Mr. GIFFORD. Is not this bill going to give the Government control over the banking system of the country?

Mr. COOLIDGE. I do not see that it gives it any more than it has today.

Frankly, I do not see the need of this bill for financing the Treasury. There is no need of it from that point of view, in my opinion.

Mr. GIFFORD. You encourage Congress to spend any amount of money, and if I should follow that out I might as well vote for the soldiers' bonus tomorrow.

Mr. COOLIDGE. I am not encouraging Congress. So far as I am concerned, the question of the Budget, to my mind, is entirely aside from the question of this banking bill.

Mr. GIFFORD. It is not entirely aside from it when you have to find the money with which to pay it.

Mr. RUSSELL. Would it not be appropriate to suggest that Mr. Gifford confine his questions to the bill before us instead of going into the question of the appropriations which Congress may make?

Mr. GIFFORD. Mr. Chairman, because my friend has suggested that, I will be glad to do that. But the amount, in all probability, will be 12 billion, and my idea was that there should be somewhere some power that might say to Congress that it looks probable that you will spend $12,000,000,000, and I have named $12,000,000,000 here without anyone contending that that is not true.

I would rather protect you, Mr. Coolidge, than embarrass you, and I will withdraw from any further questioning.

Mr. HANCOCK. Mr. Coolidge, in your own mind there is nothing political about this banking bill, is there? It is designed to help the entire country rather than any particular class or group.

Mr. COOLIDGE. Yes; it is designed to improve the banking situation.

Mr. HANCOCK. It would be used for the welfare of all, regardless of politics, would it not? And any suggestion to the contrary is unwarranted and absurd.

Mr. COOLIDGE. I feel so.

Mr. BROWN of Michigan. Is not the main purpose of the bill to increase the power of the Federal Reserve banks to rediscount paper for member banks in the Federal Reserve? Is not that one of the main purposes of the bill?

Mr. COOLIDGE. The question of whether it is the main purpose, I think, would be open to some argument.

Mr. BROWN of Michigan. One of the main purposes?

Mr. COOLIDGE. Opinion would differ on that. But the bill does enable the Federal Reserve banks to loan on any sound assets rather than on certain specified types. The bill leaves it to the judgment of the individual bank whether they desire to make these loans.

Mr. BROWN of Michigan. But when the individual banks know they can borrow on any sound asset, as expressed in section 13 of the Federal Reserve Act, as amended, they are more likely to be more liberal in their loaning attitude toward business generally, when they know they can rediscount that paper, or borrow upon it at the Federal Reserve bank? When they know that they are going to be less harsh than they have been in the past. Is not that true?

Mr. COOLIDGE. It prevents the past preferences for certain types of assets that are rediscountable. All assets are on the same basis instead of there being a preferred class for certain assets.

Mr. BROWN of Michigan. But the effect of the amendment would be to liberalize, as far as the Federal Reserve System can do it, the loaning policy of the member banks?

Mr. COOLIDGE. I should think so.

Mr. BROWN of Michigan. When they know they can turn over their sound assets and get assistance from the Federal Reserve banks, they will be more willing to loosen up and make loans; is not that a fact?

Mr. COOLIDGE. I should think so. I feel it will be of use in time of trouble, but, on the other hand, it may lead to some careless lending in good times.

Mr. BROWN of Michigan. I want to say, in commenting upon your statement, I am pleased to find you recommend the reduction from 75 to 60 percent as the basis for real-estate loans.

Governor Eccles expressed somewhat the same attitude; and I think, personally, that it is a little dangerous to go as high as 75 percent on long-term real-estate loans on the part of commercial banks, and I want to commend your view in that respect.

Mr. HANCOCK. On the point about which Mr. Brown questioned you, as to changing the law so far as eligibility is concerned, under the provisions of this bill an honest effort is being made to insure liquidity for all sound assets; is not that correct?

Mr. COOLIDGE. I think that is correct. I would rather phrase it a little differently myself. I would rather say that the banks were given power to borrow from the Reserve banks when the Reserve banks desire to loan, and not just when there are certain specified assets in their possession.

Mr. HANCOCK. Under the old system, do you not think that the opinion or obsession of a great many bankers, which was perhaps natural under the system, that everything in their bank had to be liquid, had more to do with destroying real values than almost any other thing? This was particularly true with reference to real estate and local securities.

Mr. COOLIDGE. That is a hard question for me to answer. It is a matter of opinion.

Mr. HANCOCK. You do not think, do you, that the value of an asset, so far as its eligibility for discount alone is concerned, should depend on its quoted value on an exchange? Is that a fair or always honest test?

Mr. COOLIDGE. I think that should be taken into account; I will not say " depend "; I think it should be taken into account.

Of course, at the present time there is no borrowing, and the surplus of funds is such that that provision is of little use. It is of use only in times of trouble.

Mr. HANCOCK. Do you not think that back in the bank panic days, the fact that bankers looked to the exchange quotations rather than to the intrinsic value of the assets in their bank had much to do with the failure of many banks and was in some instances a curse?

Mr. COOLIDGE. It had something to do with it.

Mr. HANCOCK. Do you not know that that system for years and years operated against sound real-estate assets and almost made them worthless?

Mr. COOLIDGE. I think it caused a great destruction of sound assets during the panic. I do not think it operated against them until the depression came on.

Mr. HANCOCK. Do you think that values should be determined by the price you can get for the property within 24 hours, or by the ticker service?

Mr. COOLIDGE. No; and I agree with you entirely on that, at least in times of great panic, but the whole problem is difficult.

Mr. FORD. Mr. Coolidge, I would like to make not so much a question as a statement, and ask you if you agree with me: Under the Federal Reserve Act as at present constituted was it not the idea, in a period of expansion, that it supplied money in a large measure and made it easy to get money for going concerns for going ahead? Was that not true?

Mr. COOLIDGE. Yes; that is true.

Mr. FORD. Then we came to a period of—it was all right for expansion, but when we came to a period of contraction the character or class of assets held by a bank that were rediscounted in an emergency was so restrictive that it did not furnish a cushion to take sudden reactionary or sudden dropping; is not that true?

Mr. COOLIDGE. That is so.

Mr. FORD. Now, then, this measure undertakes to broaden the basis of the assets in the banks on which loans can be made?

Mr. COOLIDGE. Yes; that is correct.

Mr. FORD. So that in a period of emergency a bank can take its sound assets to the Federal Reserve bank and, for temporary purposes, get sufficient currency to meet its demands?

Mr. COOLIDGE. I agree.

Mr. FORD. Therefore, by giving people the money that they are clamoring for, you stop the clamor?

Mr. COOLIDGE. I agree; but the bank has to be sound, and many were not.

Mr. FORD. There has been an attempt made in this committee by the minority to show that the sole purpose of this measure was to make it easier for the United States Government to borrow from the banks. That has been the purpose of the minority right through, and they have left out any possible good that was contained in the bill for the purpose of using it, the banking system, as a national institution as against a particular institution that was particularly framed for the facility of just a limited class.

Mr. COOLIDGE. I stated already that I saw no possible need of this bill from the point of the Government financing, as far as that is concerned.

Mr. FORD. This bill does not cover that; in other words, they are going on and doing the financing without it, and it will not even facilitate your financing?

Mr. COOLIDGE. I do not see that it facilitates financing. We have always sold our bonds to people who wanted to buy, and expect to continue so.

Mr. FORD. And the attempt to show that this is simply a bill for the purpose of enabling the Treasury Department to finance its needs is pure bunk?

Mr. COOLIDGE. In my opinion, there is no need for the bill for that purpose.

Mr. HANCOCK. You are pulling your rate of interest down practically every new issue, are you not?

Mr. COOLIDGE. Yes; interest rates are running lower and lower and we are selling a lot of bonds at lower rates.

Mr. HANCOCK. I have no other questions, Mr. Chairman.

The CHAIRMAN. Any questions by anybody?

Well, Mr. Coolidge, this is not important, but I think there was one slight unintentional inaccuracy in your statement as to the make-up of the committee. I understood you to say that there would be three members of the Federal Reserve Board to be elected to the Board. As I understand the provisions of the bill before us, it is that the Governor would be a member and two others would be elected; is that correct?

Mr. COOLIDGE. That is correct. I was careless in that statement.

Mr. HOLLISTER. I would like to ask one question on the theory which is, perhaps, too broad and you would not like to answer it; but if that is so, you are at perfect liberty to say so. As I stated before, it is the compulsion that worries me in this bill, chiefly worries me. When the situation gets such that it is compulsory, in the very nature of things, to take the bonds, that is the first step, of course, in credit contraction. That is, I suppose, axiomatic, is it not?

Mr. COOLIDGE. I do not quite follow "compulsion" in it.

Mr. HOLLISTER. You say, of course, it would not be compulsory, but if it were compulsory and compelling upon the banks of the country to take Government bonds against their better judgment—I suppose when that time comes, it is really compulsory, is it not?

Mr. COOLIDGE. That is a very bad time; yes.

Mr. HOLLISTER. In other words, when it comes to financing by any government, the difference in financing the Government's expenditures by the issue of bonds—which is, of course, borrowing from the accumulated resources of the country—and financing by the issuing of currency, the difference in the two is that the issue of bonds is a voluntary matter; it is a question of bargaining between the parties, of the seller on the one hand and the buyer, being a willing buyer, on the other hand; but when a government once reaches a situation where it decides to do its financing merely by running the printing presses, the difference is that they are compelling a person who would ordinarily be a buyer—compelling that person to take the piece of paper, which is the promise of the government, and really against his will—then, of course, the value of that paper goes down, because the person does not want what he is compelled to take.

Therefore, if the situation should ever come about where bonds must be taken, where there is a compulsion placed upon the credit resources of the country to take the bonds, there is not much difference between the sale of bonds and the issue of currency, is there?

Mr. COOLIDGE. Yes; that sounds pretty logical.

Mr. HOLLISTER. And I simply wanted to bring that out for the record, wherein a central board, as long as it is not constituted by the people, or on which they might not have majority control, or at least the veto power—that is the situation which is dealt with in this bill.

Mr. HANCOCK. Mr. Coolidge, apropos of what my good friend, Mr. Hollister, has just said, it is also true, is it not, that the Government should have the right, at all times, to use any profit which it might have in the Treasury for the payment of its obligations, without resorting to he further issuance of bonds?

Mr. COOLIDGE. Well, that seems perfectly logical.

(Here follows discussion off the record.)

Mr. CROSS. Are you through, Mr. Hancock?

Mr. HANCOCK. Yes.

Mr. CROSS. Mr. Coolidge, what do you think, what is your idea about the open-market operations, having the effect of being able to raise or lower the wholesale commodity prices?

Mr. COOLIDGE. I do not pose as much of an economist on that subject. I should say the effect was a slow one, and only one of many forces affecting price levels.

Mr. CROSS. You remember—or were you with the Department in 1923 and 1924, and through there—I think it was in 1924, or 1923, that they had an open-market committee, and their open-market committee bought $510,000,000 of bonds, and almost immediately the wholesale commodity price level rose 11 percent, and agricultural commodities rose 20 percent. Do you remember that occurrence?

Mr. COOLIDGE. I am sorry to say I do not. I remember it, but not in detail sufficient to help you.

Mr. CROSS. Anyway, the theory is that, when you buy bonds, you tend to lift the price level and when you sell bonds you take the currency out of circulation and tend to lower the price level, and that is one of the levers you expect to use along that line?

Mr. COOLIDGE. That is a lever. I feel that is one of many other forces. If you look back to the war time, when we entered the war, the Federal Reserve banks had pretty high money rates, but under of the force of spending money, and so on, prices were driven to very high levels. So I would not feel that the rate for money caused by open market operations is more than one of several forces that operate on the commodity price levels.

Mr. CROSS. How long have you been in the Treasury Department?

Mr. COOLIDGE. Just under a year.

Mr. CROSS. Have you discussed the question of there being put in the law a goal to which the Board should seek to go, for instance, something along the lines suggested by Governor Eccles, that you attempt to reach the price levels, for instance, in 1926 or some such period through there? Did you discuss that with them? What is your idea?

Mr. COOLIDGE. I did a little, and tried to apply it to different periods of the past. Now, if it were applied in 1917, when we entered the war, the Board would have been almost under a duty to stop the Government spending money to fight the war, because that would have been their only method of keeping the price levels where they were. When we get to 1932, we all knew the price levels were too low, yet that language seemed to tell the Board to keep the price levels stable and not permit a rise.

Mr. CROSS. Are you familiar with the system that Sweden has put in force?

Mr. COOLIDGE. Not sufficiently to discuss it.

Mr. CROSS. I believe that is all.

Mr. HANCOCK. Mr. Chairman, I would like to ask one more question. Go ahead, however, Mr. Williams.

Mr. WILLIAMS. I have in mind one or two questions to ask you about this board. You have perhaps answered it while I was out, but as I understood you, before I left, you were of the opinion that open-market operations should be centered in one particular board, for the reason that it was a national policy, and it should not be interfered with, or have divided authority by each bank or each group of banks being permitted to pursue their own course along that line.

Now, it is desirable, is it not—that is true, I think, myself, as a general policy—that the board should be brought in contact with, and kept in close touch with the representatives of the various individual banks throughout the country, in order to get a true picture of the situation that exists at any particular time throughout the country?

Mr. COOLIDGE. I agree entirely.

Mr. WILLIAMS. Now, under the present set-up as it has been from the beginning, the Secretary of the Treasury has been a member of the Board. Has there been any thought given to setting up a board without him on it?

Mr. COOLIDGE. I have heard that discussed by different people. I think I would rather have him answer that question.

Mr. WILLIAMS. Well, no; I do not mean to be personal at all, not because of this particular Treasurer, but what is the idea back of any of the Treasurers being a member of the Board?

Mr. COOLIDGE. I do not see that it is of any particular importance.

Mr. WILLIAMS. No particular importance? Well, then, what is the idea of having the Comptroller of the Currency being a member; is there any reason at all for that?

Mr. COOLIDGE. I would rather leave that to him. I do not know his duties and——

Mr. WILLIAMS. I mean to say, any reason——

Mr. COOLIDGE. I am not sufficiently familiar with the connection of his duties with the Reserve Board, the bank examiners, and so on, to answer that. I would really prefer not to go into that subject.

Mr. WILLIAMS. I do not mind saying, myself, that I do not see any reason for the existence of his office at all, much less for him to be a member of the Board.

Mr. COOLIDGE. Both of those are questions I would rather have addressed to them, or to the particular or appropriate persons involved.

Mr. WILLIAMS. I thought perhaps, in framing this legislation, the need of membership on the Board of the Comptroller of the Currency and the Secretary of the Treasury had been considered.

Mr. COOLIDGE. It was decided not to recommend changes in the Reserve Board.

Mr. WILLIAMS. Well, unless there is some good reason why they should be there, I do not know why they should be members of the Board, and I was just inquiring as to what the reason was.

Mr. COOLIDGE. We decided not to go into the composition of the Reserve Board.

Mr. WILLIAMS. You have gone into the composition of it, in submitting this bill, have you not?

Mr. COOLIDGE. We did not change the composition of the Reserve Board.

Mr. WILLIAMS. Of the Reserve Board, but you did change somewhat their functions in the open-market operations.

Mr. COOLIDGE. Yes.

Mr. WILLIAMS. I believe that is all.

Mr. HANCOCK. Mr. Coolidge, just one further question: From the statements made by the different members of the committee and the discussion which has taken place here for the past 10 days, it seems that there is a fear being planted in the minds of some people that, under this measure, the Government might be in position to compel or force banks, against their will, with respect to the open-market operations. Do you not believe that it is necessary that there should be some central control, so far as open-market operations are concerned, and especially when we review what happened back in 1929?

In other words, do you not believe that there might come a time when the compulsory powers contained in this bill, if you care to call them that, would be absolutely necessary, and especially if the country should be off again on a wild speculative "jamboree"; and if you had those powers, you would be able to enforce uniformity by all of the banks, in order to serve the country, and save the country from the sort of crash like we experienced in 1929, 1930, and 1931; and then, by the reverse use of those powers, in a period of great depression and deflation and dislocation, the Government could and should employ those powers in the interest of all of the people, going so far if necessary of forcing banks to purchase Government obligations, to sustain and protect the Government in its duty to enable people to live and not starve?

The CHAIRMAN. Well, have you finished?

Mr. HANCOCK. Let him answer that question, Mr. Chairman.

Mr. COOLIDGE. Excuse me. I agree with you. I think that the power should be concentrated, and I think the open-market committee should act to prevent excessive speculation and furnish money in times of deflation.

Mr. HANCOCK. And that is the main purpose why these changes are put in this bill, is it not?

Mr. Coolidge. That is the purpose that I see in it.

Mr. Hancock. That is all, Mr. Chairman.

The Chairman. Well, gentlemen, if there are no further questions, we will excuse Mr. Coolidge. We thank you for your able and informative statement.

Mr. Coolidge. Thank you, Mr. Chairman.

The Chairman. We will adjourn and meet tomorrow at 10:30, gentlemen.

(Thereupon a recess was taken in the hearing until 10:30 a. m.. Friday, Mar. 22, 1935.)

BANKING ACT OF 1935

FRIDAY, MARCH 22, 1935

House of Representatives,
Committee on Banking and Currency,
Washington, D. C.

The committee met at 10:30 a. m., Hon. Henry B. Steagall (chairman) presiding.

The Chairman. The committee will be in order.

We have with us this morning Mr. Robert Hemphill, who was the first credit manager of the Atlanta Federal Reserve Bank and is well known as an authority on money and banking and as a financial writer contributing to the Hearst newspapers and to financial magazines. He will discuss this bill, and I am going to suggest that he be permitted to make his statement without interruption, after which members of the committee may propound any questions that they may desire.

STATEMENT OF ROBERT H. HEMPHILL, WASHINGTON, D. C., REPRESENTING THE NATIONAL MONETARY CONFERENCE

Mr. Hemphill. Mr. Chairman and gentlemen of the Committee on Banking and Currency, I am not an orator; I have been in business all my life, so I am going to get down to business as rapidly as possible.

This banking bill which is offered, in my opinion, crystallizes in a large measure, and perpetuates and exaggerates what is today the worst monetary banking system in the world.

In the founding of our country the patriots who had vision enough to protect us from tyranny and to imagine a society composed of intelligent individuals who would be permitted to carve their own destinies, saw that the control of money would control the total amount of business transactions, and that the total amount of goods and services people can produce and exchange with each other marks the measure of civilization.

That is all there is to civilization, creating and exchanging the facilities for a higher standard of living. That is all there is to it.

Necessarily, in our system, we cannot directly exchange our goods and services; we have to first convert them into money. Money is the intermediate commodity, if you wish to call it that, into which we have to exchange everything we produce.

So this subject, Mr. Chairman and gentlemen, is necessarily as important, just as important as all of the rest of the subjects which a civilized people has to consider. I think that point is worth getting clearly in your minds.

To exchange those goods and services there must necessarily be in existence an available quantity of money which is equal to all of the goods and services in process of exchange. That is a self-evident proposition. We cannot exchange in any other way.

If you diminish that quantity of money, you are going to restrict the exchange of goods and services, and restricting the exchange of goods and services means that you lower your standard of living, and that means that you destroy civilization to that extent.

That is a principle that has been recognized by every philosopher of ancient and modern times. But there has been for 200 years, since one certain man came into power as a financial genius, Mayer Anselm Rothschild, who was born in 1790—since he came into power there has been a constant, organized, shrewd conspiracy to convince the people of the world that this is not true, to convince men against their own judgment, against a thing which is self-evident. And that conspiracy has involved the press, it has involved the pulpit, it has involved our schools, a conspiracy to mislead people about the importance of a very simple thing—money.

The interests who promote this confusion profit by retaining for themselves the monopoly of manufacturing our money.

If you will pardon me a bit, I will read you a little fable at this point which illustrates how our private banking system originated. Sometimes these things get home the central idea a little clearer than by technical explanation.

This is the fable of the Temple of the Thirteen Suns, a very ancient fable.

Once upon a time to the Temple of the Thirteen Suns came the rich and powerful chief, Oomah the Third, who said to the goldsmith of the temple, Hansen L. Roschab, "I have much gold and am about to depart for a far country. Wilt keep this gold safely for me against my return a year hence? I will pay thee well."

The wily Hansen coughed loudly and covered his countenance with a cloth lest the rich Oomah the Third observe his joy to have this treasure in his possession. When he was calm and could look serious he said unto Oomah, "It is a very great responsibility and risk but I will undertake it for a tithe which shall be 1 shekel in every 10."

Then said the Chief Oomah, "it is a deal", and forthwith his slaves delivered many bags containing in all a thousand shekels of gold for which Hansen L. Roschab, the goldsmith, gave the chief a parchment deposit writing payable to whomsoever, and thereupon Chief Oomah departed happily upon his journey.

As soon as he was well out of the country the shrewd Hansen called his confidential scribe and bade him thus, "Go thee now to the merchants whom I tell thee of and secretly say to each that thy master hath a little gold for hire upon good security", and the servant departed swiftly.

Soon there came to him a great merchant, who said, "Hansen, you old crook, I am in a jam for a few shekels of gold. Wilt lend me?" and Hansen replied, "Money is very tight these days, but it might be so arranged. What is thy need?"

The merchant answered, "Two hundred shekels."

Then said Hansen, "It is much money. What security couldst thou pledge for so great a sum?"

Then the merchant shewed Hansen a writing of his possessions of merchandise to the amount of a thousand shekels. Hansen said, "It is not enough; thou must also pledge thy dwelling and thy slaves and thy raiment", whereupon the merchant, after much protest, pledged all his possessions, even to his innermost raiment.

Then said he to Hansen, "I have no place to store so much gold—keep it safe for me and give me a writing which I may deliver to whomsoever I will", and Hansen did even so.

The next day came another merchant, and another, and still another, and to each Hansen loaned a portion of the gold of Chief Oomah the Third, taking from each as security his entire possessions, including his innermost personal raiment, and gave to each a writing upon parchment shewing that each had on deposit the gold he had borrowed, until upon the tenth day he had given parchment deposit writings for the whole of the thousand shekels; but he still had all the gold.

Hansen reflected much upon this curious state of affairs, and said to himself, "These birds know not how much gold I possess. They do not want the actual gold itself—what they really want is credit, some deposit writing which they may pass from hand to hand as money. I have one grand idea."

On the next day came another merchant, and another, and still another, and to each Hansen shewed the great store of gold of Oomah the Third, and to each he pretended to loan a portion, although he had previously loaned it all to the first ones who came.

And it came to pass that at the end of another 10 days Hansen had pretended to loan to many more merchants and had given writings of deposit for a second thousand shekels, making 2,000 shekels in all, although he had only the 1,000 shekels of Oomah the Third.

And still he had all the gold.

Whereupon Hansen reflected to himself, "What a leaden-pipe cinch. I wonder I did not think of this before. I can collect just as much usury for the phony deposit writings as for the genuine—verily I am a financial wizard."

Thereupon Hansen caused it to be noised about that he possessed a vast store of gold for hire, and many more merchants came to borrow, and to each Hansen delivered writings of deposit and collected generous usury and demanded pledges from each of all his possessions even unto his innermost personal raiment, until he had issued writings of deposit for 10,000 shekels and held mortgages on substantially the whole city.

Then went Hansen to the wise man of the city and said unto him, "Verily I have discovered the greatest racket of all time. I have learned the magic of making gold out of "baloney"; and if I can keep my formula secret for a few years, I will collect a fortune that will make Solomon's treasure look like a second-hand clothing store. Tell me how I may keep secret this bonanza for mine own profit."

Then said the wise man, "Look wise and say little and only upon little known matters afar off. Obtain the ear of the town crier. Engage him to spread the impression that money is a mysterious subject which no one understands save thee alone. Be friendly with the king's councilors and grant their favors that the king may smile upon thee."

And Hansen did as he was bid and collected much usury from his phoney loan deposits and built for himself a mansion, collected works of art, and clothed his wives and concubines with fine linen and jewels, and when his business had grown to many times its humble beginnings, he took over the entire temple and by way of a sly joke called it the first national bank, the same being from an obscure language and meaning "Place of imaginary money."

And that is the reason all banks have great marble pillars and bronze doors, so that they may resemble outside as well as internally the "place of imaginary money" which Hansen L. Roschab builded upon the gold of Oomah the Third in the Temple of the Thirteen Suns.

I have read this fable because sometimes a little foolish parable like that will give one a very much clearer idea of what we use for money than a whole book of economics.

When this country was founded and the Constitution was framed, it was unquestionably the idea of the patriots who founded this country that Congress should issue all the money necessary to exchange the goods and services of this Nation. To get what passed in those men's minds we would have to go back and picture the situation at the organization of the United States, the Thirteen Colonies, who were not so sure of their own governments, and were not so sure of this federation that they were forming.

They were afraid to delegate very much authority but they did delegate to the Congress of the United States the sole power to issue money, and took it away from the States, prohibiting the States from issuing it. But they failed to provide a system by which Congress would issue the money. They failed to visualize the rate at which the commerce and industry of this country would grow, and to provide some system which would be under the direction of Congress, which would keep pace with the growth of industry and commerce and provide a sufficient quantity of money and keep it in circulation, to enable the exchange of goods and services.

Private banks were formed, and the pressure for more money than there was in circulation was so great that these banks began issuing their own money, wildcat bank notes, we call them, and it was an important service. It was an unsafe and an unsound service, but it was an important service, because that money was greatly needed.

They say that there is in use in the United States today a very considerable sum of counterfeit money which is passing from hand to hand, and making it possible to exchange goods and services. I do not know how much there is; I have heard some people estimate there is half a billion dollars constantly in circulation, performing just as important service as the money which is issued by the United States Government.

Now, we go further and find that these banks which issued this wildcat money, one after another failed, and created enormous disturbances. One bank failure back there in the early eighteen hundreds was a matter of very great importance in the United States. At that time we were a country of small population and commerce, so that one bank failure was a tremendous event and created a panic, and we had a succession of those panics.

Finally, the Government prohibited the issuance of these private bank notes. And again, Congress failed to supplant that mechanism with some other adequate mechanism. Congress failed in its duty to provide for the issuance of enough money to sustain our rapidly expanding industry and commerce, and another disastrous depression ensued.

The pressure for more money than Congress has ever furnished has built up another system, which is just as wild, just as uncontrolled, and just as uncontrollable as the wildest bank-note system, and that is our present wildcat bank-credit system.

In every particular, and in every effect the issuance of bank credits by the commercial banks today is exactly the same thing that we prohibited back there in the sixties, and it is just as dangerous.

I have no quarrel with the bankers; the bankers are doing wonderfully well with the most imperfect system, the most unsound system which could possibly be devised.

There is no business man anywhere who would operate a commercial bank today. I know; I am talking as a banker to you, although I am now out of the banking business. But, there is no business man who would operate a commercial bank.

There is no business man who would operate an institution so inherently unsound as a commercial bank. There is no man who would take hold of a business which had demand liabilities 10, 15, or 20 times its currency and liquid assets.

It is a preposterous thing, when we look at it in a cold, calm, dispassionate way. It is the most preposterous institution in the civilized world today, and yet we are absolutely dependent upon that unsound, preposterous institution to issue the money with which to transact our business, our exchange of goods and services.

Congress has consistently failed, or declined to study this monetary question and devise some instrument which would efficiently execute the power that was conferred upon it in the Constitution.

Do not blame the banker; he is simply filling an essential need, a facility which civilization must have, in the only way he can do it, in the creation of bank credits, just as this fabulous character I have read about this morning issued phoney deposit writings.

The banks are still doing the same thing. They are creating imaginary money because commerce and industry has to have money of some kind. If Congress continues to fail in its most important duty, some private device must supply the deficiency. But I do want to make it clear that we have got to have a quantity of money which is absolutely, mathematically related to the amount of goods and services which we are in process of exchanging. The speed with which they can move from one transaction to another is determined by the facilities of our present state of civilization, facilities used in our trade such as transportation, and that sort of thing, and the method of clearing checks. All these elements are fixed and move only so fast.

So, the amount of money which is in circulation, of some kind, some usable medium of exchange, necessarily determines the total amount of our exchange of goods and services.

That is the central proposition in this whole money question. That is the central proposition to which we have got to give consideration; I do not care whether you are monetary students or not, you can certainly understand that one thing, that you have got to have in circulation a quantity of money equal to the total amount of goods and services you are going to exchange, because you have to first convert them into money to exchange them. They have all got to be converted into money first. That is the central and controlling proposition.

It is only in recent times that we have collected enough data to get some fairly dependable idea of that relation; not because we could not have collected it 50 or 100 years ago, but because there has been a constant effort, as I told you a while ago, on the part of interested parties, to talk about anything in the world except money.

Therefore, we have all grown up and accepted money as a matter of course, and nobody makes any inquiry about it until it stops coming in.

When it seems as if the common source of our money is drying up, as it has been for the last 5 or 6 years, then people begin to think about money. Then they are told, through the daily press, that it is a mysterious subject which no one can understand. But that is "baloney."

There is nothing at all about money or finance, or about banking, that a 12-year-old boy clearly grasp and understand.

Banking is simply a private system of creating the money that commerce and industry has got to have, because Congress has failed to issue it. That is all there is to it.

Today, in the situation which has developed since this depression started, we have almost completely reversed the intention of the men who founded this Nation. It was intended then that the Government should issue the money, all of it that we should use, and that the banks should receive that money and care for it and loan the idle surplus of their customers, their time deposits, and their savings. Today the banks are creating the money and the Government is lending it. We have the Government in the banking business and the banks in the Government business. That is the present situation.

This bill that is before you gentlemen is designed to make no fundamental change in the banking business. It is designed to bring under control of one body of men, who may be good, bad, or indifferent, and who may be ethical or who may not be, and who may be impressed with a duty to the public, or who may be impressed with a duty to some private interest, the control of the monetary system of the United States. And when I say that, I am going to tell you that it puts into the hands of those men the control of your business and mine, because those men will control the total volume of money, and you and I can get our share, and that is all we can get, of the total amount. If they double the amount in circulation, we can get our share of the increase, and if we compete properly, our share will be twice as great as it is now.

You can take the contraction in demand deposits, subject to check, today as compared to 1928–29 and figure the gross income of your own business, whatever business you are in, if you have a business, and you will find that the contraction in your business is almost identical with the contraction of demand deposits. The contraction of the business of the Nation is almost identical. In fact, it is so close that it is absolutely astonishing, because it is figuring on a rule of thumb formula, and we have available for our calculations the total amount of money represented in these demand deposits for 1 day only in the year, 1 day only, and we now nothing about what the average is. Assuming that these total figures for 1 day, June 30, is the average for the whole year, which certainly cannot possibly be more than an approximation, we find that the national income is invariably about 3 to 1.

If we had some accurate figures for every day in the year and had an actual average, I am convinced—and when I say that, gentlemen, I want you to understand I have given this particular subject profound study for 20 years and have made extensive researches—I am convinced that it would always be within 10 percent of 3 to 1 of our national income, under all circumstances, in good times and bad, that is to say that the total income of this Nation in prosperity or depression is within 10 percent of three times the total amount of the medium of exchange in circulation.

Mr. Cross. Do you include check money and all the backbone money?

Mr. Hemphill. Yes; money—checking accounts and cash.

I have prepared some figures here which are rough figures; I want that understood. I simply took them out of the Comptroller of the Currency's statements and took the income figures from the Department of Commerce, without any adjustment for "float" or without any other adjustments, but simply compared those figures as they run. I have done that as far back as I could get accurate figures, and they invariably run very close to 3 to 1, showing that there is no great difference in the velocity of our total money from one year to another.

	Billions of dollars		
	Demand deposits	National income	Ratio
1929	24.3	81	3.3
1930	24	75.4	3.1
1931	21.3	63.3	3
1932	16.4	48.9	3
1933	15.2	46.8	3
1934	[1] 17.6	52.8	3

[1] Estimated.

Now, then, there has been some increase in the national income, and while the figures are not yet available, the 1934 figures ought to be about the estimated amount shown on this sheet, 52 billion, but the general price level which has been forced up by the Government's artificial price-raising activities more than offsets this increase in income. Normally increasing the amount of money in circulation should produce a greater income through greater activity until we reached full production before there would be any substantial rise in the average level of prices. After that if we continued to increase the money in circulation prices would rise exactly in proportion to this increase. As long as we are operating below full production because of a scarcity of money increasing the money in circulation increases the volume of business but not prices. Profits increase because costs decrease when the volume increases, and wages also increase with the volume of business without increasing prices. In fact, profits and wages may increase very substantially if the volume of business increases greatly and at the same time prices may decrease.

A great many of our economists who talk about the wide variation in velocity of demand deposits are confused because they include in their calculations the money employed in speculation, and at times there is a great deal of money employed in speculation. There was a great sum in 1929. For instance, brokers' loans, I think, ran up to 7 or 8 billion dollars at one time. I do not think they were all entirely employed in speculation, but there was at least $5,000,000,000 at the peak in 1929. A large amount of deposits which should have been classed as demand deposits in 1928 and 1929 were classed as time deposits, and so forth.

These factors eliminate any very fine calculation for that year, any very accurate calculation; for instance, if you wanted to get the figures down to four or five decimal points you would have to take the money employed in speculation into consideration. But this sheet which I have here does not go into the matter to that extent. I think, however, it is dependable as a rough-and-tumble calculation.

This brings your problem, gentlemen, to a very definite objective—that of putting into circulation approximately 8 billions of dollars in such a manner that it will permanently increase our individual demand deposits that amount—to restore the status quo ante this depression.

Now then, the banker has the privilege today of issuing our money, practically all of it. The amount of currency and coin in circulation actually transacts, I believe, less than one-half of 1 percent of our total business. I do not believe that statement has ever been made before.

That does not mean that the proportion of actual money to bank credit should be one-half of 1 percent. But it does mean that you can almost disregard money in your banking calculations, not only because the total of transactions performed with currency are small but also for another reason. The money that we have in our pockets was drawn out of a bank by ourselves or somebody who had a deposit and who drew a check for it, and we ordinarily use it for one transaction only while it is outside the bank. That is, we buy cigars, or pay off the grocer, or pay for some other thing, and it goes directly back into the bank. It does not circulate through several transactions as in our early history before the days of the check book.

Say there is a check for $100 on which you drew out the money you have in your purse. This check has no direct effect on commerce, but you spend this money in several transactions whose total is $100 so that in your total of checks you have automatically all of your cash transactions. But you do not have to bother with the cash at all in your calculations.

Currency and coin in circulation has very little effect on any calculation in which you are trying to determine the velocity of money.

As I see it, the problem before Congress is one of refurnishing this Nation with a sufficient quantity of money of some kind, not guessing at it, and not leaving it to expand or contract by accident—not leaving it entirely to a mechanism that is operated entirely by emotion of two kinds, optimism and fear. Those are the two controlling factors in the operation of the banking system today, optimism and fear, and under this absurd system these two emotions are responsible for our recurring periods of inflation and depression.

When things go along good our banks, prudently and properly, in order to make money for their stockholders, expand this credit money until their reserve is so thin that it looks like cellophane. And as far as our State banking system is concerned, it can go beyond that; it can borrow book credit from another bank and use it as a reserve, so they have no reserve at all. And they loan some more on that bank credit reserve, hoping to God that nothing will happen, and the banker goes around all day in nervous apprehension hoping that nothing will happen. He is out on a limb, clear out on the outermost twig of a limb. And then something does happen. It may be in Russia, it may be at the North Pole, but the banker is trying to operate a machine which requires such a delicate balance of income and outgo that its preservation depends upon the succession of a series of improbable accidents and when something happens, real or imaginary, he gets frantic to get on a safe basis. He begins calling every loan, destroying our active medium of exchange, and industry and commerce are shot as innocent bystanders.

That is the picture of our monetary system today. That is the absurd, impossible system which we, an intelligent and resourceful Nation, are trying to create and exchange wealth with.

Now then, gentlemen, I calculate that since 1929 it has cost this Nation in loss of property values and loss of income $400,000,000,000 to preserve the sensitive feelings of a few men and to preserve a $3,000,000,000 investment in the bank stocks of this country. That is what it has cost us. That is what it has cost this Nation, $400,-000,000,000 in material loss, to say nothing of the total of human suffering and misery and despair, to preserve a $3,000,000,000 institution, and we need not necessarily have destroyed the $3,000,000,000.

New, gentlemen, really, you know, we ought to be approaching the point in intelligence when that sort of thing is no longer possible. We ought to be getting nearly to the place where we could understand this situation and where we, as a Nation, could have some reliable medium of exchange to do business with.

We all know what the banking system is; let us be frank about it. If we could get one week's open honest discussion in America, a perfectly frank discussion, unlimited or uninfluenced by prejudice or selfish interests, we would have a monetary system through the operation of which this country would soon rule the world. We have the resources, and we have a surplus of inventive genius and a very extraordinary capacity for organization in this country. The other nations do not seem to have it. We have the natural resources, and there is no computing, there is no imagination sufficiently active to fully picture what this country could be if we had a sound and adequate monetary system which would permit us to operate at full capacity. We have everything else. We have the resources, we have the productive facilities, we have the machinery for distribution, but we have not got the money to make the transfers that we ought to have. That is all that matters with us today. Eight billions of our demand bank deposits which were in active use—one-third of our active medium of exchange, has been withdrawn from circulation.

That is the only reason all of these alphabetical monstrosities are being created daily by people who have a cloud over their imaginations, who apparently cannot distinguish between cause and effect, but who are trying to remedy, by some obscure means, a glaring thing which is right out before us where everybody can see it, simply the lack of sufficient money to effect the transfer of goods and services we can create. That is all we lack and all we have lacked.

We do not have to promote the interests of any groups, gentlemen, to balance production and consumption. Under the capitalistic system and with a sufficient amount of money in circulation to transfer the things that we produce, we will continue to produce and exchange more until we are at the limit of our producing capacity, until every man in the country is producing all he can, to get all he can in return.

We do not have to protect labor, because when we reach that situation—and I have seen that situation many times in various sections of our country—labor is at a premium.

Your total capacity for production depends upon the labor you can secure, and when labor is at a premium the employer, in competition with other employers, forces automatically and will force without an organized labor effort a fair division of the gross income for labor.

We have had in this country, sometimes for 4 or 5 years at a time, a condition in which we had that perfectly balanced situation. Every time we have reached it some selfish interest strong enough to influence

Congress has opened our immigration doors, getting in a lot of cheap labor, or something of that sort, or has shut off the money and created a panic.

Now, then, Mr. Chairman and gentlemen, my objection to this bill is that it does not amount to anything positive and certain. You have not done anything definite and fixed. You have made no real progress at all in monetary science. You have come no nearer supplying this Nation with a stable, adequate, and permanent supply of money when you have passed this bill than we have now. But you have created the machinery, gentlemen, by which selfish interests could take hold of this central organization and in a very short time own what little of the country they do not already own.

I am afraid of such a device, tremendously afraid of it.

I mean to cast no reflection on Mr. Eccles or the other members of the Federal Reserve Board. They apparently are unable to imagine any system other than the present one. They unquestionably have done in this bill what they could to help make usable the machinery which they propose to control. I believe their intention to use the power they seek for the public good is sincere. But what about future bodies of men you are going to turn this machinery over to, who you cannot control? What are they going to do with it?

Suppose Mr. Eccles passes out of the picture tomorrow and we get somebody out of Wall Street, or some of the partners of Rothschilds in Europe—and we have some of them here in America, and they are the most powerful influence in America today.

Ordinarily, they run our Government as certainly as though they owned it. Suppose you give them this mechanism? That is something to think about, because they are going to be in power again. They may be out of power temporarily, but they will not be for long.

You are creating a mechanism, exactly the mechanism that they have tried to put into operation in this country since the Declaration of Independence. It has no brakes on it anywhere. It just simply creates the mechanism and the power and puts it in these men's hands and says, do what you darn please with it and with this Nation. There are no safety devices; there are no mandates from this Congress, which has the power to say, under the Constitution what they shall do with the volume and value of our money, which controls our destiny.

I think it is the most dangerous piece of legislation that has been offered in the United States Congress for many, many years.

I think it could be amended. I think the objectives of the men who have designed this bill are all right. I think they are moving toward giving this country enough money, but it is for this Congress to put in this bill definite mandates which will compel these men to attain their objectives.

Some time ago there was a call issued by one of the Senators and some men who are devoting their lives to a study of this question for a conference here in Washington of the representatives of a large number of independent organizations, all of whom have made their own independent study and concluded that our present situation is purely a monetary phenomenon. They met here in Washington, and it was called the National Monetary Conference.

I was present at that conference as an independent monetary student, representing nobody but myself. Men were called upon to express their views as I was, and I expressed my views there, and at the conclusion of the meeting certain resolutions were drawn up. I was appointed chairman of the committee to draft the legislation contemplated by those resolutions.

On that committee is also former Senator Robert L. Owen, who designed the Federal Reserve law and, as you all know, is one of the profound monetary students of the country, and who has devoted the major part of a lifetime to this study.

On this committee is also Prof. Irving Fisher, who, I will say, is unquestionably the outstanding monetary authority in this country, and who has devoted at least 20 years to intensive monetary study under circumstances which have given him the opportunity, the extraordinary opportunity, for arriving at correct conclusions. As I say, he was on that committee.

Mr. Robert Bruce Brougham, who has also—in recent years at least—devoted considerable time to this study; Mr. Ward, who is an attorney associated with Father Coughlin, and who was quite prominent in this discussion, and myself were on the committee.

The conclusions of this committee do not represent any personal ideas that these men have. Three of these men are students, real students, not for the purpose of promoting some pet idea but for the purpose of assembling and digesting all of the knowledge that is reliable and available anywhere in the world, and all of the conclusions of all other outstanding men who have studied this monetary question extensively and concentrating for their own guidance, as clearly as possible a summary of the most enlightened thought and investigation and conclusion upon this monetary question, in addition to their own extensive experience and knowledge.

Those men also know this Nation; they know the United States, and I believe are able to distinguish between the necessities of this country and that of other countries in so important a movement as improving our monetary system.

Some things which we need would not fit Europe at all. Some things which they require would not fit us at all.

So we cannot simply take the English banking system or the French banking system, or some other foreign system, and apply it here, because it would not work, for a great many very simple reasons. But some of the foreign systems do have some good features which are abundantly proven by long satisfactory use.

We have drawn up a bill and intended to attempt to interest some of the Members of Congress here who have made a particular study of this question, when this bill which you are now considering came on from the Treasury Department. This bill, which was drawn by Mr. Eccles and by Mr. Morgenthau, or perhaps Mr. Coolidge, the Under Secretary of the Treasury, and the man who is at the head of the Federal Deposit Insurance Corporation, Mr. Crowley. They were the principal parties, as I understand it, in drawing the administration bill. How much advice they took from other people, or how much study they made of the question, I do not know.

I do not think the bill is very adroitly drawn. In some respects it seems to me to be very amateurish.

I perhaps ought not to say that, but it does not seem to me like a fininshed bill, even for what they want to accomplish. However, it is what it is.

We decided—and I am speaking now not as an independent monetary student, but as the representative of the monetary conference—we decided that the cause would be more swiftly advanced if we joined in with the progressive sentiment in Congress which was unquestionably for monetary reform, to see if we could not get all of our ideas together and amend this bill, instead of promoting the measure we had prepared.

I prepared a little statement, which I have here, which presents the concensus of our opinion as to the amendments necessary to make the administration bill constructive, practical, and safe.

I would like to say in reference to these suggestions that there are three proposals here, and they are to a large extent already anticipated, perhaps in other proposed legislation, which has been discussed for the past 3 or 4 years.

The most important proposal, it seems to me, is to create a Federal Monetary Authority. This proposal was first advocated by Mr. Frank Vanderlip, who is perhaps our ablest commercial banker with a full and useful lifetime of experience, and Mr. Goldsborough of your committee, who is regarded as one of your outstanding monetary students.

Mr. SISSON. Do you expect to answer questions asked by members of the committee at some point in your statements?

Mr. HEMPHILL. Yes.

Mr. SISSON. Would it interrupt you now if I asked you one or two questions?

Mr. HEMPHILL. May I read this recommendation first, and then we will have it on the fire.

Mr. SISSON. Yes.

Mr. HEMPHILL. It is recommended that the bill now being considered be amended by striking out title II and substituting therefor three paragraphs in appropriate language which will, first, establish the Treasury of the United States and its branches as the sole depository for all bank reserve funds.

Second, require all banking institutions in the United States and the Territories—and the United States post offices in certain rural districts—to carry checking-account deposits as trust funds in cash in their vaults or deposited in the United States Treasury, or invested in United States Government bonds; and all banks to maintain a 5-percent cash reserve against all time, savings, or other than checking-account deposits.

Third, create a politically independent Federal monetary authority which would exercise, under definite congressional mandates, the constitutional monetary powers of Congress.

As to the last provision I want to say that owing to Congressman Goldsborough's activities you have had before you for 2 years, I think, a monetary bill, or a bill to establish a monetary commission, which is what we have in mind here.

I think it is greatly to the credit of Congress and it is a great compliment to the intelligence and the sincerity of this House of Representatives that you gave that bill such an enormous vote.

Mr. GOLDSBOROUGH. We had a bill passed in 1932 which would simply declare a policy, which was a different bill from the monetary authority bill.

Mr. HEMPHILL. But it had the same objective. You have that principle in all the bills you have introduced here, have you not?

Mr. GOLDSBOROUGH. Yes.

Mr. HEMPHILL. Now, this recommendation further suggests that the mandates should require (*a*) that the Federal Montary Authority purchase for cash or credit upon the books of the Treasury of the United States all United States bonds not held by banks as of some past date, preferably June 30, 1934, or so many of same as may be necessary to restore full employment at a satisfactory price level, and thereafter to keep the price level stable by, first, the purchase or sale of United States bonds; and, second, the issue of currency or assessment of taxes.

(*b*) That the Federal Montary Authority liquidate all Government financing organizations as rapidly as possible by transfer of their business and assets to commercial and savings banks of the Nation.

In other words, let us take the Federal Government out of banking business entirely.

These additional recommendations are suggested: Repeal the Federal Reserve Act, as amended; repeal the National Bank Act, as amended; and let our banks go back to the supervision of the States, all of them.

The program I have read, which is suggested, would put in circulation approximately 15 billions of additional currency and would restore full employment in the Nation, and elevate prices, wages, and property vaues to about the 1928–29 level. It would increase the national income by 45 billions. Thereafter, the payment of normal Federal Government expenses would be substantially the correct amount to preserve full employment without elevation of the price level.

Thereafter the wealth of the Nation would increase as fast as our productive capacity increased.

Attention is called to the fact that it was no doubt the intention of the founders of this democracy that the Government should issue all the money necessary for our exchange of goods and services and that the banks of the Nation should care for it and loan our savings and surplus profits. That situation is now precisely reversed. The private banks of the Nation are creating the money and the Government is loaning it to agriculture, commerce, and industry.

The program proposed is merely a return to the status originally contemplated.

It is also designed to end the present period of wildcat-bank-credit issue, which in effect is but a continuation of the wildcat-bank-note period of the first half of the nineteenth century.

I do not believe, gentlemen, there ever has been a time in our history when the opportunity was so favorable to create for this Nation for the first time, and, in fact, for the first time in civilized history, a real monetary system. We have none today. We have no monetary system.

We have to borrow every dollar that we have in circulation, cash or credit.

If you will examine the consolidated statements of all the banks you will see—we took all the money that the Government issued and bought bank stock with it, and when we finished doing that we had neither money nor bank credit and since that time the individuals in this Nation have been obliged to borrow from their banks every dollar of cash or credit there is in circulation. That may be a startling statement to you, but that is true.

Every dollar you have in your pocket, every dollar of credit you have in your bank account, was borrowed by somebody from some bank. It may have been borrowed by the man who gave you a check for it, or it may have come to him through several different transactions. But if you will go back far enough you will find it was borrowed from somebody, and you are lucky that you have it. If someone, in the chain of transactions between the borrower and you had been compelled to pay a note to the bank, you would not have your bank account today. That will show you how absolutely we are dependent upon a system which is essentially unsound. If we had a system which did not have to destroy commerce and industry to preserve itself, every few years, nobody would kick about it. I am not kicking about the interest we pay; that is a small matter. It is unnecessary, but I am not kicking about that.

But this institution, for its own preservation, has periodically to almost destroy this Nation in order to preserve itself.

Those are the considerations which I think that this Congress of the United States ought to think about. You gentlemen are here representing the people of this Nation and not a few banks in Wall Street or elsewhere; and not just a few subsidized newspapers.

You are here to pass as few laws as possible to preserve individual freedom in this country.

We are slaves today; we are the absolute slaves of an impossible, unsound, unworkable system which creates what we call "business cycles." When things are going good they will go along, but they almost immediately get out on a limb and when everything happens they are compelled to contract the currency we are using to exchange our goods and services and we have a depression and we call these recurrent periods of bank credit expansion and contraction "business cycles."

I think, Mr. Chairman, that I have said all the mean things I can think about for a while, and I will be glad to answer any questions the members of the committee may desire to ask.

The CHAIRMAN. Your objection, as I understand you, to the bill before us is that it continues and emphasizes the present condition; it does not enlarge the absolute control of any limited number of men in charge of the Federal Reserve System or the business life of this country?

Mr. HEMPHILL. Yes, sir.

The CHAIRMAN. As I understand you, the thing you advocate is to set up a similar body with similar powers and similar authority and similar possibilities?

Mr. HEMPHILL. No, sir. We propose to set up a body which will operate strictly within the lines prescribed by this Congress, who will be nothing but office boys, nothing but clerks, with nothing to do except to carry out the specific provisions in the law.

The CHAIRMAN. Are you sure that your statement is entirely accurate, in the light of the program which you have just read or the resolutions which you have just read to the committee?

If I caught the reading of those resolutions, you would have a monetary authority with the power, and whose duty it would be, to establish a satisfactory price level. Could that be accomplished automatically?

Mr. HEMPHILL. Yes, sir.

The CHAIRMAN. Who would determine whether it was satisfactory?

Mr. HEMPHILL. I think Congress should determine that—put it in the law.

The CHAIRMAN. You do not say that Congress shall determine what the satisfactory price level shall be. You provide that Congress shall set up a body who shall conduct their operations and exercise their powers to the end that they may establish a satisfactory price level which, of course, would be determined by them, would it not?

Mr. HEMPHILL. I am glad you mentioned that point, because I want to make that very clear. Our proposal as I have read it here is merely a statement of objectives in general terms—you understand it is not in any way a bill.

The CHAIRMAN. I understand that you have not put it in the form of a bill, but to the extent I have pointed out you have been specific.

Mr. GOLDSBOROUGH. May I interrupt for a moment? If you will remember, in the monetary authority bill considered in the last Congress by a subcommittee of this committee the powers of Congress were not delegated except insofar as delegating to the authority as experts the power to carry out the specific mandate contained in the bill.

Mr. HEMPHILL. Exactly. Let me read this recommendation again.

The CHAIRMAN. Mr. Goldsborough is quite correct in what he says about the bill he introduced last year, which was considered in this committee. But you are not following that bill in toto. You leave to that Board the exercise of discretion which would be used to bring about a satisfactory price level and restore employment. But they would be the judges of whether or not that had been accomplished.

Mr. HEMPHILL. Not necessarily. Let me make myself very clear. This recommendation provides: Create a politically independent Federal Monetary Authority which would exercise, under definite congressional mandates, the constitutional monetary powers of Congress.

The CHAIRMAN. Let me make myself clear. I think that is all desirable and that it is a good mandate, insofar as you may give one in generalities; that is the thing that is desired.

But that leads me to this inquiry. I have never been able to see the difference in any machinery that might be set up under the new suggestion of a monetary authority and the authority that we establish or preserve under the bill now before us. And, just as you said a few minutes ago, I think it is quite true that, after all, the selection of the personnel constituting the controlling body to exercise this authority, whether it is done under the provisions of the present bill or under any other legislation, would, after all, drift into the usual processes under which the selection of personnel for boards of that kind goes on today and has gone on for years.

In other words, I do not see how, under either plan, we get away from this weakness of control by fallible human beings.

Mr. HEMPHILL. I think there is very much in what you say, although that is not the picture we have in mind. We do not propose to leave this monetary authority any discretion at all in that direction. In fact, I will be willing to tell you how much money you must have per capita in order to accomplish the results sought, and this specific figure could be a mandate objective.

The CHAIRMAN. If you did that, then what do you have for Congress to determine for itself, insofar as it can be determined?

Mr. HEMPHILL. Let us put the figures in the bill. We have enough knowledge today to determine the amount of money per capita that we need. If you will consult the available records, this committee can determine the amount.

Mr. HOLLISTER. How much would you need?

Mr. HEMPHILL. About $250, to restore our highest former standard of living and property values. Two hundred and fifty dollars per capita in circulation will create an annual per capita income of $750. You can set the mark anywhere you want to for the average per capita annual income, and take a third of that figure and you have the amount of money or substitute medium of exchange which must be in circulation.

The CHAIRMAN. I will say to you frankly, that so far as I am concerned, if somebody will show me a plan how Congress may do this job and accomplish the results you have in mind, which all of us would like to accomplish——

Mr. REILLY. It is results that we would like to have.

The CHAIRMAN. Yes. If somebody will show me how that can be done by Congress and take the matter out of the control of human beings, I would like to do it. We are all subject to the limitations of judgment and other weaknesses, but I would like to do something like that. But I confess I do not know how to do it, and I am not sure that anybody else does.

Mr. HEMPHILL. Let me say this, that it was not the intention, in making these recommendations, to present in detail the bill you refer to. I will say this, and I believe that the economists who are here and who have made a life study of this subject will agree with me, that it is possible to do it, within small limits which would not be important, to have Congress fix the total amount of money necessary to be put into operation and circulation to produce a certain definite standard of living in terms of money per capita income. I think that is possible to do, if that would be considered by this Congress, and that is what we are going to propose.

I had in mind, in connection with this proposed amendment here, a specific provision which was in Senator Cutting's bill last year, which was introduced in the Senate, and I believe was introduced in the House by Mr. Patman. Those bills contained a provision for issuing currency or credit to the total amount of $250 per capita.

Mr. SISSON. Mr. Hemphill, if I understood you correctly, you said, in substance, that if what you advocate, if your prescription were followed by Congress, namely, that if the country had an adequate monetary system, an adequate supply of money, the United States would rule the world. Am I quoting you correctly?

Mr. HEMPHILL. Yes, sir; eventually.

Mr. SISSON. When you said the United States would rule the world, in what respect did you mean that, in trade?

Mr. HEMPHILL. In trade and commerce; yes, sir.

Mr. SISSON. Then would you advocate that the United States try to increase its foreign trade, as a policy, or would you have it try to isolate itself further from the world of trade in the future than it has in the past?

Mr. HEMPHILL. I think, as the result of what we advocate, our foreign trade will take care of itself. Foreign trade consists of manufacturing goods that the people in other countries want and that they can afford to buy.

Mr. SISSON. You cannot sell to the rest of the world indefinitely, in increasing quantities, unless we buy from them.

Mr. HEMPHILL. England did it for 100 years.

Mr. SISSON. I understand that is what Mr. Hearst is advocating.

Mr. HEMPHILL. Listen, I do not represent Mr. Hearst here. I want that distinctly understood. I do not know that Mr. Hearst agrees with the detail of what I am advocating. Early in this administration Mr. Hearst advocated replacing the bank credit withdrawn from circulation by issuing bonds or currency. That is precisely what we are advocating. I don't think Mr. Hearst is interested in technical methods of how this objective is accomplished.

Mr. REILLY. The matter of this banking system, in your mind, is a very simple question?

Mr. HEMPHILL. Yes, sir.

Mr. REILLY. Do you not think it would be possible for Mr. Eccles to create a committee of equal size as the committee proposed, of distinguished students of finance in this country, bankers and college professors, who would put thumbs down on your bill?

Mr. HEMPHILL. Yes; I think there are a great many very accomplished and competent students who are not free to express their opinion.

Mr. REILLY. Has there not always been a radical difference of opinion among men who think they know something about banking as to what is or is not a good banking system?

Mr. HEMPHILL. There has been no difference of opinion among the men who actually know this subject. There are a great many whose opinions are colored by some necessity, and a great many economists who have given monetary subjects only the most superficial study.

Mr. REILLY. You assume that the members of the committee who approved these suggestions know all about the system?

Mr. HEMPHILL. Yes. Most legislation, as you know, is a compromise of conflicting opinions. I do not mind saying this, and I think everybody knows it, that the United States Treasury has always been in control of a group of very few banks.

Mr. REILLY. That may be true.

Mr. HEMPHILL. And as a consequence, the financial legislation which has been effected in the United States is the result of the cumulative intelligence of a succession of bankers who have controlled this Congress of the United States so far as financial legislation is concerned. The people have never had a chance at it, and have never even been represented.

Mr. FORD. If I have correctly understood your original statement, you say that we should have a dollar in actual money in circulation for every dollar's worth of goods in existence now and what will be produced in the future—an actual dollar?

Mr. HEMPHILL. We have got to have a dollar for all goods in process of transfer that are finished and ready for transfer. There has to be money enough to buy those goods—that is self-evident—or else they have to go on the shelves.

Mr. FORD. Does not the present Federal Reserve System provide for that in this way? Say, for instance, I am a manufacturer and I need $100,000 with which to buy my raw material and pay my labor during the process of manufacturing the goods and delivering them to the men who have to purchase them.

I go to a bank and borrow $100,000, and after the purchasers have taken the goods and moved them off of their shelves they return to me the money I charge them at the manufacturer's price, and I in turn pay my note in the bank. In the interim, there has been $100,000 issued to take care of that transaction in its various stages. When my note is paid that money goes out of existence. Under your plan that money would remain in existence?

Mr. HEMPHILL. The point is if you are to pay your loan somebody else has to borrow $100,000 to take the goods off your hands. You create $100,000 worth of goods that never existed before, and the money to buy them does not exist. The money that exists now is all in use in the exchange of other goods. You have to have new money and you have to continue to borrow to continue to create.

If you create $100,000 worth of new goods to be transferred, you must at the same time create the purchasing power. If, instead of paying your loan, this money is permanently introduced into the system you have furnished society with the necessary new purchasing power to consume the newly created goods.

Mr. FORD. If that money remains in existence, according to your theory, other people would not have to borrow?

Mr. HEMPHILL. No.

Mr. FORD. Then you want a matched dollar; you want a dollar in existence, in actual money, for every dollar's worth of goods and services that are transferred in exchange, in the course of business?

Mr. HEMPHILL. Let me turn the proposition around. Let us look at it from the other angle.

You cannot exchange any more goods, regardless of what your creative capacity is, until there is money ready to pay you for the goods. That is the same thing from another angle.

Mr. FORD. Then there is a difference in opinion between your school and the present school. One school creates the money during the period when it is necessary in order to take care of the transaction, and then upon completion of the transaction the money goes out of existence.

The other school would have that money remain in existence so that for every building, for every railroad train, and for every transaction of any character or kind, and for every kind of goods purchased, there would be a dollar still in existence some place in the United States.

Mr. HEMPHILL. Only sufficient to buy goods and services.

Mr. FORD. Then we would be affecting our national production of wealth.

Mr. HEMPHILL. This has not anything to do with wealth.

Mr. FORD. This confines it to monetary circulation and actual goods in process of production?

Mr. HEMPHILL. Absolutely.

Mr. FORD. When they are consumed, there would still be that money in existence?

Mr. HEMPHILL. You have to have some more goods. Our production and consumption are continuous processes.

Mr. FORD. But those goods go out of existence. It seems to me you do the same thing in the other way.

Mr. HEMPHILL. It is doing the same thing, creating money, but I call your attention to the fact that at certain recurrent periods under our present system this synthetic money, bank-credit money, disappears from circulation and is not reproduced. That is what we are suffering from now. You cannot borrow the $100,000 that you are talking about from any bank today. I will show you on my desk application after application of men who have sound industries, and who could have borrowed at any time previously $100,000 or more and who have asked me to help them. I have been trying to get money for some of them from the R. F. C. and from the Federal Reserve System, for men who could have borrowed many times the amount they require, whose notes would have been instantly rediscounted at any Federal Reserve bank.

Mr. FORD. But if that money had been in existence, and it was still in the hands of some people who did not feel that they wanted to loan it, you could not get it.

Mr. HEMPHILL. I understand that.

Mr. FORD. Then the presence of the money in existence makes no difference?

Mr. HEMPHILL. You are assuming a situation which does not normally exist.

Mr. FORD. If the banks had all this money in their vaults instead of credit, in their present mood of refusing to loan, they would not loan.

Mr. HEMPHILL. Why would they have that mood? They have now the depression mood. They are afraid to loan. I agree with the banker. I agree with him if he cannot make a loan safely he should not make it. He is very properly unwilling to loan and thereby weaken his relative reserve. In 1916 when we were considering the question of the amount of reserves of banks, I fought to have the bank reserves increased instead of diminished and a great many conservative bankers felt the same way. I thought reserves should be progressively increased until every bank could pay any part of its checking accounts—demand deposits—at any time. Until this was done I considered banking a gamble with the public always loser.

Mr. FORD. We are arguing about different things, I think. I am arguing whether it is necessary to have a dollar in actual money in existence for every dollar's worth of goods produced, or in the process of production, and have the money available all the time, or whether it is just as feasible to have that money created through a transaction such as I have described.

Mr. HEMPHILL. It would be perfectly feasible if our banking system functioned all the time only for sound loans. If they were on a sound basis so they have no recurring necessity to refuse what you have here pictured in your mind, I would be for the banking system.

Mr. FORD. You are trying to make that situation impossible. But here we say, instead of restricting the character of the security that the bank can use at the Federal Reserve bank to get money, we are saying all sound assets. That is asset money. If you are lucky and have $1,000 you put it in the bank, and when you put it in there it is money.

Then the bank turns that into an asset and it loans to somebody and then the security it takes becomes an asset of the bank. If that bank can then take that asset to some source and turn it back into money in an emergency, the currency it secures is asset money, and with the plan you are suggesting you would have everything in this bill.

Mr. HEMPHILL. But you do not guarantee it in this bill.

Mr. FORD. Yes, we do.

Mr. HEMPHILL. No, you do not. It is discretionary with the Federal Reserve Board.

Mr. FORD. It is guaranteeable.

Mr. HEMPHILL. I agree that it is guaranteeable and am asking you to guarantee it by adding some amendments which is in effect precisely a guaranty. You say that three or four men here are going to have the right to do these things if they want, but if they do not want to they will not do it. What we advocate is that this Congress compel their action.

Mr. FORD. But we are going to say, to some extent, what a sound asset is.

Mr. HEMPHILL. They are going to say whether your banks can loan on it or not.

Mr. FORD. You cannot pass any law forcing a bank or anybody else to loan money if they do not want to.

Mr. HEMPHILL. Certainly not. That is precisely the difficulty with this Nation. We have to borrow all the money we have in circulation. If the banker is optimistic we are prosperous; if pessimistic, we starve.

Mr. FORD. We are creating facilities in this bill to cope with any emergency that comes along, and if we had had it in 1929 the present situation would not be so bad.

The Federal Reserve Act, as stated today, was probably the most ideal vehicle ever created to handle business in banks, but they left out one thing; they did not make facilities under the bill capable of taking care of a depression, which is the thing we are trying to do, which is calculated exactly to cure that condition.

Mr. HEMPHILL. I agree with you to the extent that the Federal Reserve Act was an ideal vehicle to expand the possibilities and extend the life of a banking system which showed unmistakable signs of approaching collapse because of its inherent defects, and the fact that it has preserved this fundamentally unsound mechanism for more than 15 years is sufficient tribute to its potency.

I think, however, that if we had been operating in 1929 under the bill you are considering, with the same Federal Reserve Board we had then, some of our $10 stocks would have sold for $5,000 per share instead of the $500 they did sell at. Some of our skyscrapers and big hotels would have been mortgaged for five or six times their cost of reproduction instead of the two or three times they were. The crash of 1929 would have brought on an immediate and permanent bank holiday instead of the temporary suspension of 1933 and the frozen situation which has since continued, and we would likely have had a communistic government instead of the socialistic dictatorship we now have. Did you ever run a bank?

Mr. FORD. I worked in a bank; yes.

Mr. HEMPHILL. A country bank?

Mr. FORD. Yes.

Mr. HEMPHILL. You must agree then that this bill introduces nothing new in the banking system except to enlarge its scope and to admit a wider latitude in discount and rediscount.

Mr. FORD. It gives a reverse action that you did not have before.

Mr. HEMPHILL. It gives a broadened action, similar to the action that the creation of the Federal Reserve Bank System gave. The Federal Reserve System simply expanded our then credit system.

Mr. FORD. It has terminal facilities both ways.

Mr. HEMPHILL. I know that. It creates a central body which has important discretionary power. I will say this to you—this bill, if you have the right men and can guarantee to the people of America that you are going to have the right men all the time, men of great understanding and courage who will not be influenced by politics or the selfish interests of anyone—this bill will do the trick, but it should have discretionary mandates.

Mr. FORD. And if we also have the right President and Government and Congress, you would not have any need of this bill.

Mr. HEMPHILL. The President and Congress do not operate our banking system. We could have the best President and Congress possible, and still have all our present distress. You have here a measure which preserves and enlarges a situation which is essentially unsound.

Mr. FORD. I disagree with you. How do you cure it by legislation? All progress is a thing that is just as the Governor said the other day, a matter of evolution, and in order to cure the evils of our banking system we must do it not by revolutionary processes but evolutionary processes, and we are intelligently trying in this particular measure to bring about a situation in the United States that is in my judgment the only possible way we can function under the capitalistic system, unless you want to go to some other system. As long as we are in this capitalistic system, 75 percent of the people seem to desire it to be preserved, we have to create facilities or machinery within that system that will give us the very best results obtainable thereunder. I think that this measure, I am not assuming all knowledge, will help inmeasurably. I am just one individual who has made a study of this bill and compared it with what other bills have done.

I have tried to apply such experience as I have had to it. I was 35 years in the same game you are in, the newspaper game—I think this bill will give us results that everyone is hoping for. That is my view of it.

Mr. HEMPHILL. I have already stated my opinion of this bill, and I am not disposed to argue with you. The capitalistic system is not involved in this question. You spoke of me as a newspaper man. I know nothing about publishing. I have been a financial writer for only 2 or 3 years. I have been in active business almost all my life. I have in the past owned and operated railroads; I organized the Mississippi Power & Light Co. I have operated harbors, operated a great many industrial enterprises, have been in banking and finance since I began to vote, and I was credit manager of the Federal Reserve Bank of Atlanta, because some of my good friends perhaps mistakenly presumed that I knew something about the practical side of money and banking, as well as monetary science.

Mr. BROWN of Michigan. Did you agree with them or not?

Mr. HEMPHILL. Yes; I did. There is nothing difficult about the subject. Let me say this about this bill: In my opinion, whatever faults or whatever virtues you have had previously in the banking system, this bill exaggerates them. I do not think it cures anything. I think that you do nothing in this bill which is curative or constructive. The only thing you do is to create a central body here which will exercise some control which has not before been had. I think that is true. I will say this, and it is the reason I asked you if you were a country banker: I have been a country banker, and when things are going good there is nobody under this bill who will or can stop a country banker from going out on a limb; no device that we have ever found except a law which defines the limit of his loans; and some of the big city banks are just as bad.

Mr. FORD. I realize that.

Mr. HEMPHILL. That is what creates the trouble with our banks all over the country. In 1929 some of the banks of New York who ought to know better would lend on anything you could bring in the front door. Today they will lend almost nothing. That is the essence of our trouble. The oscillating psychology of the banker. I am with their present views. Do not think I am criticizing the banker, because, as I said a while ago, nobody but a gambler would run a bank according to our present laws. There is no business man who would run a bank on a basis of 10-percent reserve. It is a straight gamble. It is not a business. What we propose here is to convert it into a sound business.

Mr. FORD. Do they not have a pretty substantial kitty?

Mr. HEMPHILL. You see what happens to them. We have lost 15,000 of them in the last 20 years and almost wrecked this Nation. In fact, we are not yet out of the political woods by a " long " shot.

Mr. REILLY. Have not thousands of banks gone on doing banking that are absolutely sound?

Mr. HEMPHILL. But they busted everybody else doing it.

Mr. REILLY. No.

Mr. HEMPHILL. Have you forgotten the drastic foreclosures in 1929, and 1930, and 1931, and 1932, that forced thousands of our finest creative and constructive men into bankruptcy and some of them into insane asylums and suicide? You cannot have forgotten that mad period of ruthless destruction; it was the most drastic period of contraction ever forced on any country.

Mr. REILLY. Mortgage companies, stock exchanges, and other things have brought about that.

Mr. HEMPHILL. I understand. But I am discussing this one feature. There is nothing right about our banking system. It is a rotten, unsound system. You all know this as well as I do. We can have a better one. If you are all going to be tied, if you are bound, indebted to some interests here so that you cannot use your independent judgment, you will not do anything constructive. This bill is not anything. It is not even an advance. It opens the whole banking system wide open, and we will have as an absolute certainty—no question about it—we will have another period of inflation which will be a wilder thing than we have ever had, and a worse collapse, and I want to tell you gentlemen that our democracy will not survive it.

Mr. SPENCE. You stated that the money per capita should be $250.

Mr. HEMPHILL. Yes.

Mr. SPENCE. What do you mean by that? What do you mean by $250—in money or cash?

Mr. HEMPHILL. In bank deposits. Something that you can transfer, any kind of money; we can use soap wrappers.

Mr. SPENCE. That is more money than we have ever had.

Mr. HEMPHILL. No; it is about what we had in 1928–29. It is a little more in total because we have more people; but it is not substantially more per capita.

Mr. SPENCE. In 1926 there were $24,000,000,000 in banks.

Mr. HEMPHILL. In bank deposits, yes; but in money of all kinds there was $27,000,000,000, about $230 per capita.

The CHAIRMAN. That was not entirely in demand deposits.

Mr. HEMPHILL. In demand deposits, and cash, outside of banks, $27,000,000,000.

Mr. CAVICCHIA. I would like to know if this $250 per capita is based or has any relation to the time deposits in the bank.

Mr. HEMPHILL. No. Time deposits are not in circulation. Time deposits are just investments like bonds or United States Steel stock; you do not draw checks on them or use them as money.

Mr. CAVICCHIA. You do not have deposits in there when you make up that figure of $250 per capita?

Mr. HEMPHILL. Yes; demand bank deposits and cash.

Mr. CAVICCHIA. You did not have that relation in mind, then?

Mr. HEMPHILL. Yes. Twenty-seven billion dollars in demand deposits and cash is about what we had in 1928–29. Now we have more people, which would make it necessary to have about $32,000,000,000.

Mr. SPENCE. Do you think business conditions govern the amount of bank deposits?

Mr. HEMPHILL. No; I know about that. It is the banker who says "Yes" or "No." I could talk all afternoon about that. Business psychology does not change. Business conditions change because we vary the volume of synthetic money. We try to create just as much business tomorrow as today. We do not shift our ideas about business. The business man will attempt to transact business with a persistence second only to the persistence with which he tries to preserve his life, all the time. There is no such thing as business scares. It is only expanding and withdrawing credit that creates the fluctuation in business. That is true.

The business man does not even know whether expansion or contraction is coming. We try harder to buy and sell in depression than any other time but we have insufficient money in circulation. It is a mysterious thing to the business man. His business begins falling off and he doubles his efforts to again expand it. He does not know that money is going out of circulation because the banker has overexpanded and is getting cold feet.

Mr. CROSS. We have learned from the night schools that the question of velocity and backbone money was to be figured in considering the amount of money in circulation.

Mr. HEMPHILL. Velocity.

Mr. CROSS. In other words, that when they have many advantages, this backbone money and pocket money continues to circulate with the same velocity all the time.

Mr. HEMPHILL. Yes.

Mr. CROSS. What do you think about the velocity of money cutting any figure?

Mr. HEMPHILL. I do not think there is any great difference in the velocity of money in good times or bad. Everyone does not agree with me but everybody agrees when we get the same figures before us. I will show you gentlemen something in the Literary Digest, a graph in the back of the book which shows, among other things, the checks charged to individual accounts in all banks outside of New York City and the carloadings. Those are the two lines right there. That one is the checks charged to individual accounts outside of New York City which more or less eliminates the major part of our checks employed in speculation. These carloadings represent the goods we are shipping to each other and those checks are what we are paying for them.

I think these are the two most important indices of what is going on in this country that can be constructed, because the minute we trade more it means that we ship more goods immediately. We have to do this, and we pay more money for them, so a graph showing those checks outside of New York City and those carloadings, I consider, if properly constructed, gives a perfect picture of what is going on in the United States, and you will notice that they have not changed substantially since June 1933; the graph shows clearly that there is no substantial increase or decrease.

Mr. CAVICCHIA. Carloadings and checks.

Mr. HEMPHILL. Yes; all checks charged to individual accounts outside of New York City. You cannot laugh those figures off. There it is, the picture of what we are actually doing.

Mr. CAVICCHIA. I take it that you would not have the country put on a gold basis as far as the monetary system is concerned?

Mr. HEMPHILL. What difference does it make? We have now behind our money, our fiat money, all the wealth of the Nation—all the gold and silver, and diamonds and everything else we own. Why tie it to gold alone? If you limit our money on a gold basis you are restricting it to a very small part of our wealth. I believe in the gold standard for international payments if anyone wants it at the value of the gold today—on the date of payment. And if you want to make payment with gold, all right, give it to our foreign cousins—that is the way I feel about it—at whatever the price is, $30 or $40 per ounce, that is all right. He understands gold and what is the use of arguing with him; we have the gold—avoid argument.

Mr. Cavicchia. The issuing of 25 or 26 billions of currency—would that in any way restrict the banks from lending; lending money on mortgages?

Mr. Hemphill. The banks would have more to loan and could give longer credits. You gentlemen know what the present credit condition is.

Mr. Reilly. Credits?

Mr. Hemphill. Yes.

Mr. Reilly. What would this new money be issued against?

Mr. Hemphill. The wealth of the United States, which at the peak was $480,000,000,000.

Mr. Reilly. That is purely an inflationary measure?

Mr. Hemphill. No; these proposed amendments are initially deflationary, tremendously so, and if it were not for the fact that we have included provision for a monetary authority, operating under a definite mandate to restore the currency, it would be drastically deflationary as these amendments eliminate our present imaginary money and replace it with a permanent currency, controlled by Congress.

Mr. Reilly. It is your idea to use money based on the credit of the United States to take up the present indebtedness?

Mr. Hemphill. Bonds; yes. What is the difference?

Mr. Reilly. Not $28,000,000,000.

Mr. Hemphill. Yes. What is the difference between bonds and money? They are identical obligations of the Nation. One states on its face that it is legal tender, the other does not.

Mr. Reilly. Do you believe that if we adopted these amendments this movement would pull us out of the depression?

Mr. Hemphill. Yes; we reversed a disastrous depression in 1929 in 6 months. We did it by credit expansion, what we are asking you to do today, and stopped a depression as bad as this one.

Mr. Reilly. Would you use the $4,800,000,000 work-relief measure in financing our recovery; what would you suggest about that?

Mr. Hemphill. Throw it out the window.

Mr. Brown of Michigan. You do not favor the Government spending for the purpose of increasing employment at the present time.

Mr. Hemphill. No; I do not.

Mr. Brown of Michigan. What would you do during the interim it would take to put your system into effect with millions of men unemployed?

Mr. Hemphill. Do just what we have been doing since 1929. We have to support our unemployed. That question is not open to argument.

Mr. Brown of Michigan. I have read for a good many years the Hearst newspapers for which I understand you are working and they have advocated, although they have not stressed it very much in the past few months a 5 billion dollars public-works program.

Mr. HEMPHILL. I do not know.

Mr. BROWN of Michigan. You must know that.

Mr. HEMPHILL. I do no tknow that.

Mr. BROWN of Michigan. You know as a matter of fact they have for many years adocated that to get us out of the depression.

Mr. HEMPHILL. I think Mr. Hearst, whom I have a very great respect for, takes about the same position on this general subject as I do.

Mr. BROWN of Michigan. You know that he advocated a 5-billion-dollar public-works spending program?

Mr. HEMPHILL. I do not know that. Mr. Hearst has long advocated that the Government have constantly on hand uncompleted desirable projects all ready to go into action and the necessary authority and appropriations complete, so that they could be put into action whenever general business showed signs of slowing up. That is a far different picture from the hasty and wasteful and doubtful emergency program now being considered. Mr. Hearst's idea is to prevent unemployment—prevent emergencies by a sane, well-considered, thoroughly digested, and prepared program. As he recently wrote me—provide knee action for our economic machine, to compensate minor bumps. I will say this. Most of the things Mr. Hearst has advocated in the past have been adopted 10 years later, as I have no doubt this suggestion will be. However, I want to repeat that here, I am not representing Mr. Hearst and have no authority to speak for him. He may have some respect for my views on money and banking because of my long experience. He has given profound study to many questions of great importance and on these questions I think he is the soundest philosopher of our times. I do not know that he has recently advocated a 5-billion-dollar spending program.

Mr. BROWN of Michigan. I will supply that knowledge to you. I know that he has. How would you take care of the people of the country at the present time? You say that we should take care of them as we have in the past. The only way we can do it is through a spending program.

Mr. HEMPHILL. No; the emergency spending program is new. We have heretofore been paying for relief, certain definite relief.

Mr. BROWN of Michigan. Would you confine Government activities to straight relief?

Mr. HEMPHILL. Yes.

Mr. BROWN of Michigan. Instead of a public works program?

Mr. HEMPHILL. Yes.

Mr. BROWN of Michigan. In other words, you thing it would be better to give them the money rather than enable them to work for the money.

Mr. HEMPHILL. I do not think that question would be a question more than 6 months. This depression is a monetary phenomenon; that is all. I think almost everyone knows just what our trouble is. Why do not you gentlemen get to the guts of this thing and cure the thing that is wrong? It is a monetary phenomenon. The contraction of our synthetic money—bank credit. That is all that has ever been the matter with us—the direct cause of every depression.

All these other things are simply the visible evidences of the maladjustment caused by taking $8,000,000,000 out of circulation.

Everybody in the world knows this except us.

Now, gentlemen, I want to summarize our situation and the reforms advocated.

I want to define this proposal so clearly that you cannot pass the buck.

I want in all kindness and consideration to put you in a corner from which there is no escape.

You have here a simple and certain method by which you may end this depression, by which you may recover your constitutional right to issue and control the money of this Nation; by which you may restore prosperity to your stricken constituents; by which you may confer on the people the independence which an omnipotent Creator intended all men should have and which the patriots who founded this Nation believed they were securing for their posterity.

There is no theory whatever involved in this proposal.

You have all the facts before you. The authentic data which you may verify from our public records, if you have not already done so.

You know now that the national income is invariably three times the individual demand deposits in our commercial banks.

[In billions of dollars]

	Demand deposits	National income	Ratio		Demand deposits	National income	Ratio
1929	24.3	81	3.3	1932	16.4	48.9	3
1930	24	75.4	3.1	1933	15.2	46.8	3
1931	21.3	63.3	3	1934	[1] 17.6	52.8	3

[1] Estimated.

No 2 years in a century could subject this rule to a severer test than 1929 and 1932. The peak of the wildest inflation and the bottom of the most severe depression this Nation has ever known. The variation is only 10 percent.

This ratio has been established beyond question in this country, in England, and in France, as far back as reliable records are obtainable.

You know that to restore the income of our predepression days you must put into circulation additional money until you have expanded individual demand deposits to one-third of that predepression national income.

That means that to have an average annual per capita income of $750 there must be in circulation in individual demand deposits in our commercial banks $250 per capita, approximately $32,000,000,000.

To accomplish and control this result you must eliminate from the private banks the power to expand or contract the money Congress puts in circulation.

That is a very simple matter.

The banks now hold cash and Government bonds equal to their individual demand deposits, but they have the potential capacity to inflate or deflate their demand deposits and nullify and destroy any program you devise.

You know that Congress can never control the volume of money in circulation and therefor its value as long as private banks retain this power.

We propose to you that you require that hereafter all banks maintain their demand deposits in cash or Government bonds.

They can then no longer inflate or deflate. They are profitable on their present basis and will share hereafter with everyone in the general prosperity, but Congress alone will hereafter have the power to increase or decrease our medium of exchange—to create prosperity or depression.

The welfare of the Nation will then be in your hands.

We propose that you then command the Federal Reserve Board to buy from individuals and corporations, as rapidly as possible, the 15 billions of United States bonds they hold, putting into circulation that amount of new money which will go immediately into action.

(If it is considered desirable to encourage the banks to increase their demand deposits by purchase of bonds, there is no objection, provided that they are not permitted later to sell, except to the United States Treasury.)

Each billion increase in demand deposits will increase the national income $3,000,000,000.

There is no doubt of this whatever. It is a demonstrated fact. It is no one's theory.

You have it in your power to do this.

If you do this you will confer upon the Nation the priceless gift of liberty and continued prosperity. If you fail, you have failed miserably and ignominiously in your duty to the Nation.

The Constitution endowed you with the power to issue the money of this Nation, and by that act prohibited all others from exercising such a power.

It is a sacred trust because it controls the welfare of each individual.

Your predecessors have signally failed or have been influenced or intimidated into neglecting to exercise this power, and have permitted private selfish interests unlawfully to exercise this function for their private profit, and by this monopoly to have an unholy power over the people of this Nation, through which they have exploited them, have in effect made them a subject people, reduced them to economic slavery.

Your predecessors may plead ignorance. They may plead that too little was known of monetary science, that no clear definite plan was available, that the data upon which such a plan might be determined was not available.

You cannot plead such ignorance.

This committee, which has studied monetary matters for so long, is now well informed.

There is no confusion in your minds.

You know that you do not now issue and control the money of this Nation, as the Constitution empowered and directed you to do.

You know that private interests have seized and created for themselves and their favored circle, a monopoly of this vital public function; that today they are more powerful than this Government.

You know that they control the economic welfare of this Nation, and that Congress is powerless.

That they maintain their sinister control of this public function and of this Nation by subterfuge and intrigue and intimidation.

You know that to a large extent the private banks of this Nation are little more than private rackets.

That only to a limited extent do they serve the public welfare.

That in the majority of instances they are operated to promote the interests of a small group which has an unfair advantage over the remainder of the community.

That through their power to create a synthetic money at their pleasure the "inside groups" in financial circles can and do constantly buy the results of the genius and labor of their fellows at bankrupt prices.

You know that the banking system is controlled by the policies of a few big speculative banks, principally located in Wall Street, who dominate the whole system and the banking organizations.

You know that the men who have of late years come largely into control of these speculative banks are parasites. That they control our great securities and commodities markets and the machinery of foreign exchange.

That by manipulating the powerful machine they operate they obtain an unfair and unearned share of the wealth created by our commerce and industry to which they contribute nothing.

You cannot plead ignorance of these facts.

You know all about them, and millions of your constituents know all about them, and know that you know all about them, and know where your duty lies in this crucial situation.

The question before you, gentlemen, is fundamental.

Are your constituents and posterity of more moment to you than the small group of parasites who own and manipulate this synthetic substitute which we are forced to use for money because of the failure of Congress to exercise its constitutional function, to issue and control the money of this Nation?

That is the fundamental question here involved.

You cannot escape a clear position in this matter.

Are you going to do your duty, or are you going to decline to do it? That is the question.

Are you going to recapture your constitutional perogative to control the money of this Nation, and control its material welfare, or are you going to permit a private monopoly to continue to exploit you and your fellow citizens, and to constantly concentrate in the hands of this small group the wealth created by the whole Nation?

That is the question now before you gentlemen. You cannot dodge it. You cannot plead ignorance.

We are not suggesting that you recapture the wealth these parasites have obtained by fraud, through this unholy power which the negligence of your predecessors has conferred upon them.

We will leave that to the fact that these men, divested of their unfair advantage, will be unable to compete with constructive minds and their unearned wealth will soon be dissipated to the real creators of the wealth of this Nation. They are largely the accidents of financial politics. Many of them are not fitted by birth, breeding, race, intelligence, culture, or any other characteristic to occupy positions of leadership or control.

Divested of their unholy power over their fellows they are largely an ineffectual class without constructive resource and with little to contribute to society.

We are asking you to end this period of wildcat credit manufacture by private interests. This bonanza banking period through the machinery of which a few greedy predatory men have been able to maintain a stranglehold on this Nation and its Government.

Who are you for?

Are you for the people of this Nation or for the small group of international bankers who dominate and manipulate and exploit the commercial banking system of this Nation and through it dominate and exploit the Nation?

That is the question you must answer your own consciences, your constituents, your children, and posterity. The following amendments to H. R. 5357 are recommended:

1. After 1 year after the passage of this act, all individuals, firms, associations, or corporations in the United States or Territories or possessions thereof, engaged in the business of banking as defined by law, and among other things receiving deposits of money or any substitute medium of exchange, withdrawable or payable upon the check or equivalent order of the depositor, upon demand or within 30 days shall be required to hold said deposits in trust for said depositors in lawful money of the United States, on hand, or on deposit in the Federal Reserve bank of its district, or with the Treasurer of the United States: *Provided, however*, That said bank may at its own risk keep no more than 95 percent of said deposits invested in interest-bearing bonds or notes of the United States Government, and the interest on said bonds or notes may be received and retained by said bank for its own use and benefit: *Provided further*, That any of said bonds or notes of the United States shall be eligible for discount at any Federal Reserve bank at the par value thereof and at the interest rate borne by said bonds or notes, and after the date on which this act becomes effective the Federal Reserve banks shall discount for any bank in its district any of such bonds or notes upon application and shall discount no other obligations, all laws or parts of laws in conflict with this provision being hereby repealed.

2. After the passage of this act, the Treasury of the United States may receive and hold for safe-keeping and credit any funds in lawful money or bonds or notes of the United States deposited with it for the account of any Federal Reserve bank and shall deliver such funds so deposited to the said depositor upon demand; or upon duly authenticated order of such depositor shall transfer the title to such funds to such other Federal Reserve bank as such order may direct. Duly authenticated credit upon the books of account of the Treasury of the United States shall be legal reserve for any bank, banking firm, or banking corporation in the United States or its Territories or possessions, and the Treasurer of the United States shall, upon demand, issue and deliver to any depositor, non-interest-bearing Treasury certificates against such credit in denominations of 1, 5, 10, 20, 50, 100, 1,000, 10,000, 100,000, or 1 million dollars, or such other denominations as the Federal Reserve Board may from time to time direct, and all such Treasury certificates so issued shall be legal tender for all public and private debts, and may be redeemed by the Treasurer of the United States upon demand in bullion, gold or silver, at the option of the Federal Reserve Board upon such prices, terms, and conditions as the Federal Reserve Board may direct.

3. The Federal Reserve Board is hereby directed to use all its powers and facilities to increase the circulating medium of exchange of the country until there shall be in individual demand deposits in the commercial banks of the Nation the sum of $250 per capita, in accordance with an estimate of the population as of the date of the passage of this act, to be furnished by the Census Bureau, and the Federal Reserve Board is further directed to use all its powers and facilities to maintain the said sum of $250 per capita in circulation in individual demand deposits in the commercial banks of the Nation until and unless this mandate is hereafter modified by further act of Congress.

STATEMENT OF D. J. NEEDHAM, GENERAL COUNSEL AMERICAN BANKERS ASSOCIATION

The CHAIRMAN. Mr. Needham, representing the American Bankers Association, is here and has a statement for the committee that he desires to read. I did not think we should interrupt Mr. Hemphill this morning, but since it was understood we would go forward with Dr. Fisher this afternoon, I am wondering if you might insert your statement in the record, Mr. Needham, and that will give every member a copy.

Mr. NEEDHAM. I will be glad to file the statement and see that each member gets a copy.

(The statement referred to is as follows:)

RECOMMENDATIONS OF SPECIAL COMMITTEE OF THE AMERICAN BANKERS ASSOCIATION ON THE PROPOSED BANKING ACT OF 1935

WASHINGTON, D. C., *March 22, 1935.*

Hon. HENRY B. STEAGALL,
Chairman Committee on Banking and Currency,
House of Representatives, Washington, D. C.

DEAR MR. STEAGALL: The American Bankers Association, through its accredited committees, has given careful consideration and thought to the provisions of titles I, II, and III of the proposed Banking Act of 1935 (S. 1715 and H. R. 5357).

At a joint meeting of the administrative committee and the executive committee of the committee on banking studies, held earlier this month, resolutions were unanimously adopted authorizing the following official statement on behalf of the association:

"The administrative committee and the executive committee on banking studies of the American Bankers Association, in joint session, have made a careful analysis and study of the proposed Banking Act of 1935. While the committees realize that certain provisions of title I of the pending bill affect adversely the larger banks, and that other provisions of the bill are not entirely acceptable to some of the (Federal Reserve) nonmember banks, they believe that the aims and purposes expressed in the provisions of titles I and III of the bill are, in the main, in the public interest, as well as in the interest of banking. The committees have, therefore, on behalf of the association approved in substance title I and III of the bill.

"Since the introduction of the bill in Congress the executive officers of the association have conferred at length with leaders of Congress and administrative heads of the Government regarding the provisions of title II. The committees believe that certain constructive changes should be made in this title. They recognize that some members of the association are of the opinion that it would be advisable to postpone definite action on this title of the bill until such time as a more detailed and careful study of its provisions can be made, but the committees believe that if the changes which they have in mind can be brought about through conferences it will then be possible for the committees to approve the entire measure.

"A special committee has therefore been appointed consisting of the president, the first vice president, the chairman, and one other member of the banking studies committee, and the chairman of the committee on Federal legislation. The above-mentioned special committee is authorized and directed to confer with the leaders of Congress and the administrative heads of the Government with a view to procuring such changes in the bill as are believed by the association to be in the best interest of commerce, industry, and the public.

"The personnel of the special committee is as follows: R. S. Hecht, president; R. V. Fleming, vice president; Tom K. Smith, chairman of the committee on banking studies; W. W. Aldrich, member of the committee on banking studies; Ronald Ransom, chairman of the committee on Federal legislation, of the association."

The special committee, having made further study of the proposed Banking Act of 1935, now submits the following recommendations:

TITLE I

We believe that the provisions of title I of the bill, if enacted into law, will improve the operation of the Federal Deposit Insurance Corporation in such manner as to enable it to serve more effectively the interests of the public and of banking. We are of the opinion, therefore, that the provisions of title I should be approved in substance. We know, however, that there are many nonmember banks, members of the American Bankers Association, who feel that the provisions of title I, making it compulsory for all banks to join the Federal Reserve System by July 1, 1937, should be given further careful study by Congress before that time.

TITLE III

We believe that the provisions of title III of the bill, which consists of amendments to the Banking Act of 1933, will materially clarify and improve the present law, and we are therefore of the opinion that the various provisions of this title should also be approved in substance.

TITLE II

We have given particularly earnest and careful consideration to the provisions of title II of the bill, which relate to the Federal Reserve System. The committee is deeply impressed with the fact that the changes contemplated in title II go to the very root of the theory and practice of banking as it has existed in this country and that it is difficult, if not impossible, to formulate final conclusions with regard to the provisions of this title in the brief space of time which has elapsed since the bill was introduced. If, however, it is considered advisable and necessary to pass legislation covering the subject matter of title II during the present session of this Congress, the committee believes that the following recommendations, if carried out, would eliminate many of the objections to the present bill.

The Federal Reserve Act is the result of years of study of the banking systems of the world and of extensive debate throughout the country and in Congress. The framers of the act intended that the operation and administration of the Federal Reserve System should be based primarily upon the requirements of agriculture, commerce, and industry, with due regard to the general credit situation of the country and the reasonable requirements of public finance.

The Federal Reserve System has now been in operation for a period of more than 20 years. During that period the laws relating to the system have from time to time been modified and adjusted, primarily to improve its application to changing conditions in agriculture, commerce, and industry. At no time, we believe, has there been any essential departure, through amendments to the law, from the basic purposes of the act, as originally drafted. We believe that these basic purposes should be preserved, although we recognize that in view of the rapid and material changes which have taken place in the economic structure of the country in recent years, further adjustments in the Federal Reserve System are from time to time inevitable.

1. The Federal Reserve Board

The committee believes that many of the changes in the Federal Reserve Act proposed in title II of the bill are of a constructive nature and should have the support of bankers, if the method of appointment and the tenure of office of the members of the Federal Reserve Board, in whose hands it is planned to concentrate greater power than ever before, could be so altered as to insure, as far as possible, the absolute independence of the Board from partisan or political considerations. It is our view that if a satisfactory solution of this problem can be found, one of the greatest objections to title II of the bill, as proposed, will have been eliminated. We will address ourselves first, therefore, to section 203 of title II of the bill which deals with the all-important question of the membership of the Federal Reserve Board.

Since the passage of the Federal Reserve Act, informed opinion both in Congress and among bankers has been striving toward the ideal of making the Federal Reserve Board a body of such independence and prestige that it might be described as the supreme court of finance and banking. We believe there is greater need now than ever before for realizing this ideal.

In order to bring about this result, we recommend that the Board be reduced from 8 members to 5. We believe this should be accomplished by the retirement from the Board of its ex-officio members, namely, the Secretary of the Treasury and the Comptroller of the Currency, and by reducing the appointive members of the Board to five as soon as a vacancy occurs (such a change would necessarily involve an adequate revision of the salary of the Comptroller who now receives a portion of his compensation through the Federal Reserve Board).

We heartily approve the proposed increase in the salaries of the members of the Board and would, in fact, like to see their compensation fixed at a somewhat higher figure than that mentioned in the bill so as to attract to these tremendously responsible positions the very best talent available. We believe that the plan of providing suitable pensions for the members of the Board is especially desirable because the security with which such an arrangement assures would be a further help in inducing outstanding men to accept a call for service on the Board and give them the financial independence which such a position requires.

2. The Governor of the Federal Reserve Board

The bill as originally introduced provided that the Governor should serve only at the pleasure of the President and that his service as a member of the Board should cease upon the termination of his designation as Governor. It has already been suggested that an amendment be made in the bill as proposed which would provide that the Governor, if no longer designated as such by the President, might, if he chose, continue his membership on the Board, but would be permitted to reenter private business (without the 2-year limitation) if he chose to resign upon not being redesignated. We would be entirely satisfied with this suggested change. If, however, it is deemed essential to give each incoming President the right to name a Governor of his own choosing, because of the fact that the administration will no longer be represented on the Board by the Secretary of the Treasury or the Comptroller of the Currency, it may be desirable to give the President the power to select the Governor of the Board and to provide that the term of the Governor of the Board will be the same as that of the President. It should also be provided in the act that the members of the Federal Reserve Board, including the Governor, shall be removable during their term of office only for cause.

3. Election of Governors of the Federal Reserve banks

It has been suggested that section 201 of the bill be modified so that the governor of each Federal Reserve bank shall be approved by the Federal Reserve Board every 3 years rather than annually, so that his term as governor would coincide with his term as a class "C" director. We believe that in order to preserve the independence of the governors of the Federal Reserve banks the term during which they may serve without having to be reapproved by the Federal Reserve Board should be as long as possible and that this approval should certainly not be required more often than every 3 years. Corresponding changes should be made in the act with regard to the election of vice governors of the Federal Reserve banks.

4. Open market operations

Neither the original text of section 205, providing for the open market committee of 3 members of the Federal Reserve Board and 2 governors of the Federal Reserve banks, nor the subsequent suggestion which has been made that authority over the open market operations be vested in the Federal Reserve Board, which would be required to consult with a committee of 5 governors selected by the 12 governors before adopting an open market policy, a change in discount rates or a change in member bank reserve requirements, seems to us to constitute a satisfactory solution of the open market problem.

Our suggestion is that the open market committee shall consist of the entire Federal Reserve Board (reduced to 5 members) and 4 governors of the Federal Reserve banks, selected by the governors of the 12 Federal Reserve banks annually, each member of the open market committee having a vote in the deliberations of the committee on the 3 subjects to be entrusted to it, i. e., open market policy, change in discount rates, or change in members bank reserve requirements.

5. *Changes in Reserve requirements*

It has been suggested that section 209 of the bill be amended so as to provide that the open market committee shall not have the power to change reserve requirements by Federal Reserve districts but only by classes of cities and it has been suggested further that for this purpose banks be classified into two groups, one comprising member banks in central reserve and reserve cities and the other comprising all other member banks, and that the reserve requirements be uniform within each group. We believe that these suggested changes are desirable but we think serious consideration also should be given to the desirability of fixing limits in percentage of deposits beyond which reserve requirements cannot be increased or decreased by action of open market committee.

6. *Real estate loans*

We do not favor section 210 as originally proposed, permitting advances against real estate up to 75 percent of the actual value of the property if amortized within 20 years, or up to 60 percent of the actual value of the property for term of not more than 3 years, in both instances without territorial limitations.

We are in favor of the suggestion subsequently made that all real-estate loans hereafter made shall not exceed 60 percent of the appraised value of the property and that the Board be given discretion to make regulations governing real-estate loans held by banks at the present time.

We also believe that the presently existing territorial limitations, or some similar limitations, should be retained in the law and that unamortized real-estate loans should be permitted up to a period of 5 years.

SUMMARY

We believe that the foregoing modifications in title II of the bill (nos. 1 to 6, inclusive) are fundamental, and that all of them are in the national interest. If changes substantially along these lines cannot be made in the original draft of the bill, we would be strongly opposed to the enactment of title II. However, if these changes, some of which in whole or in part have been heretofore recommended by Governor Eccles and placed into the record of your committee, are adopted, we would be in substantial agreement with the provisions of title II, provided that the following additional changes, which have also been suggested by Governor Eccles during the course of your hearings, are included in that title:

(*a*) *Admission of insured nonmember banks*

It has been suggested that section 202 of the bill should be amended so as to provide that the Federal Reserve Board shall have authority to waive not only capital requirements but all other requirements for admission of insured nonmember banks to the system, and that the Board be permitted to admit existing banks to membership permanently without requiring an increase in capital provided their capital is adequate in relation to their liabilities.

(*b*) *Federal Reserve bank experience for Federal Reserve Board members*

It has been suggested that section 203 (1) of the bill be amended so that as a general policy two members of the Federal Reserve Board shall be selected, when possible, from persons who have had experience as executives of the Federal Reserve banks.

(*c*) *Federal Reserve Board pensions*

It has been suggested that section 203 of the bill be modified so as to provide that any member of the Board, regardless of age, who has served as long as 5 years, whose term expires and who is not reappointed, shall be entitled to a pension on the same basis as though he were retired at 70 years of age; that is, he is to receive an annual pension of $1,000 for each year of service up to 12.

The committee offers all of the foregoing suggestions in the earnest belief that they represent constructive modifications of title II of the bill as proposed, with a view to rendering the operations of the Federal Reserve System more beneficial to the interests of the Nation as a whole.

We respectfully request, therefore, that these suggestions be given consideration and study in the deliberations of your committee. We expect to continue our study of the bill, and would like to have the privilege of submitting to you any further suggestions which may occur to us.
Respectfully submitted.

AMERICAN BANKERS ASSOCIATION,
RUDOLPH S. HECHT,
ROBERT V. FLEMING,
TOM K. SMITH,
WINTHROP W. ALDRICH,
RONALD RANSOM,
Special Committee on the Proposed Banking Act of 1935.

(Thereupon, at 12:30 p. m., the committee recessed until 3 p. m.)

AFTER RECESS

The committee reconvened at 3 p. m., Hon. Henry B. Steagall (chairman) presiding.

The CHAIRMAN. We have waited some little time, and I am sorry we have not more members present. Your statement will be in writing, where all members will have an opportunity to acquaint themselves with it, and I am going to suggest that we proceed with Dr. Fisher.

STATEMENT OF DR. IRVING FISHER, ECONOMIST

The CHAIRMAN. Dr. Fisher, we would be glad for you to address the committee without any interruption, if you so desire; and when you desire to be interrupted, please let us know.

Dr. FISHER. I want to say, in the first place, I agree substantially with the position taken by Mr. Hemphill this morning. In some details and minor matters I would differ somewhat, but we certainly agree on the main point—that the depression is substantially due to lack of money, money being used, in his sense, including bank deposits subject to check.

I myself believe very strongly that this depression was almost wholly preventable, and that it would have been prevented if Governor Strong had lived, who was conducting open-market operations with a view of bringing about stability. When I say " prevented ", I mean to a large extent. We would have had a stock-market recession, but not a subsequent depression.

I believe also that the depression is mostly curable today, even after all that we have been through, and in a very few weeks, if this bill is passed with suitable changes, which have been suggested by Mr. Hemphill, and which, in some other forms, I will suggest also.

As I see it, the most outstanding important factor in the depression has been the destruction of what may be called "checkbook money or bank credit."

As you know, we, each of us, think of our balance on the stub of our check book as though it were money, comparable with the money which we carry in our pockets. But the checkbook money and the pocketbook money, under our present system, are distinguished, to a very considerable degree, and that is really the source of our difficulties. Our pocketbook money cannot be changed in amount without action by the Government authorizing more greenbacks or silver certificates or currency, or changing the weight of the dollar, or otherwise.

But the checkbook money not only can be changed but is constantly being changed. And as it changes it carries with it a change in the purchasing power of the dollar and in our business conditions, so that we have the so-called "business cycle" and depression as a consequence.

We had, in 1929, $23,000,000,000 of checkbook money—that is, deposits subject to check. Of this, $8,000,000,000 was destroyed. I am not now speaking of the savings deposits or time deposits which draw interest, for they do not circulate, as Mr. Hemphill so well said this morning. They are not a part of our circulating medium, and it is rather unfortunate that we use the same name to designate these two widely different things. "Deposits" apply properly to the deposits subject to check, but the so-called "deposits" in savings banks are really investments, and no more deposits in the sense that something is there which you expect to find when you want it and want to use it as money. They are really investments, like a Liberty bond.

If we had destroyed 8,000 miles of railway out of 23,000 miles—if some earthquake or other catastrophe had destroyed, so that everyone could see it and it was visible, 8,000 out of 23,000 miles of track—I think everyone would realize that it must interfere with traffic, and as traffic was reduced, everyone would recognize the fact that the reason it was reduced was that there was not the track to carry it.

Our money is the highway of commerce and it is more important than the physical track, and when we destroy eight twenty-thirds of that trackage, it does interfere with traffic.

I believe that the situation is still serious and that something must be done. In fact, it is so serious that, when speaking with reporters present and for the press, I hesitate to say how serious it seems.

This bill, I believe, is the most important bill which has come up in this administration. For good or for ill, it means much for the country. I regard it only, however, as a half-way measure and almost as a half-constructed measure. I think the plan of Frank A. Vanderlip, formerly president of the National City Bank, for a monetary authority is better. I would say that the Vanderlip plan is a three-quarter way measure. I think the plan Mr. Hemphill presented this morning might be called a "100-percent measure."

He and I and Mr. Vanderlip have the same objectives as are in this bill.

As Mr. Hemphill said this morning, if this bill were rightly administered—if that is conceivable—it would, as he expressed it, "do the trick."

On the other hand, if it were wrongly administered, it could do irreparable damage. Rightly administered, it might get us out of the depression in a few weeks. Wrongly administered, it might thrust us deeper in.

As a matter of fact——

Mr. Brown of Michigan. Professor, are you speaking of the bill as submitted to us?

Dr. Fisher. Yes.

Mr. Brown of Michigan. The Steagall bill?

Dr. FISHER. The bill as is.

Mr. BROWN of Michigan. Not inclusive of yours?

Dr. FISHER. Not including any suggestions of mine. I am referring to title II, the heart of the measure.

The CHAIRMAN. I had assumed, without saying so, that you would address yourself to title II of the bill.

Dr. FISHER. Yes. But when I said, " if the bill were rightly administered, wonderful results could come ", I did not mean that I expect it to be rightly administered; and that is not because of any lack of faith in Mr. Eccles, nor is it any reflection on anybody, but it is merely because the bill does not specifically state what is right and what is wrong. In all probability it canont be rightly administered. There is too much discretion in it and too little guidance, too little in the nature of a criterion, to tell those who administer this bill what is expected by Congress of them.

For instance, the bill contains—and perhaps this is the most important feature—the power to increase or decrease reserves. Can you imagine that that power will be exercised with promptitude and effectiveness? If the reserves of a bank, that are now required to be 7 percent, are raised to 15 percent or 20 percent or 30 percent, or even to 8 percent, I think there can be no question but that it will be resisted by several thousand banks out of the 15,000 banks. It is inconceivable to me that there would not be hundreds, if not thousands, of letters protesting against any disturbance. Even if there were no disturbance of the reserves, there would be fear of the disturbance all the time, and we have fear too much already.

Not only would there be this resistance of the banks who would feel that they were the victims, and most of whom would not be willing to sacrifice their own personal individual interests, in the belief that Mr. Eccles was wise, and that it would be for the interest of the public as a whole; not only would there be this resistance from many banks, but I think it is altogether likely, if you follow the experience that we have had in the last few years, that there would be dissension in the Federal Reserve Board itself; as it is now constituted, I think I know how the lines would be formed, and that there would be those who would say, " Yes, we have this power, but we do not propose to exercise it. Mr. Eccles, you come in here and tell us what to do. We have had more experience than you. We do not think it is wise to rock the boat and disturb conditions as they are."

Mr. Eccles would be right and they would be wrong, but he would find it very difficult to convince them of that fact.

What you want, it seems to me, is to law down a policy. The Congress should prescribe in this bill what that policy is, when the reserves should be raised and when they should be lowered, or what is the object at the present time to be aimed at. In fact Congress should provide a better means of doing it than by constantly changing the reserves and creating the uncertainty that even the power to change will make.

Now, it seems to me that the policy which should be pursued is in general terms the policy which has been outlined by President Roosevelt. On several occasions he has outlined a twofold policy for money, reflation, and stabilization. I believe he never used that word "reflation", but it carries in it so many things that I like to use it. It does not mean "inflation." It means correcting deflation. Inflation comes only when you have not only made the correction, but have gone further.

Reflation restores the price level to a certain prescribed form, which should be prescribed by Congress, say, the price level of 1926, which I think would be a very good one to adopt. You should prescribe two things; reflation to that price level and stabilization thereafter. Congress should also prescribe the sort of index numbers which should be used. In my opinion, it should be similar to that which is used in Sweden, an index number of the retail price of the cost of living. But, at any rate, there should be in this bill, in some form, a statement of policy of these powers in it. As they are now, you give a tremendous and dangerous power to people, and some day it will be abused. I do not believe that it would be what you call abused by Mr. Eccles or even by those on the Board now, who would disagree with him on the policy, but the time might come, and eventually it would almost certainly come, if so great a dangerous power were put in the hands of the Federal Reserve Board, and it would be manipulated for some ulterior purpose.

It is natural that Mr. Eccles should want the discretion. It is natural that the President wants the discretion that he has got. I do not think that Congress should have given the President the wide discretion that they have given him, and I do not think he has used it wisely in many respects. I do not think it is American to give the discretion that has been given, and would be given in this bill, to Mr. Eccles or the President. It seems to me that it is shirking the problem, and that Congress should solve the problem and prescribe to the Executive what is expected to him.

I know the same thing happened with Governor Strong of the Federal Reserve Bank of New York, to whom I have alluded. He resisted the introduced of any criterion to determine how he should manage the open-market operations. He discovered, although economists before him had pointed out the possibility of it, that open-market operations would stabilize—he discovered for himself what was necessary to cure the deflation that started in May 1920 and to prevent an inflation that might otherwise come. And for 7 years he maintained a fairly steady price level in this country, and only a few of us knew what he was doing. His colleagues did not understand it. And yet when we, who were intent on having a legal regulation, tried to get a bill in Congress passed, first the bill introduced by Congressman Strong, when we had a Republican administration, and afterward almost the identical bill introduced by Congressman Goldsborough (afterward it was passed by the House, but that was after Governor Strong's death), Governor Strong told me that if that bill were passed he would resign. He said:

> If you let me alone, I will do the best I can. But if you try to prescribe a criterion, I am not sure that I can measure up, and I do not want that responsibility.

Every one likes to have discretion, or seemingly difficult, and not be told to toe the mark, and that something difficult is expected of him. Then they may not be able to perform.

It seems to me that it is un-American and unwise in every way to leave the policy at loose ends.

I was here when Mr. Eccles spoke the first day, and I quite agree with what he said in regard to one measure in this bill, to make the open-market operations easier and prompter. He said:

> In this matter, which requires prompt and immediate action and the responsibility for which should be centralized so as to be inescapable, the existing law requires the participation of 12 governors, 8 members of the Federal Reserve Board, and 108 directors, scattered all over the country, before a policy can be put into operation.

Naturally the results were disappointing. When Governor Strong had his own little committee of five, which were irresponsible, which was not even controlled by the Federal Reserve Board, but was really himself, surrounded by four men whom he could call on the telephone, governors of the next biggest Federal Reserve banks to his, he could immediately put in an order to sell or buy Government bonds to the tune of $100,000,000.

But because of the dissension, because of the feeling by certain members of the Federal Reserve Board, that Governor Strong was acting without the authority of the Board, and because they wished to be the ones to prescribe something for him and to show him that they were the boss, the Federal Reserve Board discharged that committee and then reappointed it subject to their own wishes, and then enlarged it until you have this cumbersome board with 12 governors, 8 members of the Federal Reserve Board, 108 directors, scattered all over the country, before any policy could be put into operation.

This bill would cure that, and it is well that it should. On the other hand, it does not prescribe what the policy should be. The policy would be simply left to discretion, with fewer men to decide upon it. There will be, I am afraid, the almost same opposition, dissension, vacillation, that we have at present. There would merely be less delay.

As Mr. Eccles said:

> Open-market operations are the most important single instrument of control over the volume and the cost of credit in this country.

I think that the bill need amendments. The most important amendment, in my opinion, is one that was stressed this morning by Mr. Hemphill. Instead of allowing Mr. Eccles, irresponsibly, without any guidance, to raise or lower the reserve requirements of the 15,000 banks in this country, according to whatever rules he and his associates may establish, instead of doing that and getting all the resistance and all the uncertainty and the futilities that would surely come, it seems to me it would be very much better to raise the reserve requirements at once to 100 percent, as Mr. Hemphill has suggested.

Then there would be no question of what the reserve was. This would not cause any shock in the present situation, although it shocks some people at first to think of it. The 100-percent reserve could consist, to a large extent, of Government bonds until those bonds matured, and we have, counting the Government bonds, practically 100 percent already. All you would need, therefore, would be to galvanize the situation as it is, so that the reserve would consist of three factors: Cash, that is pocketbook money; Federal Reserve credit, which is, so to speak, the checkbook money of the member banks against deposits in Federal Reserve banks; and Government bonds.

As I say, we have that situation already, very nearly. All that we need to do is to perpetuate it; but that is extremely important.

Mr. BROWN of Michigan. Professor, you mean that reserve against the deposits in the banks?

Dr. FISHER. I mean the deposits subject to check only, only demand deposits, but not time deposits or savings.

Mr. REILLY. A bank would be a bailee, then?

Dr. FISHER. Yes; a bank would be a depositary. These deposits would be real deposits. What you call your cash in bank would really be cash and really be in the bank. When you deposit an umbrella you expect it to be kept there so that if it rains it won't be to somebody else when you want it.

Mr. BROWN of Michigan. I suppose you would have a basis of compensation to the bankers for that service?

Dr. FISHER. Yes, certainly.

One great object, and I think it is the principal object of galvanizing this 100 percent, and not allowing a constant trombone of expansion and contraction, such as is permitted in this bill, is to avoid uncontrolled inflation. It is true, as I say, that if this bill is passed such inflation could be prevented, provided the resistance to it is not too great and there is not too much dissension within the Board. But as things are at present; that is, if this bill does not pass in any form, you are under constant danger of tremendous, uncontrolled inflation. With reserves now at 100 percent, counting in bonds, as soon as the banks feel a little confidence and business is willing to borrow, its reserves will go down, which means that credit will go up, so that checkbook money will expand. We need a certain amount of that, as I say, reflation; but I fear we are going to have real inflation.

No one, I think, has written more against inflation than I have, and it has irked me a great deal to have my name associated with the idea of uncontrolled inflation. But I am just as much opposed to deflation as I am to inflation. What we want is to avoid both, to get stabilization, after we have once reached the point at which we want to stabilize.

Mr. BROWN of Michigan. Dr. Fisher, I do not want to keep interrupting you, but I do not follow you in one respect. You speak of there being sufficient bonds now to provide a 100-percent reserve. Are those bonds in the hands of the bankers or do you mean all bonds?

Dr. FISHER. Government bonds in the hands of the bankers, about $10,000,000,000 of those bonds now in the hands of the bankers.

Unless we do something to galvanize this situation and to prevent inflation, we are in constant danger of it. I have not joined those like Professor Kemmerer and Professor Sprague, who have been constantly warning the country about inflation, because it did not seem to me wise. I think the public does not understand this subject well enough, and the effect of their statements, to the effect that we are in danger, merely fills the public with fear, and that is all it does. That fear produces deflation rather than inflation. If the people really understood, they would immediately want to part with their money and get something for it; but instead they are hanging on to it, hanging on to their money, because they think there is this vague fear, and they are in debt, and they think they better keep their money and not part with it or buy with it, or anything of the sort.

The result is that this propaganda, intended to promote the President's very proper desire to have a moderate reflation, this propaganda has paralyzed almost everyone with fear and produced, apparently, undue caution in the administration itself; so that it has been a deflationary influence, and at the same time we are accumulating these surplus reserves. The reserves of the banks now, in cash or credit, only need to be 7 percent, 10 percent, and 13 percent, respectively, in the three different grades of banks. So that there are now surplus reserves, and if ever that big surplus is used and lent out, then you will have a tremendous inflation. And the result is that the administration is afraid now to proceed with the reflation for fear that it will turn into inflation and become uncontrolled. That is the fear which is gripping the banks and those who understand the present situation, and the longer we stay where we are or suffer deflation the greater the danger ultimately of inflation. If I may use a simile, it is as though stabilization is represented by running your automobile on the road, while on one side is the inflation ditch and the other side is the deflation ditch. We have gone off the road into the deflation ditch, and we are trying to get back onto the road. We turn the wheel and finally we get it going, and instead of getting onto the road and staying there, we cross over the road and into the other ditch. That is where the present danger is. That danger will exist as long as you have got this situation, with a movable reserve, unless it is moved with the utmost wisdom. It is better to have a rigid reserve, and no reserve can be rigid unless it is 100 percent.

Mr. FORD. Doctor, you spoke of surplus reserve.

Dr. FISHER. Yes, sir.

Mr. FORD. In what sense do you mean that?

Dr. FISHER. Surplus reserve, reserve above the legal limit. A typical bank needs 10 percent. If it has 11 percent, it has 1-percent surplus reserve. I noticed this morning when I got off the train, an article by Professor Kemmerer, in which he says:

> If the value of gold remains where it was in February 1933 and approximately where it is today in the free-gold markets of the United States—

meaning by "value of gold" the purchasing power over commodities—

> the cost of living will have to rise about 50 percent above what it is today, and the slack represented by the reduction of the gold content of our dollar has been completely taken up.

Later in the same article he says:

> If the value of gold depreciates to its 1926 level, after the present worldwide scramble for gold has subsided, then, once the slack represented by the gold content of the dollar has been completely taken up, the cost of living will be about 116 percent higher than it is now.

In other words, the cost of living will be doubled.

That will be just about as bad as the situation we have now in the opposite direction.

A recent article in the Harvard Review of Economic Statistics puts the figures far higher than Professor Kemmerer.

Mr. REILLY. Have not the prophecies as to price relations, by deflating the gold dollar, all been disappointing?

Dr. FISHER. No; if you will look at some of the charts of Professor Warren, you will find that for the exportable or importable commodities, and the commodities closely associated with them, what they call "basic commodities", there has been a close and immediate relationship. Every change of the price of gold has been accompanied by a like change, almost exactly proportional change, in these basic commodities. But the "sticky" prices, the prices of commodities that stick, that do not move easily, have not followed. Personally, I would not be sorry to see the gold content reduced still further. But there will then be this danger of inflation, even greater than at present, and you will always have that danger of inflation and of deflation as long as you have a loose steering gear, so to speak; that is, a changeable reserve; that is a reserve requirement less than 100 percent.

Mr. REILLY. Do you mean, domestic prices in England have not reflected the shrinkage of the pound value?

Dr. FISHER. The prices in England?

Mr. REILLY. The domestic prices have not reflected the shrinkage in the pound value.

Dr. FISHER. Yes; they have reflected it, to a considerable extent. I have one of my own articles here which will show that, and show like statistics for all the countries with respect to the price of gold, all the countries for which we have statistics. You will find that the price level, even if you include other than the basic prices, will correspond to the price level in any country compared with the price in a gold-standard country, like Holland or France, will correspond closely to the price of gold.

Mr. REILLY. Doctor, is it not a fact that England is not anxious to go back on the gold standard, because of the fact that she has an advantage, as an export nation, because of her low domestic prices?

Dr. FISHER. I do not think that the advantage in exporting from deflation is a major consideration. I doubt if it is a major consideration even in England. I think I know the man who is really doing this adjusting of the price of gold in England, and I know that that would not be his—at least I think I know—that would not be his idea.

There is an idea, such as you refer to, but it is a temporary one, and it is not the important factor. The important factor is the domestic situation. However, that would take us a little aside from what I was aiming at here.

The point here is that, as long as you have any reserve less than 100 percent, you have a loose steering gear, and you have got the same degree of control over your monetary machine. There are many advantages in having a 100-percent reserve. One is that it obliterates the distinction between the two kinds of money, the check-book money and the pocketbook money, which we have today.

I noticed this morning that there was some confusion in the questions which were asked of Mr. Hemphill. He used the word "money" to refer to both. When you have a 100-percent reserve there would be no distinction, because the money which you think you have in the bank would really be there. I do not mean that it needs to be right on the spot. It could be in the Federal Reserve instead of in the individual bank. It should always be available and always exactly corresponding to your deposit. You can call it credit, if you will, but it cannot disappear, under the 100-percent system, and that is the important thing. Then there would be no need to distinguish between the pocketbook money and the checkbook money.

I might say that this plan of 100 percent is not a new idea. I myself took it up quite recently, but Mr. Hemphill had it much longer than I, and some professors at the University of Chicago had it longer also, and looking over the literature, I find that it has been an old idea, and not only that, but it was the original idea of deposit banking. It was how banking really started. Banking really started with deposits which were real deposits, gold, and other valuables, and they were transferred by written instruments, corresponding to what we now call checks, and the banker was expected to keep all the gold that was deposited. When he found it was never called for, or almost never called for, he thought no one would be the wiser if he should loan some of it out, and it was a breach of trust, and that is how modern banking started.

Afterward, when they were found out, the bankers said, "What of it, as long as you get your money back and as long as I have protected myself by collateral, and so why should you complain?"

The depositor, not thinking of the mechanics of the thing as to public policy, but merely looking at it from his personal point of view, with little understanding of the mechanics of money and banking said, "All right, I will give you my consent."

Today, you cannot accuse the banker of any breach of trust, but it is bad policy for the public just the same, because it makes a constant increase and decrease in the volume of the circulating medium.

Now, today the proposal of the 100-percent plan has astonished a good many bankers. Some of them have tried to laugh it out of court, or ridicule it, but those who have studied it have come to think that that is the best thing for the banker; not only Mr. Hemphill, who has one of the acutest minds in banking that I know, but a good many others.

I have a book coming out on this subject, which will be out soon, and I think I can get some advanced copies to send members of the committee if you will do me the honor to read it, next week, but it will be out in the proper sense of that word "out" in 2 or 3 weeks.

The second appendix to that book, which is a very short paragraph contains quotations of two bankers who have become quite enthusiastic on this subject. One is the president and the other the vice president of the Plaza Bank of St. Louis. The president's name is Von Windegger, and the vice president's name is Gregory. They have written me joint letters, sometimes one signing and sometimes the other, but always representing the opinions of both.

Mr. Brown of Michigan. To do justice to a distinguished citizen of my State, I might say Henry Ford had that idea 2 or 3 years ago, when the banks were in trouble in Detroit.

Dr. FISHER. I am very much interested to know that, and I will make a note of it.

I sent to these St. Louis bankers a number of letters and these men have read my book and manuscript three times. I will quote, not to tire you, just two passages from these letters:

> My first impressions, I think, were naturally to disagree with you on several points, but I would like very much to have an opportunity to think about your plan some more, and if it is not too much of an imposition I would like to have you send me the draft of your complete manuscript.

Their first reaction was unfavorable.

In a later letter:

> We have, I think, both approached the problem in the past from the social point of view rather than the economic, and our hopes for correction have largely been in the thought that our existing system should be placed in the hands of more honest administrators, and that the evils could be largely overcome with the existing machinery.

That is what this bill is trying to do. [Continuing quotation:]

> I think we had hopes that more men of Governor Strong's admitted ability would miraculously appear as saviors of our system. Not because we were selfish, but because we overlooked it. We did not conceive such a system as your 100-percent system. Realizing that we lived a lie, we did not see the obvious thing that the correcting of this lie, would at the same time, correct most of our evils. From this you will understand that, although we were at first reluctant to admit that banks, good and bad, had definitely failed to control their credit system, on deliberation we have finally agreed on practically every major point in your system.

I could go on and quote other bankers as well. I have no doubt the bankers, as a mass, will record themselves as opposed to this proposal, but those who are thinking, who have thought it through, who have studied it, who have read this book which I have written, which gives it in more detail than anything else, have come to the opposite conclusion.

I have taken a whole year in which to prepare this book and to submit it to 150 different people, including a number of bankers, in order to find out whether there was something there which was in need of change. Of course, I have modified it considerably as time went on. I have found that Mr. Hemphill was the most constructive of all the critics.

Besides introducing the 100-percent reserve, and seeing to it that the banks were properly recompensed, as has been mentioned, for having to sterilize their assets to a certain extent, a second proviso is important. We should bring in all the banks into the Federal Reserve System which have checking accounts, or, if a bank does not want to come in as a whole, its checking department could come in. That is, all the checking institutions in the United States would be in one system, under the control of your central authority, whether it is the Federal Reserve Board or what it may be. Then you can have control of the money of the country.

I want to make a big distinction between controlling the money of the country and controlling the banking of the country. Properly speaking, banking is lending money, and it is my idea that the more the Government keeps out of the banking business, in the sense of the money-lending business, the better.

I think if there is anything the Government cannot well do, it is this business of lending money. I think that should be left to the bankers.

But the matter of regulating the quantity of money, creating money, and destroying money, is a governmental function and cannot be delegated to private hands. Under our Constitution, article I, with a liberal interpretation, Congress is given the power to regulate the value of money, and it has never properly exercised that function. That is the reason why we have these chills and fevers that we call the business cycles, these booms and depressions.

Our present system, as distinguished from the 100-percent money system, may be called the "10-percent system", and is essentially unstable and uncontrollable. Money comes into existence whenever a loan is created and goes out of existence when that loan is paid. That was mentioned this morning by one of the committee in a question directed to Mr. Hemphill, in the thought that it was good, that when any commodities were created they would be financed by the man or merchant involved going to the bank, borrowing the money to turn over those goods with, and then paying his loan after the transaction had been completed, so that the money comes into existence when there is need for it and goes out of existence when there is no need for it. That is a beautiful dream, and an irridescent dream. It has never worked that way. The money comes into existence and stays there, to a large extent, even when its usefulness has passed, and the money goes out of existence when it ought to come into existence. This is not simply because of the necessities of commerce, but it is more primarily because of the necessities of the bank. It is the bank reserve which makes the trouble. We have in our Federal Reserve Act the phrase "to accommodate business."

We are supposed to regulate the rediscount rate, and since Governor Strong, we also have regulated the open-market operations with a view to accommodating business, but the average bank makes its average operations accommodate not business but the bank, and it has to do so. I say this not intending to sneer; the first law of nature is self-preservation, and every bank must observe that law like other organism. You cannot blame the bank, and you would blame it if it did not try to keep its own existence. But when there is a run, when there is an incipient depression, when other banks are liquidating, there is a pressure on all the banks and the tendency is for all of them to liquidate in order to be safe. And for every dollar that the public pulls out of the banks about $10 of checkbook money is destroyed. And that explains what happened between 1929 and 1933. Checkbook money disappeared to the tune of about $8,000,000,000 because people paid their loans at the banks and they paid their loans at the banks not because they had finished any transactions, but because the banks demanded payment, and the banks refused to renew, and the banks refused to extend new credit. Why? Because the banks were afraid. Why were they afraid? Because their reserves were so low.

It is a case of low reserves. If they had had a 100-percent reserve there would have been no fear and no operation of this sort, but with a 10-percent reserve it was inevitable. The result was that the public pulled out of the banks nearly $1,000,000,000, and destroyed, as I said, $8,000,000,000 of checkbook money to do it, because every dollar of actual money in the banks means the pyramiding of $10 of loans and deposits by the banks as a whole. That is the essential thing. We have not a homogeneous relation between the pocketbook money and the checkbook money.

When the public would draw its money from the banks, as we think they do, they are withdrawing other people's money, as well as their own, and the bank has to pay the loans and reduce its checkbook money and at once that increases the money in circulation. Some people, not realizing that checkbook money is the most important money in this country, pointed to the fact that instead of four billions, we had five billions circulating, and said "Look there. We have got plenty of money," not realizing that eight billions had been sacrificed to produce the one billion. The banks had destroyed eight billions of checkbook money in order to supply the public with one billion or less of pocketbook money.

Mr. FORD. Doctor, might I interject a thought there? If the banks had been on a 100-percent reserve, with reference to deposits, demand deposits, and this matter came about, what would have occurred?

Dr. FISHER. What would have occurred?

Mr. FORD. Yes, sir.

Dr. FISHER. It depends on how for back you go. In the first place, you would not have had any boom to make a banking cycle or depression. In the second place, assuming that we had the boom, when the time for the depression came, we would not have had the depression, because there would not have been either the fear on the part of the public, or the fear on the part of the banks which stimulated them to ask for the payment of the loans.

Mr. FORD. Let us assume that when the thing came about, the banks had the privilege of taking their sound assets, as distinguished from the limited number of assets that were capable of discounting at the banks, and if all those sound assets had been discounted, what would have happened?

Dr. FISHER. It would not have made any difference, as long as your cash reserve was a fraction of the outstanding deposit liabilities. That is the vital point, and not the nature of the assets. That is where people are making the great mistake in trying to reform the Reserve System. They say, "The trouble is it is this kind of asset instead of that kind of asset." That has almost nothing to do with it.

Mr. FORD. You mean to say, here is a bank with a deposit liability of $500,000, and they have a 10-percent reserve——

Dr. FISHER. Yes.

Mr. FORD (continuing). If, after they have paid the 10 percent on demand deposits, they were able to go into their portfolio and take other securities which were owned and take them to the Federal Reserve and discount them for a period, would not they have been able to get sufficient money to have met that demand, and, therefore, have stopped it?

Dr. FISHER. Yes; the Federal Reserve would act as a cushion.

Mr. FORD. Yes, sir.

Dr. FISHER. They could get there on a 10-percent reserve, with the action of the Federal Reserve, but in the end that means even a more unstable condition.

Mr. FORD. I wish you would elaborate on that point. That is what we are trying to do here.

Dr. FISHER. Yes, sir. We have now what I called a "10-percent system", but the 10-percent reserve that we now have, as Mr. Hemphill pointed out this morning, is not cash. It is simply a deposit liability of the Federal Reserve. So that, for, say, \$3,000,000 of deposits subject to check, representing checkbook money, in the hands of the public, the banks which have these checking accounts, are supposed to keep 10 percent reserve on the average; \$300,000, then, are supposed to be in reserve at any time, to meet that demand liability of \$3,000,000. But the banks do not keep that 10 percent reserve in their value as money. They deposit it in the Federal Reserve, and the Federal Reserve in turn only has to have 35 percent of the \$300,000 reserve or about \$100,000 of actual cash in its vaults.

Mr. FORD. Against that?

Dr. FISHER. Against that. So that you really have \$100,000 actual cash supporting \$3,000,000 deposits circulating as cash; that is a 3½-percent system instead of a 10-percent system. And the reason that we are having, I think, worse depressions than before the Federal Reserve System was started—we have had two bad ones, one in 1920 and this subsequent one—is because of that. I remember an economist writing me in astonishment, "How does it happen that the price level could be almost cut in two between May 1920 and December 1921?"

I think the reason is the instability, to which I am referring here. The pulling out of a dollar of pocketbook money from the banks means a reduction of \$10 of check-book money. In fact, if the dollar is pulled out of the Federal Reserve, it really means a reduction of \$30. And it is only when you have very good management on the part of the Federal Reserve, so that they always have a surplus reserve of their own and managed with a great deal of discretion, that you can avoid this. But when you get into difficulties, in either direction, with booms, as in 1920, or with depressions, such as we have had in the last few years, then you have a thirtyfold variation possible. Before the Federal Reserve Act was passed we had bigger reserves, 25 percent, and so forth, and these reserves had to be cash, to a large extent, in the hands of the individual banks. Even when the Federal Reserve was started we had more than the present 7, 10, and 13 percent.

They were lowered, and when that lowering was proposed, Robert Hemphill was then credit manager of the Federal Reserve Bank of Atlanta, and he proposed, instead, they should raise them, with the idea ultimately to make them 100 percent.

But he was almost a minority of one. Others thought, just as the goldsmiths did, "What is the harm? I am not going to keep this money idle."

The CHAIRMAN. Dr. Fisher, why cannot we accomplish—which some of us have tried to do—the same safeguard against the fear of the depositor who wants to withdraw his deposits, and the fear of the banker who, because of the possible fear of depositors, is himself afraid to lend—why cannot we safeguard agaisnt those developments by adequate and complete insurance of bank deposits, as some of us have tried to do, and as we have done in part?

Dr. FISHER. That is a substitute method for accomplishing the purpose of safety of the individual deposit. On the other hand, one of the advantages of the 100-percent system is that it makes insurance unnecessary for deposits subject to check, and have your insurance for the others if you want to.

Mr. BROWN of Michigan. It does not seem to me you have completed an answer to Mr. Ford's question.

Dr. FISHER. All right. I will come back to it. But meanwhile I am on this. The main danger, Mr. Chairman, that we want to guard against is not the safety of a man's deposit. It is the safety of the price level.

The CHAIRMAN. Dr. Fisher, what you really want to do is to safeguard against the fear of the depositor?

Dr. FISHER. Not only that——

The CHAIRMAN. And, in turn, safeguard against the fear of the banker.

Dr. FISHER. Yes.

The CHAIRMAN. Who, when fear exists, calls his loans and turns on a squeezing process, and, therefore, of course, affects the price level and general business conditions?

Dr. FISHER. I would like to emphasize that the main point is not fear at all. The main point is, we should produce stability. You might conceivably have a system, such as ours, operated in such a way that there would be no bank failures, no bank runs, keep insurance and so forth, but all the time the bank is destroying and creating money, and it is only when the two are balanced properly that you have stability. But if they are creating more than they are destroying, or if they are destroying more than they are creating, you have a boom or a depression.

This morning I remember a man said to Mr. Hemphill, there are many sound banks that maintain their stability, and he said, "Yes; but by busting everybody else", and that is perfectly true. Of course, he did not mean everybody, but the banks save themselves, to a large extent, by this process—and if all the banks had saved themselves and if there had been no runs and had been no panic, but the bankers had merely prudently seen that there had been too much assets, and called a halt, there would still be these chills and fever, not as bad as we have them perhaps, but the expansion and contraction is what we want to avoid rather than fear.

Mr. BROWN of Michigan. Let us get to the final answer of Mr. Ford's question.

Dr. FISHER. Yes; you said I did not answer it.

Mr. BROWN of Michigan. I take it that he assumes in this bank, having $500,000 of deposits or demand liabilities, that the bank would have $400,000 of sound assets, say. Now, under the bill as presented by Governor Eccles, we have this section:

Upon the endorsement of any member bank, and subject to such regulations as to maturities and other matters as the Federal Reserve Board may prescribe, any Federal Reserve Bank may discount any commercial, agricultural, or industrial paper, and may get advances in any such member banks on its promissory notes, secured by any sound assets of any such member bank.

I take it that the purpose of that addition to section 13 of the Federal Reserve Act was to enable banks in times of emergency to borrow on this $400,000, in Mr. Ford's bank, in sound assets. Is not that banker in a much better position than he was, under the present law, and would not that eliminate a good deal of fear, on the part of the banker and on the part of the depositor?

Dr. FISHER. Yes; it would go a certain distance in that direction, to help allay the fear of the individual depositor.

Mr. BROWN of Michigan. It would give something like 75 percent liquidity as against 15 or 20 percent under present conditions. Do you not think that that is a great improvement?

Mr. FISHER. Yes; I think that that is a great improvement, but I do not think it is at all adequate to prevent booms and depressions. I am much more interested in preventing booms and depressions than in anything else, and you could still have what you call "safety", with booms and depressions.

There is no reason why we should not get rid of big booms and depressions completely, if we will avoid this partial reserve system which is what makes the banks destroy money sometimes and create money at other times.

Mr. BROWN of Michigan. It practically liquefies a very large percentage of the balance of the banks' assets?

Dr. FISHER. Yes, sir. What you call "liquidity" merely means safety to the individual depositor. But the liquidation affects the volume of the circulating medium, and you must not have a liquidation which affects the circulating medium. Let me put it another way.

Mr. BROWN of Michigan. How does it affect that? By increasing the amount of the currency in circulation, does it not?

Dr. FISHER. Decreasing the liquidation will decrease the amount of deposits subject to check, and decrease it very markedly. You see what really happens today is, when a bank is started with $1,000,000 of actual cash in its vaults, you can picture it something like this: On the first day it lends out of that $1,000,000, in loans of $10,000, $1,000, and so forth, until that million dollars is gone, and that is covering its capital. That is all right. Those people who borrow it, let us suppose, put it all back in the bank. Then there is $1,000,000 in the bank and $1,000,000 of deposits against it, and the depositors really virtually own the money in the bank, instead of the bank itself owning it, and the bank has the promissory notes of the depositors in its place.

So that there are $2,000,000 of assets, consisting of $1,000,000 of notes, which we can say belong to the bank, and $1,000,000 of money which belongs to the depositors. That is all right, too. That is 100-percent reserve. But the next day the bank proceeds to lend that $1,000,000 a second time, and at the end of the second day it has got $3,000,000 of assets, $2,000,000 in promissory notes and $1,000,000 in cash. As against the cash of $1,000,000, it has demand deposits. So that it has only a 50-percent cash reserve.

The third day it lends out that $1,000,000 a third time, and the fourth day the fourth time, and so on until after 10 days it has loaned it out 10 times. Then it has pyramided the former $1,000,000 ten times, $10,000,000 of demand liabilities, and all it has got against it is $11,000,000 of assets, $10,000,000 in promissory notes, and $1,000,000 in cash.

Now, during that process, it has created $9,000,000 which did not exist before, of circulating medium. There were only $1,000,000 before this bank was started, and now there are $10,000,000. Then when it reverses the thing and liquidates, it reduces that from $10,000,000 to $9,000,000, $8,000,000, and so forth, until it goes out of existence entirely, and destroys the whole $9,000,000. The bank is always creating money when it is lending, and destroying money when it is getting paid. In normal times these two offset each other. Just about as much is created as is destroyed. But there will come times when the equality is badly broken, and when that happens you have got either a boom or a depression.

It is all due to the fact that the bank is pyramiding. It is lending its money out more than once. Some of you may have seen in the paper recently an article by Walter Spahr, professor of banking of the University of New York, in which he tried to show that Father Coughlin, when he stated something about this pyramiding, did not know anything about banking because the individual bank does not pyramid this way because 80 percent of each cash deposit goes into other banks. That is, other banks pull out 80 percent of the cash which is deposited in an individual bank. So that, actually, it only lends out a little more than the actual cash it receives instead of lending 10 times that cash. That is true of the individual bank in a country like the United States, where we have got 15,000 banks. But what should be made clear is that all of this 80 percent is treated in the same way by the other banks as the original deposit; so that, for the system as a whole, you do have this pyramiding. I say this because if I do not, some of you may read that article and say, "Fisher did not know what he was talking about."

If you had only one bank in the country, what I said about pyramiding would be literally true. And when you have 15,000 banks, it is still true of the entire 15,000, but not of any individual one. The individual banker does not know what he is doing. The individual banker thinks, when he gets a cash deposit of $1,000 he can lend out about that amount. However, other banks do——

Mr. Brown of Michigan (interposing). In each instance, Doctor, of the additional successive loan the bank has received, if it is a sound banking institution properly run and conducted, it has received either security for the additional $1,000,000, or it has received a statement which shows that the borrower is in sound condition.

Dr. Fisher. Yes; but it is not a matter of individual soundness that I am talking about. That is a part of the picture, when you get into a very acute situation.

Mr. Brown of Michigan. What I am saying refers back to the law of supply and demand, which a great many people seem to want to repeal; why we have a situation there, where the needs of the borrowers from that bank are met by what amounts to sufficient or adequate security for those loans, and the current needs of that particular community are met in just the way you have outlined, although I think your case is somewhat extreme.

Dr. Fisher. So far as security and safety are concerned, you are quite right. All of the arguments I have given against the present system can be fairly well met by such methods as you have suggested, so far as giving security or safety to the individual is concerned, but you will still have this problem of fluctuating deposits all the time.

Mr. Brown of Michigan. I am talking about the same thing you are. I am referring back as to how the bank can meet the demands of this depositor when that demand comes. And I say it could meet it by turning over to the Federal Reserve banks, assuming, of course, that there is security rather than statements of the bank of these loans, by turning over to the Federal Reserve banks the securities it has back of its deposits, and getting from the Federal Reserve banks, under this additional section 13 which Governor Eccles proposes, additional funds to meet the demand of depositors.

Dr. Fisher. That would help, and it would cushion it, as I say, but the time would sometime come when the Federal Reserve itself would need cash; that is, its cash reserve was so near the limit that they would not extend the credit, which you would like to have them extend.

Mr. Brown of Michigan. The time has come, then, in our little business venture when inflation to too great a degree has taken place, inflation of credit money?

Dr. Fisher. Yes. That is what I am talking about.

Mr. Brown of Michigan. It has gone probably too far. I think perhaps it is healthy that it, then, should be stopped.

Dr. Fisher. Yes; but it is far easier to stop it if you do not have your expansion and contraction of reserve. This is the same principle to which I just referred, where the individual bank creates $10,000,000 of circulating medium where $1,000,000 existed before.

Mr. Brown of Michigan. I won't interrupt you further.

Dr. Fisher. The same thing applies to the Federal Reserve, which creates $3 where $1 existed before, and they can contract and expand in the same way.

Mr. Ford. One other question I would like to ask. You say a 100-percent reserve. We will take this same bank with $500,000 demand deposits. In order to meet your plan that bank would have to have, we will say, in Government bonds $500,000 to match that. Would not that require that a bank would have to take certain steps? How would you get that? By additional capital and surplus, or how would they have that money to put up?

Dr. Fisher. You would get it from the Government through the Federal monetary authority or the Federal Reserve Board, or whatever is your apparatus which you put in this bill, buying the bonds, United States bonds, of the banks with cash or credit.

Mr. Ford. But every dollar of deposits which the bank takes it has to have another dollar which is commensurate?

Dr. Fisher. Yes, sir; that is true. I was proposing, with Mr. Hemphill, to make the transition easier, to let the Government bonds stay, as is, in the bank, making part of your reserve, but ultimately as maturities are reached they would be replaced by actual cash, while what we call "credit" of the Government, or the Federal Reserve bank, so that you would have a 100-percent reserve then of actual cash.

Mr. FORD. Then if I organize a bank and I am planning on building up my deposits to $500,000, as fast as those deposits come in I have got to put up in a reserve, dollar for dollar with it?

Dr. FISHER. Yes.

Mr. FORD. That is, of my demand deposits?

Dr. FISHER. Yes.

Mr. FORD. Bonds.

Dr. FISHER. Yes. Of course, as has been pointed out, the bank would lose, or would have a dead asset, as they call it, this money not earning interest, in place of an earning asset, and that would have to be provided for to see that they were not made worse off in respect of profits by this substitution. That can be done and that can all be provided for in any of several different ways.

Mr. FORD. The Government bonds would give a little.

Dr. FISHER. Yes; as long as they were there, but ultimately they would be replaced by actual cash, in which case the banks would lose about $300,000,000 a year of interest on bonds, which they would have to make up in other ways. That is a detail which I will go into now, if you like.

The CHAIRMAN. Presumably the Government will pay off its bonds sometime.

Dr. FISHER. Yes.

Mr. HANCOCK. Doctor, on that point, how long have you been criticizing the fractional reserve system?

Dr. FISHER. Only about a year. I was stimulated to it partly by Mr. Goldsborough asking me if it was not possible to get up a system by which the money of this country could be created and controlled without somebody having to go into debt to create it. And then I discovered that a memorandum on the subject had been prepared at the University of Chicago by a half dozen economists there, and, putting my own thoughts and theirs together, I became aware of the fact that the original system of banking used by the Bank of Amsterdam 300 years ago is the only real sound system of banking.

Mr. HANCOCK. Doctor, do I understand that you thought that the system in 1929 or the spring of 1929 was unsound?

Dr. FISHER. To a certain extent; yes.

Mr. HANCOCK. Did you not make a statement back in 1929, when we were at the peak of credit expansion, that there was nothing dangerous or unsound about it?

Dr. FISHER. No; I think I was the first one, probably, to predict that we were going to have a recession. That was in the first week of September 1929. And I said, and in that respect I was wrong, that I thought it would be a mild recession. I thought it was only going to be in the stock market. The reason, or a reason why, it was much more severe and continued into the commodity market was that Governor Strong had died and his policies died with him, as I had told him I feared they would. When I said that to him, he said, "No; they won't because there are men, especially in my bank, who will continue it."

His successor did endeavor to do so, but without the degree of success of Governor Strong. I have always believed, if he had lived, we would have had a different situation.

Mr. HANCOCK. I was under the impression that certain administration leaders at that time used your prophecy to allay fear and unrest in the minds of the public.

Dr. FISHER. Yes; I believe, as I have stated earlier today, that the most of the depression could have been prevented if the right policy had been pursued at that time.

Mr. BROWN of Michigan. Dr. Fisher, there are several New York and Chicago bankers who, in the spring of 1929, advised the slowing up in speculation and the raising of the rediscount rate.

Dr. FISHER. Yes; they were right, and the Federal Reserve Board would not do it.

Mr. BROWN of Michigan. Others had the same thought earlier.

Dr. FISHER. The Federal Reserve Board would not allow them to do it. It is also true, I think, that Governor Strong's death was hastened; he was ill at the time at Atlantic City—realizing his policies were not being pursued. He paced the floor, wishing that he had control again.

Mr. HANCOCK. You did not warn about it, Doctor, until after it was here?

Dr. FISHER. That is nearly true. I did not think there was much danger. I merely said there would be a recession in the stock market.

Mr. BROWN of Michigan. To be fair to Dr. Fisher, the stock-market recession did not occur until after September.

Dr. FISHER. That was the worst.

Mr. HANCOCK. It began in September, and we had a very noticeable decline in September.

Dr. FISHER. Yes.

The CHAIRMAN. Doctor, Governor Strong, to whom you referred, of course, was the governor of the New York Federal Reserve Bank?

Dr. FISHER. Yes.

The CHAIRMAN. One of the 12 regional reserve banks?

Dr. FISHER. Yes.

The CHAIRMAN. And his operations were conducted entirely by him and independently?

Dr. FISHER. Not exactly. He formed what he called an "open-market committee", consisting of himself and the governors of the Federal Reserve Banks of Boston, Philadelphia, Chicago, and Cleveland.

The CHAIRMAN. But, as a matter of fact, that was really Governor Strong, and it died when he died, as you said.

Dr. FISHER. Yes.

The CHAIRMAN. With some method of concentrating the authority for such action as he took, and controlling it, it would be possible to have a repetition of that control by one bank, and it might be employed in either direction?

Dr. FISHER. Yes.

Mr. HANCOCK. Doctor, I did not mean to be criticizing you at all, but I just wanted to get the facts about it so that I might be able to judge.

Dr. FISHER. I am not at all hurt. I have been very much lambasted about what I said or failed to say, and, to a certain extent, doubtless deserved it, though I could make many excuses.

Mr. Cross. Let me ask you about something which I think is practical, and which we want to get at. I am one of those who are convinced that we ought to put a goal for the Federal Reserve Board to go to and hold everybody to that price level and stay there. Now, what are your views about that?

Dr. Fisher. I think the price level of 1926 is as good as you can get, if you are going to go on the basis of the price level.

Mr. Cross. All right. Now, assume that we do that. The testimony here by Governor Eccles and apparently by the testimony of Governor Strong and Dr. Miller and others who have testified in years gone is that they have no question but what they can pull inflation down, but they are lost when it goes to lifting a depression up. How can we get to that price level under this bill?

Dr. Fisher. You can make absolutely sure of it if you introduce the 100-percent reserve.

If you do not introduce the 100-percent reserve, you have got now a great deal of slack between your 10-percent reserve and your excess reserve, which slack makes the danger. It paralyzes us with fear and we do not dare increase it for fear of the still greater danger of inflation that increase would cause.

Mr. Cross. Doctor, is it not then a fact that your suggestion would tend to do away with the banks manufacturing "moonshine" money or "phantom" money?

Dr. Fisher. Yes.

Mr. Cross. What would be the effect of this kind of a situation: Suppose we had an agency, whether you call it a monetary authority, Federal Reserve System, or what not, that had nothing to do with banking, but whose business it was to issue money and to seek a price level, the banks go ahead and do their own banking and run their own affairs, but the business of this body or agency is to see that money is put out. The question, of course, is, How can you get it in circulation? But if you would pay all your civil-service employees, Army and Navy pay, offer your bonds as they fall due, necessarily call in bonds until the purchasing power of the dollar diminishes or the price level rises until you get to 1926, could such a body function and could such a body accomplish that purpose in that way?

Dr. Fisher. Without the shadow of a doubt.

Mr. Cross. Why should the body whose duty it is to the people of these United States to supply them with an adequate means of exchange, why should they be tied up to some banking outfit? Why should not they be independent of that and let the banking system be a different propostion, and this body or agency see that the country was furnished with an adequate means of exchange and the price level is kept or the purchasing power of the dollar kept stable?

Dr. Fisher. That is exactly the object of the proposal that I am advocating and that Mr. Hemphill advocated this morning. That exactly expresses it. The monetary authority would issue money or credit—it does not need to be printed—in exchange for Government bonds, and it could reverse that process and get back money by reissuing bonds, so that it would have, through the open-market operations, a two-way arrangement. It can expand or contract.

I would like to say, in reference to those ideas which you quoted from earlier testimony of Governor Strong and others, that I would like to point out what Sweden has done. Sweden has, beginning with September 1931, actually accomplished what we stabilizers have been talking about for 20 years. She has done it partly because she has a unified banking system. She has kept the price level the same as it was in 1931, when she started, within 1¾ percent at the utmost. It has been once 1¾ percent above that price level and once 1¾ percent below. Ordinarily it did not reach 1 percent above or below. It has kept thus near the mark for 3½ years, week after week, without a single miss.

I get the reports every week from Governor Rooth, of the Riksbank, who is doing this thing. This bill which you are presenting ought to be able to bring about in the American case what Governor Rooth is doing in Sweden in the Swedish case.

I have here the information on the figures beginning with August 4 last. I have them at home all the way back to September 1931.

Mr. HANCOCK. Professor, at that point, do they require in Sweden a 100-percent reserve?

Dr. FISHER. No; you could do this, if you have a sufficiently unified banking system, and succeed without the 100 percent.

Mr. HANCOCK. May I ask on that point, to get my own mind clear: How much money would be available today if we required 100-percent reserve?

Dr. FISHER. I do not believe I understand your question. How much available? The Government would issue money.

Mr. HANCOCK. It is a complicated subject to me, but I am wondering if you require 100-percent reserves, how much money it would take?

Dr. FISHER. How much money would be required?

Mr. HANCOCK. How much money would be required.

Dr. FISHER. Yes. I think Mr. Hemphill is right. We ought to have something like $250 per capita, counting check-book money. He did not mean that that should be all the money that people would be carrying now in their pockets. It would be check-book money and pocketbook money, but the check-book money would have a 100-percent reserve behind it.

Mr. HANCOCK. What would that amount to, about thirty billions?

Dr. FISHER. About forty billions, I think.

Now, may I read the figures? They are rather monotonous but beginning with the week ending August 4, the price level according to the official index number which Sweden has adopted, which is an index-price retail, cost of living, and not wholesale price——

Mr. CROSS. How did they arrive at that? What did they use in getting the price level, the index?

Dr. FISHER. Prices of food and clothing and rent, and other things that they have sufficient records of.

Mr. HANCOCK. Wholesale or retail?

Dr. FISHER. Retail cost of living.

Beginning with the week ending August 4, the index number was 99.4 that week, that is, six-tenths of 1 percent below the established normal, or a little over one-half percent. The next week, ending August 11, 1934, it was 99.4 also. Next it was 99.4, next 99.6, next 99.6, 99.4, 99.2, 99.1, 99.0; it was then 1 percent away. That is a maximum in the whole list of what the figures happen to be before me.

No; I beg your pardon. It got down to 98.9, 1.1 percent. In two cases the deviation from par exceeded 1 percent. Then it was 99.2, 99.4, 99.5, 99.6, 99.6, 99.6, 99.6, 99.6, 99.8, 99.8, 99.9, 99.9, 99.9, 100.0, 100.0, 100.1, 100.1, 100.0, 100.0, 100.0. The last figure I have here is for the week ending March 2.

The CHAIRMAN. For how long a period do these figures apply?

Dr. FISHER. These go back to August 4, 1934.

The CHAIRMAN. How long have they had this in effect?

Dr. FISHER. Since September 1931, 3½ years. That is about 150 weeks. It is like a man shooting at a target and hitting the bullseye 150 times in succession, without a miss.

Mr. WILLIAMS. What is the condition of their employment over there?

Dr. FISHER. It has improved.

Mr. WILLIAMS. Has it varied in any respect with respect to the problem of unemployment, or remained on an ordinary level?

Dr. FISHER. No; in September 1931 the whole world was going down hill, you will remember, and Sweden went down hill and continued to go slightly down hill for a year or more after that, but not as fast as the rest of the world. According to the data of the League of Nations, they have recovered faster than any other country in Europe. At first the trouble was because of their foreign trade being so important, the prices at wholesale of foreign goods went up and the prices of domestic goods went down, which, of course, was a discouraging thing to the home producer. There were many who were trying to criticize the stabilization idea, who rushed into print, among them Rufus Tucker, of New York, to prove that the Swedish system was a failure, but scarcely had the words got out of their mouths when that situation began to rectify itself.

If you look at the charts which I have here in my book on Stable Money, on pages 326 and 327, and contrast Sweden with the United States during that period, you will see that even the wholesale price level in Sweden was what we would call stable in this country. We have scarcely ever had as great stability as that, even in the early period. It is almost a miracle that Sweden, in spite of the fact that a large part of her trade is foreign trade, and while they had the Kreuger trouble in Sweden, which affected almost every business man in Sweden, nevertheless, succeeded in getting what they were aiming at. The lesson is twofold. You are interested to know whether Sweden was helped. It was helped greatly. That is true, and that is the important thing, but the most conclusive lesson from this is that a nation can stabilize.

Governor Strong and others, as you were saying, said we could not do it, but Sweden is doing it.

Mr. WOLCOTT. You stabilized prices, but did you stabilize employment?

Dr. FISHER. They are getting out faster than any other country.

Mr. WOLCOTT. But that does not carry them out of the depression.

Dr. FISHER. Not entirely.

Mr. WILLIAMS. That is the question I was driving at. Were they able to stabilize employment?

Dr. FISHER. Sweden made this mistake:

Sweden did not have the other part of the twofold program of President Roosevelt. You should have not only stabilization of prices, but first of all, reflation. There should be a corrective upturn. Sweden learned it afterward. They did not try to reflate, because they had the same fear against inflation that we have had, only worse. Europe had had such a terrible result from the inflation of the war, that they were afraid of what they called "inflation", and they would not permit any reflation. In order to prevent that, they put up the Riksbank rate to 8 percent, by successive jumps, to prevent the rise in the price level which they were afraid of when they were on gold in September 1931. If they had permitted, as they should have, a reflation—enough to carry them back to the price level of 1926—instead of galvanizing the price level of 1931, which was abnormally low, they would have gotten out of the depression in a few weeks instead of having to wait a year or more.

Mr. WILLIAMS. Of course, the stabilizing of the price level is not the only objective. There are other things in it.

Dr. FISHER. Yes; but, as Mr. Hemphill said, that is the big problem.

Mr. WILLIAMS. We have here before us in this hearing, that while England finally stabilized the price level during the period 1929 to 1934, that there has been great variation in the unemployment situation, and the conclusion was reached that there was very little relation between the two.

Dr. FISHER. There is a very strong relation between the two.

In this article which I hand you, and which you can hand back, it is covered. I have another copy here. I would like to show you another chart which shows how employment is related to changes in the price level. This chart was made for the United States. There is the employment in the United States, and here is the effect of changes and the price level [indicating on chart], so that if there had been no other influence, employment would have been, right there, on the theory that a rising price level increases employment, and a falling price level decreases employment. You see, the two curves correspond fairly well, those for this period and those for that period [indicating].

Mr. WILLIAMS. For what period?

Dr. FISHER. That is from 1919 to 1933, the last one, and this is 1903 to 1918.

Mr. WILLIAMS. You say during the period from 1903 to 1918, and from 1919 to 1933?

Dr. FISHER. It is the same thing continued.

Mr. WILLIAMS. There is a very close relation between the price level and employment?

Dr. FISHER. That is between changes in the price level, with a lag. There is quite a lot of mathematics in that, which you probably do not want me to go into, but whenever there is inflation, it stimulates employment, and whenever there is deflation it causes a reduction in employment, because it cuts down profit, and when you cut down profits people close up shop.

Mr. WILLIAMS. I was wondering what is your explanation of the chart which we have here, and I do not know whether you saw it, but it was presented by Dr. Goldenweiser and Governor Eccles, about the English situation from 1929 to 1934, and it made a rather strong impression on me, I say, because it showed or seemed to show that there was very little relation between the price level and the question of unemployment.

Dr. FISHER. The relation does not show very clearly, unless you provide for a lag and a distributed lag. That is, the effect of an increase in the price level upon one amount or another does not occur until later, and the effect does not come all at once. It does not all come 6 months from now, but part of it begins in 1 month, a somewhat larger part in 2 months, and so on, and you have got to make an elaborate calculation.

Mr. WILLIAMS. The period which they presented, as I recall it, in round numbers, covered a period of 6 years, covering unemployment from 2,000,000 to 2,900,000, while the price level ranged only from 66 to 72. For that reason it seemed to show that there was not any relation between the two.

Dr. FISHER. There is no question that there is a relation, both in England and the United States. This is the relation as far as business is concerned [indicating on chart]. You will notice "T" representing the volume of trade, and that figure representing the changes in the effect of the price level corresponds even better than the employment curve.

Mr. WILLIAMS. What are you talking about, Doctor; is that ours?

Dr. FISHER. Yes; the United States. Between 1919 up through 1933, into the beginning of 1934, when this was done, you will find a strong relationship between the anticipated effect, with a distributed lag of the changes in the price level, calculated by the methods that I said would require a good deal of mathematics, and compared with the volume of trade. You will find that they correspond very well.

Here is the corresponding thing for England, and there is a fairly good correspondence, there, although the statistics are not so significant. I have no corresponding figures for employment.

Mr. CROSS. Doctor, I did not quite get through. In the beginning, in the fight for a stabilized dollar, the Federal Reserve Board and the members were practically all against that theory, were they not?

Dr. FISHER. Yes.

Mr. CROSS. After that they began gradually to come in that direction?

Dr. FISHER. Yes.

Mr. CROSS. Now, Dr. Sprague, for instance, testifying in 1928 said:

> I see an advantage from the passage of the bill—

I believe that was the Strong bill—

> and I heartily agree with you, that the difficulties in the Federal Reserve System are not so much in past errors of judgment that they have made, but, rather, in the hasty manner in which at times policies have been decided upon and then executed. I have reached the conclusion that a stabilization amendment might prove serviceable.

Originally he fought those ideas. Dr. Miller, testifying——

Mr. BROWN of Michigan. Have you stated whose book you are reading from?

Mr. CROSS. This happens to be Dr. Fisher's book, but these are the quotations from the testimony of these hearings. Besides, I would just as soon take his testimony.

Mr. WOLCOTT. Do you recall Professor Sprague's testimony in that respect last year?

Mr. CROSS. Last year? We had him here with reference to going off the gold standard and deflation, but I don't know whether we had him on the stabilization problem or not. He surprised me very much, saying in that hearing, that he thought the only thing for us to do was to get off the gold standard, and then he issued a very strong statement the other way, when he left the Treasury Department. Thereupon, I lost any faith in Dr. Sprague.

Mr. WOLCOTT. My surprise is that you are quoting from Professor Sprague as to his views, because I thought you did not place much reliance on what Mr. Sprague said.

Mr. CROSS. No; I did not, and I do not now.

Dr. Miller, testifying in 1930, said:

> It is my opinion, expressed several times in discussions at Federal Reserve meetings in the open months of 1929 that the Federal Reserve System was drifting, that it was in the midst of a perilous situation without a goal.

They had no goal to go to, they were floundering. That is one of the reasons I am convinced we should have in this bill, something for them to go to and stay to.

To the same effect, Mr. Russell Leffingwell, connected with the Treasury for awhile under President Wilson, said:

> The system has been unable to evolve properly and persist in an effective policy to counteract the deflation of the last 3 years. A deflationary policy has found only hesitant and tardy and intermittent expression and action. In the matter of monetary matters, the control of inflation and deflation, a step in time is worth nine.

All of which shows the necessity for having a goal for whatever agency is set up to go to and work to. To jump one way a while and jump the other is not satisfactory. They go out here and buy bonds and sell bonds, and when Governor Harrison came down here and saw the situation and wanted the Board to raise the rediscount rates, you will remember they would not do it. Finally they did do it but it was too late. As a result, the storm was coming, and they were too late. They would not let him do it.

I think we should put up our goal to go to.

Mr. SPENCE. Dr. Fisher, as a practical matter, how would you regard that policy in the law? Would you state the definite objectives to be obtained and the means by which they should be obtained?

Dr. FISHER. Yes, sir.

Mr. SPENCE. Have you formulated any idea as to how it should be worked?

Dr. FISHER. I would not assume to be a bill drafter, but I have made a memorandum several times, including one in this forthcoming book, on the 100-percent plan, and chapter II is entirely on that subject.

Mr. SPENCE. Is there any way that it could be made which would do away with the whole equasion?

Dr. FISHER. Yes; you could do away with the whole management of currency if you are willing to accept a less degree of stabilization than Sweden has achieved. All you would need to do would be to decree that we should increase our per capita circulation until it reached $250, or whatever you decided on, and then keep it there. That is really what was proposed by these—or substantially what was proposed by these economists at Chicago. Personally, I would prefer to have some discretion enter in order to get a higher degree of stabilization. This is like running your automobile with a robot instead of with a chauffeur. I would rather have a chauffeur and give him a little discretion, although he would be told where he is to go.

May I continue, Mr. Chairman?

The CHAIRMAN. Yes; you may proceed.

Dr. FISHER. I have not finished my statement.

I did want to quote from Mr. Gregory, of this bank in St. Louis to which I referred, who has written an article on this 100-percent plan in the Mid-Continent Banker, "Pay your debt, Mr. Banker", by which he means that the bankers ought to do some thinking on this subject, and to contribute to it—have their profession contribute to its solution; and he has tried to do it for them. This is the last sentence:

> If we cannot develop an enlightened opinion among ourselves—

Meaning bankers—

> that will assist the rest of the business world to a better solution to our problem, then may the red and black devils of alternating inflation and liquidation toss us quickly into the consuming fires of Government ownership.

I believe that the 100-percent plan, or decreeing that plan, will produce stable money—and that is the quickest and best way—I believe that is necessary if we are to prevent socialism, to Russianize this country, maintaining our American system of individualism and individual initiative.

This 100-percent plan is the only plan that would absolutely separate the control of money from banking. There would then be no need to have many, if any, banking laws. Presently you could repeal almost all the banking regulations if you would extricate from the bankers these deposits subject to check, which are a form of money which the bank issues, contrary to the Constitution of the United States—and destroys from time to time—thereby creating booms and depressions.

Mr. WILLIAMS. Here is a question I would like to ask you, Doctor. You have gone over several times about the 100-percent reserve.

Dr. FISHER. Yes, sir.

Mr. WILLIAMS. Do I understand you to mean that for every deposit account subject to check, for every dollar, that you must have 100 cents in money, cash, currency?

Dr. FISHER. Yes; in effect. Federal Reserve or Government credit which can be turned into money, by having the money printed as needed. As a matter of fact, you would not need as much actual money as you do now. As long as all the money was in the bank or could be made to order few would ever ask for it.

Mr. WILLIAMS. That would mean Government bonds could be turned into money.

Dr. FISHER. No; I did not mean that. I meant money in existence or which could be brought into existence. Government bonds could temporarily be a part of the reserve. I proposed that simply in order to make the transition easy.

Mr. WILLIAMS. As a matter of fact, how much money in actual currency do you think it would require to carry that on?

Dr. FISHER. There would not be any distinction then between the money in the bank and the money in your pocket, except as the individual wanted to change its location from bank to pocket or from pocket to bank; but he would want to keep on deposit just about nine-tenths of his money, as now; that is, out of the $250 he would probably deposit $220.

Mr. WILLIAMS. And that would take about $40,000,000,000?

Dr. FISHER. Counting the deposit money, about $35,000,000,000.

Mr. WILLIAMS. Then in order to place this country on a sound, stable basis, from a monetary standpoint, we should have actually in existence about that much in currency?

Dr. FISHER. In currency? No. It would mostly be on deposit. It would not be currency in the pocket. It would be the equivalent of currency in the banks; yes.

Mr. WILLIAMS. What is the difference between that and what we have now? We have deposit credit now.

Dr. FISHER. Yes; but the banks can control the amount of it. We want to take that control from the banks, because the banks do not now control it in any central way. If they are going to control it, then you ought to have a committee of the American Bankers' Association, or someone, do it. But if you are going to let 15,000 banks independently function, some creating and some destroying, sometimes engaged in creation or sometimes in destruction, you are going to have booms and depressions.

Mr. BROWN of Michigan. They cannot create it, Doctor, unless somebody comes into their bank and becomes indebted to the bank, can they? They can only create it on a demand for the money.

Dr. FISHER. They can create it on their own initiative, to a large extent, and they can destroy it on their own initiative still more.

Mr. BROWN of Michigan. Not unless someone wants to borrow money from the bank.

Dr. FISHER. Take it the other way: The destruction consists merely in saying you must pay.

Mr. WILLIAMS. I am not able to see the difference, as Mr. Brown says. As I see it, when a man comes in and asks for credit at a bank he wants to borrow money.

Dr. FISHER. Yes.

Mr. WILLIAMS. And you place to his credit so much money, whether you hand him out the cash and he hands it back to you.

Dr. FISHER. If a man comes to me and asks for money, I do not create it. The banks should be the same way.

Mr. WILLIAMS. In other words, you would have to have as much currency as you have credit?

Dr. FISHER. A banker could lend under the 100-percent system his capital.

Mr. WILLIAMS. Yes, sir; his capital.

Dr. FISHER. His capital could be lent. He could lend whatever is deposited with him, for that purpose, in the savings account, which we call "deposit" but which it really investment; he could relend what was left to him from previous loans. There would be these three sources for the loan of funds. It would amount to this: The loans would be made out of savings, where they should be made, and not out of thin air. A banker ought not to be allowed to manufacture the money that he loans any more than individuals should.

Mr. WILLIAMS. You would not confine those loans to any particular feature out of savings accounts? You would not differentiate between investments and ordinary commercial banking?

Dr. FISHER. I make a very big distinction between deposit banking—I mean check banking—and time or savings banking. Savings banking is mere money lending without any money creation; but commercial banking is both money lending and money creation.

Mr. WILLIAMS. In lending the savings account or the time deposit, the bankers can lend out of that, you say?

Dr. FISHER. Yes, sir.

Mr. WILLIAMS. That is legitimate?

Dr. FISHER. Yes, sir.

Mr. WILLIAMS. On what kind of loans? Any kind?

Dr. FISHER. That is a matter for banking practice.

Mr. WILLIAMS. What is your theory in making a difference in the character of a loan which he could make on that?

Dr. FISHER. My theory has nothing to do with it.

Mr. WILLIAMS. I am asking your view of that.

Dr. FISHER. I am not a banking expert.

Mr. WILLIAMS. You do not know any distinction, then, between the character of the loans which he might make or ought to make?

Dr. FISHER. I think it could largely be left to the bankers. The banker knows more about it than the Government.

Mr. WILLIAMS. That is what I am saying. There ought to be no distinction made as to the kind of loans he would make out of the savings deposits?

Dr. FISHER. I do not know. I do not know enough about money lending, which is real banking, to have much of an opinion, except this: I am satisfied that if you once had money disentangled from banking, and let the Government stabilize the money, and they had a dollar which was stabilized in purchasing power, you could let the banker have much more freedom than he has now.

The only thing that I want to take away from the bankers, the only thing I am trying to take away from the bankers, is their power to create money and their power to destroy money. Let them handle money, that somebody gives him to lend, but do not let him create money.

Mr. WILLIAMS. I am very much interested on that subject of prices. I do not see any difference between that and the system we have now.

Dr. FISHER. Now he lends the reserve 10 times over. You cannot lend me $100, if you have only got $10 to lend me.

Mr. WILLIAMS. You would not carry the loans 10 times, would you?

Dr. FISHER. No; the existing loans can be taken care of simply by buying the bonds that are now outstanding behind those loans, the United States paying for those in noninterest bearing money or credit.

Mr. WILLIAMS. And the money going into the bank?

Dr. FISHER. Yes.

Mr. WILLIAMS. Then I come back to the question: Then you would have in the banks of the country, in the vaults of the banks, all your currency handed out back and forth in the transaction of business.

Dr. FISHER. It would be available; yes. It would not need to be printed, for it would not be used as much as it is now. Anybody knowing that he could get 100 cents on the dollar, no matter if every other depositor demands his, at the same time would not demand much, if any.

Mr. BROWN of Michigan. Of course, under the Steagall amendment to the Banking Act of 1933, the right to issue that money on assets of the bank, both Federal Reserve and non-Federal Reserve banks, exists.

Dr. FISHER. That is a step in the same direction. Federal Reserve bank notes, you mean; is that right?

Mr. BROWN of Michigan. Yes, sir.

Mr. WOLCOTT. Dr. Fisher, as I understood Mr. Hemphill this morning, he advocated the repeal of the Federal Reserve Banking Act and National Banking Act, and turn the banks back to State supervision, if I understood him correctly. How would the Federal Government, if that was done, control the situation and require the banks of the country to maintain this?

Dr. FISHER. He did not mean that you would turn back to the States the control of deposits subject to check. That would be taken care of, because that is money. The control of deposits subject to check should go with the Federal Government.

Mr. WOLCOTT. I will admit, Professor, that I may be dense, but I do not understand your 100-percent reserve proposition.

Dr. FISHER. I have not tried to go into it in detail, because I thought there were so many other things which I wanted to say, and I have said all this in the book to which I referred, and which I am going to send you next week.

Mr. WOLCOTT. I would be very much interested in it.

Dr. FISHER. It is really the simplest thing in the world. All we need to do is to have the monetary authority buy the bonds, or, if you want absolute money in the banks, to buy the bonds that are held by the banks, to a sufficient extent to provide them with a 100-percent reserve behind the checking accounts only, and require them to hold that. I mean always maintain 100 percent; never to lend any of that out, as the old goldsmiths did, when they betrayed their trust. We go back to the old goldsmith idea; that this is an actual deposit.

Mr. WOLCOTT. If I understand that correctly at this point, I understand you mean that in the old days the goldsmiths had an ounce of gold in thir safes for every receipt which they gave for the receipt of gold; so the banks should have cash and capital bonds in their vaults for every dollar of deposit?

Dr. FISHER. Yes; where it is a checking account.

Mr. WOLCOTT. Then that would necessitate a divorcement of time deposits from demand-deposit banking, and you would have to separate them?

Dr. FISHER. Separate them absolutely.

Mr. WOLCOTT. And keep them absolutely separated?

Dr. FISHER. Yes; so that the business of money lending——

Mr. WOLCOTT. I understand that that is directly contrary to this bill which we have before us, because Mr. Eccles, I think, voiced the impracticability of trying to separate commercial banking from savings banking, and showed us how difficult it was to do that in practice, although it looks easy to do in theory. How would you suggest that they do that? To set up separate institutions with separate capital bases?

Dr. FISHER. Yes, sir; and each bank that now has its deposits subject to check to incorporate separately the department that handles the deposits subject to check; and after it has gotten its 100-percent reserve, which you will get by the Government buying assets, if necessary—if it has not already got the 100-percent reserve—then it must maintain a 100-percent reserve, and that department is under the supervision of the Federal Government. What happens to the other department is an entirely different matter. The savings or loan department would then handle the short-term loans, now behind demand deposits, in addition to the long-term loans which they already handle, thus getting more liquidity than now.

Mr. WOLCOTT. Let me follow up that thought with one more question. As was suggested, that would make the banks practically a bailee, or practically a warehouse for deposits?

Dr. FISHER. Yes.

Mr. WOLCOTT. What means are you providing for reimbursing the banks for servicing the accounts?

Dr. FISHER. The simplest way is by a service charge for checking. That is being done today, and you only need to charge an average of $1 per month on each checking account, as Mr. Hemphill has shown, to get back all the $300,000,000 a year that the banks are now getting from Government bonds, and half as much more.

Mr. WOLCOTT. I want to hurry through this. Do you not think that this might be somewhat deflationary, Professor? That is, to charge what is necessary to maintain that department to give me the service, it must be based upon the transaction basis, in other words, 5 cents a check or 10 cents a check, or whatever the charge would have to be to maintain the department. Is not there a tendency on the part of the public, which has been using these banks and paying by check, to go down to the bank and draw one check and send their wives around in the city to pay the bills?

Dr. FISHER. It is deflationary now under the partial system, but under the 100-percent system it would not be deflationary. The only effect it could have would be for the bank, if they chose, that is, the depositors, to take out their money and carry it in their pockets or deposit it somewhere else. But they could not destroy any money. Now they can destroy it.

Mr. WOLCOTT. In other words, where there would have been one transaction at the bank for 10 separate detailed transactions, they would have to use the money instead of checks.

Dr. FISHER. If the banks were not willing, or if the depositors were not willing to pay the service charges, or the banks were not willing to accommodate the public, as they do now, in the making of service charges, which were burdensome, it would make for more cash transactions instead of transactions by check.

Mr. WOLCOTT. Of course the banks could not maintain them without making some charge, other than through the earnings of the savings department, and that, of course, would not perhaps be correct, to ask my neighbor to have the interest which he would ordinarily draw from his savings account decreased to give me a service which is wholly divorced from any of his activities.

Dr. FISHER. The service charge would not be big. One dollar per month for each account would bring in 450 million to the banks, which is 50 percent more than they are getting now on the bonds which they have—$1 a month.

Mr. WOLCOTT. I will tell you why I think it is deflationary. I had a case called to my attention just the other day, where the Treasury Association, instead of drawing 10 checks in this city, where the charge is 5 cents a check, or something like that, went around and drew one check and paid in cash, to save the association a matter of 40 or 50 cents. Of course, he drew one check. That was one transaction.

Dr. FISHER. Yes.

Mr. WOLCOTT. That turned over just once. Whereas, we have been striving here to create a situation where that money would turn over as many times as it would be considered desirable.

Dr. FISHER. It is slightly deflationary now, because every time that is done, if it results in permanently putting $1 in the pocket, which used to be in the bank as a deposit, subject to check, it causes a shrinkage of $10, subject to check, in the country as a whole, so that there is $9 of deflation there, but, under the 100-percent system, that would not be true. You would just simply have your money in the pocket instead of in the bank vault, putting in one storing place instead of the other.

Mr. WOLCOTT. Do you explain that in your book?

Dr. FISHER. Yes, sir; but besides that there are two other answers. One is that the monetary authority would not only buy bonds of the banks, but, in order to bring about the reflation, it would buy bonds of the public, so as to increase the circulating medium, and if there were any deflationary tendency, such as you described, if there were any, it would be overcome by that process. In other words, the whole thing is in the control of the monetary commission.

Another answer is——

Mr. WOLCOTT. Just a minute, you used the term "deflationary." That, of course, gets us into the realm here of the question of relativity between the volume of currency and the price commodity index. You remember, Professor, we discussed that matter at length when we had the monetary authority question before us last year. My memory is that many of the economists found no relationship, or very little relationship, between the volume of money and the price commodity index. They claimed that the velocity of money and credit controlled it.

Dr. FISHER. There is a very close relationship.

Mr. WOLCOTT. Why I brought up that, in this respect, is that if we decrease the velocity, the turn-over of credit, currency, or bank check currency, it would not seem to make much difference, according, perhaps not to the weight of authority, but according to the opinion of many economists, what the volume was, if we decreased the velocity.

Dr. FISHER. As a matter of fact, velocity does not change very much except in the speculative field, and except where you have booms and depressions, and if you would not have so violent booms and depressions under any system of stabilization, the variation would be still less under the 100-percent system, and it is now probably not over 10 or 20 percent from the average.

But I want to say this: There are other methods of treating this reimbursement of the banks besides this method of a service charge. There are four or five different methods, discussed in my book, which I have gathered from bankers and all. And of all I find the bankers apparently like the service charge better than the others. I have been feeling somewhat as you do, that we wanted to encourage the maintenance of checking accounts, I won't say to avoid deflation, but to make it safer to keep things in the bank instead of in your pocket, and to put a premium on that. They generally do not seem to think this is necessary. The service charge will be so small, just think of it, an average of $1 a month for all accounts, including those that have millions, and it would be very easy to charge for the big accounts only, or in such a way as to reimburse the bank sufficiently for that.

There are several other ways of doing it.

Mr. BROWN of Michigan. Mr. Chairman, how long are we going to continue?

The CHAIRMAN. I had hoped to finish with Dr. Fisher. He only had a chance to be with us today, and for that reason we started the hearings today.

Mr. BROWN of Michigan. We have not heard Professor Fisher on the plan of issuing the money. It seems to me that that is the most important factor in the case.

Dr. FISHER. I have been interrupted, Mr. Chairman.

Mr. CROSS. I asked a question along that particular line, and I thought you answered my question.

Dr. FISHER. Yes.

Mr. RUSSELL. May I ask one question?

The CHAIRMAN. Yes.

Dr. FISHER. Before you ask that question, may I go ahead a little bit further with this matter of reimbursing the banks? This is the one problem, the best solution of which would require certain study, and for that purpose, Mr. Hemphill suggests that in order to put this into immediate effect, we allow the Government bonds to be counted as though they were cash reserve at first. Then, the banks would have as long as these bonds had not reached maturity, they would have $300,000,000 a year for that need, in the Government bonds. When they reached maturity, then they would be converted into cash and the reimbursement problem would come up.

In the meantime they could study this and the bankers could work out what is the best method, among the half dozen different methods I know about. It gives you leeway without stopping this legislation. This could be put into effect without any trouble. Talking about evolutionary methods, this is an evolutionary method.

Mr. RUSSELL. My question is this: Would not your 100-percent reserves greatly reduce the loaning facilities of the country?

Dr. FISHER. No; that appears to be the case and that is the question which is most often asked and raised as an objection: "Would it not make it more difficult to get loans?" On the contrary, by preventing the depressions which we have now, it would make loans always available. It has been hard during the depression to get loans. You have cases where it is impossible to get loans; whereas, under this system, it trots along all the time, and you will not get too many loans or too few, but you will have a normal supply and demand practically all the time.

Mr. RUSSELL. What money is available for a loan except the capital and surplus of the bank?

Dr. FISHER. I stated there are three sources. One is the capital of the bank; another is the money deposited in savings, which is the big thing.

Mr. RUSSELL. But you are going to divorce that from the checking account?

Dr. FISHER. Yes, but it exists, to get the loans there. Third is the funds which come in payment of old loans.

Mr. RUSSELL. But you have wiped out this, that is now available for loans.

Dr. FISHER. No.

Mr. RUSSELL. And you put nothing instead of it.

Dr. FISHER. You do not reduce any of the loans outstanding.

Mr. RUSSELL. As those are paid.

Dr. FISHER. As those loans are paid, they can be renewed or replaced out of the funds they pay them with. When Mr. Smith pays his debt, that money that he pays can be re-lent to Mr. Jones.

Mr. RUSSELL. I understand. That is based on the theory you now have a 100-percent reserve.

Dr. FISHER. Yes.

Mr. RUSSELL. But if the credit requirements of the country increased, there would be nothing available——

Dr. FISHER. That is where the monetary authority comes in. The monetary authority, with the growth of the country, in order to maintain the price level and prevent depression would find it necessary to issue more money or credit—you can call it either one of those, as there would be no difference now—more money, let us say, buying Government bonds to supply the needs of the Government. Or if you had the $250 per capita, and had no monetary authority, Congress merely prescribing that that would automatically increase with the increase in population. As I say, that would not be a very exact stabilization. Loans would take care of themselves, as they should, out of savings, for the most part.

The CHAIRMAN. Mr. Brown, did you wish to pursue your inquiry?

Mr. BROWN of Michigan. I do not recall Professor Fisher telling us how the money would be raised, but I do recall Mr. Hemphill stating how it would be. So that if you have the same idea he has, there is no use your repeating that.

Dr. FISHER. I have.

Mr. BROWN of Michigan. I would like to add as to what I said in questioning you as to the panic of 1929, this question: Is it not a fact, Dr. Fisher, that the Federal Reserve Board itself in 1929 issued a warning against excessive speculation?

Dr. FISHER. Yes.

Mr. BROWN of Michigan. In February 1929, which was some 7 months before the thing actually occurred?

Dr. FISHER. I do not remember the exact month. These verbal warnings were very disappointing in their results.

Mr. BROWN of Michigan. But they did, you might say, sense the fact that things were going bad?

Dr. FISHER. That was the weakness of the present system. You can warn banks all you like, but if the individual bank does not proceed to heed that warning, but issues money instead, it can do it under the present system. Under the 100-percent system it could not create a single dollar of more money.

There are four big arguments for this plan. One is the reduction of the Government debt, which is now frightening people. That could be practically wiped out. The second is the separation of money and banking, leaving the banker free.

Mr. BROWN of Michigan. It would be wiped out by the issue of cash in the form of printed money?

Dr. FISHER. Non-interest-bearing money of the United States. Third, it would prevent this menace of inflation which people are afraid of, both because of the Government debt or the fear that the Government will "go bust", and because of the banks having the power to inflate, a power which they might suddenly exercise at any time.

And, fourth, preventing further booms and depressions, which is the important thing.

I had a number of other minor matters, but I have taken so much time I think I can stop here.

Mr. WOLCOTT. Perhaps it is not apropos to what has been going on, but the Federal Reserve have been buying and selling and conducting open-market operations more or less voluntarily ever since their existence. What effect have those voluntary operations had?

Dr. FISHER. They have had a good effect. As long as you have not got a big storm to weather, it is easy to steer a ship, and Governor Strong succeeded in maintaining a good deal of stability during his lifetime, after he discovered the uses of open-market operations.

When the depression came, Mr. Hoover tried to do the same thing. Mr. Meyer, then Governor of the Federal Reserve Board, was not in sympathy with it. There was no law requiring any particular index number or price level, or anything of the sort, and it all rested on the value of individuals, and he balked at the idea, until the President dealt with him rather severely, and then there was at last the Steagall Act, passed February 27, 1932, in order to facilitate these open-market operations, to release a certain amount of gold, to make it free gold. When, finally, that was done, after a certain lag had normally occurred, we were really beginning to get out of the depression.

Mr. WOLCOTT. August 1932?

Dr. FISHER. Yes; and it is my opinion—and, of course, this is purely an opinion and I may be entirely wrong—but it is my opinion that if we did not happen to have what Mr. Wilson once called the "astronomical system of elections", by which we have an election after the earth has gone around the sun four times, irrespective of whether the political situation requires it or not, if it had not been that we had to have that election in the fall of 1932, I think we would have been out of the depression long ago.

When Mr. Hoover, very unwisely said, and Secretary Mills, that if he was not elected the grass would grow in the streets, and then when in September it became very clear from the election in Maine that Mr. Hoover was not going to be elected, people concluded, many millions of people concluded, that the grass was going to grow in the streets, and, therefore, they began to hoard, and finally began to hoard gold. And we had all these troubles until Mr. Roosevelt came in, and suddenly he created so much confidence that it was unhoarded to a certain extent, and we had improvement until all this mistaken N. R. A. and the A. A. A., and so forth, came in to retard recovery instead of treating it as a monetary problem.

That is, in brief, the history, and the open-market operations did work until they were stopped.

Mr. Wolcott. Do you think that those agencies have had the effect of destroying that influence?

Dr. Fisher. Yes; but it was not the destruction of the confidence, which is bad enough, but the destruction of wealth, plowing under cotton fields and lowering wheat acreage and paying people not to produce, making prices rise by making goods scarce, which is quite the opposite from making prices rise by making money abundant.

Mr. Wolcott. You believe in the prosperity of abundance rather than scarcity?

Dr. Fisher. Yes, sir; we never suffered from overproduction.

Mr. Brown of Michigan. Would not the money be less valuable in its purchasing power, if there was a plentitude of money?

Dr. Fisher. The dollar should be less valuable. It is too valuable now. The increase, according to wholesale value, was 81 percent between 1926 and March 1931.

Mr. Brown of Michigan. Which would have left us with a superabundance of a certain kind of goods, according to the law of supply and demand, and the price level would have been much lower.

Dr. Fisher. We want the price level to rise. The dollar had swollen, which means the price level had fallen, and to restore the dollar downward would mean to restore the price level upward.

Mr. Brown of Michigan. I do not think we want to get into a discussion of that kind, but I am one who believes it is wise to control production.

Dr. Fisher. I do not think so. This is a monetary problem, as Mr. Hemphill said, I think.

Mr. Cross. Mr. Chairman, I must go.

The Chairman. I think we are practically through.

Mr. Hemphill wanted to be heard 5 minutes in conclusion.

Mr. Hemphill. I was going to say this, Mr. Chairman: There are so few members of the committee present and I think this subject is so important, and sitting here listening to this discussion this afternoon I have gotten some sense of the confusion which exists in the minds of a great many of the members of the committee which could be cleared up.

The Chairman. Let me make a suggestion, Mr. Hemphill. You will have opportunity to correct your statement, and if you desire to add to it, the committee would be glad to have you do so, and it will be included in your statement.

Mr. Russell, do you want to ask Dr. Fisher a question?

Mr. RUSSELL. No. If it is not out of order, I was going to make the suggestion that it might be a nice thing to have my predecessor, Mr. Luce, to appear before the committee sometime.

The CHAIRMAN. The committee would be delighted to hear Mr. Luce. Some of the old members know pretty well what Dr. Luce thinks, and we appreciate him, just as you do, and that is quite a generous thing on your part, to suggest that he come.

Mr. WOLCOTT. I think, Mr. Hemphill, all the members of the committee are very much interested in this 100-percent reserve, and I think, as you said, there is a great deal of confusion in our minds, which now exists, and if you can put that into understandable form in your statement, it would be well.

The CHAIRMAN. Add to your statement.

Mr. HEMPHILL. It is entirely at your pleasure, but I would like awfully well to have another hour before the whole committee, if that is possible.

Mr. BROWN of Michigan. There is one thing I would like to ask for the purpose of the record, because it was based in part on the hearings of the committee. I know you criticized Governor Eccles for suggesting a spending program and a taxation increase on income, in a news article a couple of days ago. I want you to know that Governor Eccles did not suggest before this committee a present increase in income taxes. He proposed that we delay that until we had had some substantial recovery, some increase in income. I think it was unfair in that respect.

Mr. HEMPHILL. It was just what he stated to me.

Let me say this: In all kindness and with the greatest respect in the world for our Congress, you brought up a point here that is, I think, a very important charge.

I believe that Congress was intended originally and is now presumed, to legislate, and this Congress seems to me to have been engaged largely in considering the bills which have originated by the administration. Is not that true?

The CHAIRMAN. That is probably not so true as many people have been led to believe. As a matter of fact, this bill before us is not a bill that has been prepared and sent down here to us with a "thou shalt" on it, and it has not been prepared in the absence of conferences and consultations with Members of Congress. There is an exaggerated idea in connection with what you say.

Mr. HEMPHILL. All I was hoping to do was to get an amendment to this bill, not to promote any legislation at all, but to get an amendment to this bill, Mr. Chairman, which has exactly the same objective which this bill has.

The CHAIRMAN. If I may say it, everybody has the same object and the same desire.

Mr. HEMPHILL. Yes; by short-cuts.

The CHAIRMAN. A great many people think they know how to bring that about, but those who know how have not got the power, it seems.

Mr. HEMPHILL. That is true. I thank you gentlemen very much.

The CHAIRMAN. We appreciate your statement, and I am sure every member of the committee does, and we regard it as able and instructive, and, of course, the same is true of Dr. Fisher. We are glad to hear you and wish we could hear you longer.

Mr. Brown of Michigan. Have you made it very plain that we will be glad to have these gentlemen submit their proposed amendments to the committee in writing?

The Chairman. Yes; we shall be glad to have them do so.

Senator Owen, will you come around, please?

STATEMENT OF HON. ROBERT L. OWEN, FORMER CHAIRMAN COMMITTEE ON BANKING AND CURRENCY, UNITED STATES SENATE

The Chairman. Senator Owen, you are familiar with the legislation, and the committee would be glad to have you express your views on this bill. You need no introduction to the committee.

Mr. Owen. Mr. Chairman and gentlemen, in commenting upon the present bill and the principles which underlie it, I wish it to be understood that I am speaking simply as a citizen, and not as representing any groups with which I am connected. I am expressing only my personal opinions with regard to the matter.

The great question, Mr. Chairman and gentlemen, which needs to be settled in this country, the settlement of which has now been deferred 5 years, is the reemployment in industry of some 10 or 12 or 13 million men and women who have been walking the streets unable to sell their labor at any price. That is your real problem, and it is a monetary problem. There is no difficulty in understanding it. It has been explained to the committee on various occasions, and this committee took a very good step in 1931 and 1932 in its attempt to bring about a fundamental settlement of that question in the Goldsborough bill, upon which you had 500 pages of testimony, and which the House passed by a perfectly tremendous majority, 289 to 60, 172 Democrats and 117 Republicans voting for that bill, to restore and maintain the purchasing power of money at an equitable price level, and giving a mandate to the Secretary of the Treasury, through the Federal Reserve Board, and the Federal Reserve banks, to make effective that policy.

There is no doubt whatever in my mind that they had the power to do it, but so far from obeying what was the will of the House of Representatives on that matter, beginning on March 15, 1933, immediately after Mr. Roosevelt came in the White House, the Federal Reserve banks contracted credit to the extent of $944,000,000 within the 12 months up to March 15, 1934, and they contracted currency to the extent of 1,560 millions at the same time, making a total contraction of about 2,500 millions the first 12 months of the Roosevelt administration.

Of course, you did not get any recovery from a depression, under those conditions.

Now, Mr. Chairman and gentlemen, let me call your attention to the fundamental facts from which attention should not depart. They are these: That to carry on the business of this country, you must have the medium of exchange and you must have the working capital. What took place was a contraction of working capital of approximately 20,000 million dollars, from the contraction of that amount of loans, the loans having been made for that purpose.

And when those loans were contracted by the banks—I am not blaming the banks; I am a friend of the banks; I wish them well; I have been elected bank director 46 times and my sympathies are with them—when the banks contracted the loans amounting to 20,000 million dollars, they withdrew that amount of working capital which employed labor to that extent. And those loans were paid by the liquidation of $10,000,000,000 of time deposits and about $10,000,000,000 of demand deposits.

Now, as Mr. Eccles explained very clearly to the committee, the demand deposits comprise the money of the country which transacts nine-tenths of our business. So that when you contracted that working capital through the liquidation of loans you not only reduced the amount of working capital $20,000,000,000 and threw out of employment the people who were employed by the business using that amount of working capital, but, what was still more important, perhaps, you cut down the amount of money available by the contraction of nine-tenths of our business to nearly one-half of what it was. We had 23 billions of demand deposits in 1929 and about 4 billions of so-called "cash" or pocket money issued by the Government of the United States. With that 27 billions we had a production in this country of about three times as much, or $81,000,000,000, and, taking the last 10 years, you will find that the total production or income of the country, as estimated by the Department of Commerce, corresponds very closely indeed with the amount of money in demand bank deposits and in pocket money multiplied by 3. That is a uniform relationship between the money supply and production.

And your problem is to restore that money to this country. There are two ways of doing it. One is through the banks. If the banks would relax, and if the banks would relax the policy of freely lending money for productive purposes, that amount of working capital and that amount of demand deposits would be quickly restored. But the banks do not do so because of fear. You have got to remove their fear before they will return to normal banking. But the Government can accomplish that with perfect ease. All that is necessary at the present time is to have the Government buy its own bonds through the Reserve banks. When they do that, if they bought 17 billions of bonds which the private persons in this country hold, the first effect of that would be to increase the deposits of the banks by 17 billion; and when those bonds were transferred by the member banks to the Reserve banks, it would increase the member-bank reserves by a like amount.

If the Government, on the other hand, bought the 13 billions of bonds, approximately, which the banks are supposed to have, or which they do have, you would not increase the deposits, because the deposits have already been created by the purchase of those bonds. It would increase the member-bank reserves by a like amount; and when the member banks have a reserve of 100 percent, subject to check, in the form of reserves, with the Federal Reserve banks, the banks would not have any fear at all, because they could liquidate their demand deposits 100 percent without any difficulty.

That is the great problem with which you are faced. It is restoring the money of the country which has ben retired by the calling of loans by the member banks and other banks. That has been so clearly explained to the committee that I do not think it is necessary for me to enlarge upon that any more.

I was asked the question under examination some days ago by Senator Bailey, of North Carolina, "Where would you get the money from to buy the United States bonds?"

I replied very mildly that I would find the money the same way that the First National Bank of Raleigh finds the money for bonds it buys from the United States Government. When they buy $100,000 worth of Government bonds, they simply take a pen and insert on their books, their ledger, a credit account to the Government of the United States subject to check. They hold against that the bonds. That credit is available, but it is subject to demand; and if for any reason they did not have the ability to pay the amount in currency, they would have to call on the Federal Reserve banks for the currency; and if their resources failed, then the bank would fail, if they had a run made upon it. It is for that reason that the banks are apprehensive when their demand deposits are large and their available cash reserves are relatively small.

Now, taking the bill which is before you, I wish to express my approval of the proposal made by the Governor of the Federal Reserve Board, in that he asked that the bill should provide that the Federal Reserve Board should control the interest and discount rate; that they should control the ratio of reserves in member banks against their deposits; that they should control the right to buy and sell bonds.

Those three powers are necessary to expand the money of the country or to contract it, having the power either to expand or contract, the power of expansion and contraction, and you can expand when it is needed, and you can contract to prevent inflation.

I use the word "inflation" always as meaning an unjustified expansion, never to mean merely a justified expansion, because a justified expansion is not "inflation."

You need now the same amount of money per capita that we had in 1929, and that amounted to about $225 per capita up to $250 per capita. The calculations vary according to the estimates that are made. When you have furnished this country a mechanism by which this can be accomplished, if you stop there, gentlemen, and do not exercise your duty and your power to regulate the value of the money, which the Constitution of the United States imposes upon you, if you do not have a mandate upon the officials charged with the duty of exercising the powers which you grant, you need not be surprised if you are disappointed afterwards in the exercise of human judgment, which may or may not carry out the hopeful expectations you might entertain.

In my opinion, this bill is defective in the very particular matter of having no legislative mandate, such as you proposed in the Goldsborough bill, which was passed, I believe, in May 1932. That bill was discussed very fully in the House for 2 days. It had an overwhelming vote because of the obvious righteousness of the proposal, and you were confronted at that time by the story that it could not be done. In other words, the Federal Reserve banks and the Federal Reserve Board, and the Secretary of the Treasury promptly advised you they could not do it. That was the answer then. It is no longer the answer now. It is now plainly stated to you that it can be done, and you are invited to give these powers to the Federal Reserve Board.

To talk about immaterial things, to talk about little things, when this gigantic subject matter is before you does not interest me. I do not take any interest in the matter, outside of these vital fundamental questions. The responsibility is on you, it is on this administration. When the administration came in 2 years ago, the country was under the impression that this was going to be done; that we were going to have an adequate supply of money; that we were going to have the regulation of the value of money; that we were going to have a sound money, with a uniform, permanent, debt-paying purchasing power; that we were going to have property values restored.

When the Goldsborough bill passed, I took the bill and the recorded testimony before the committee to Mr. Roosevelt in New York City, and handed it to him in person. I asked him whether he was in favor of the Goldsborough bill. He replied that he was in favor of it. He has consistently maintained that position, because in his inaugural address he stated it, and in his cable to the London Economics Conference he said:

> Let me be frank in saying that the United States seeks the kind of dollar which a generation hence will have the same purchasing and debt-paying power as the dollar value we hope to attain in the near future.

And in his following address to the American public, October 22, 1933, he said:

> When we have restored the price level, we shall seek to establish and maintain a dollar which will not change its purchasing and debt-paying power during the succeeding generation. I have said that in my message to the American delegation last July, and I say it now once more.

He added:

> Some people are putting the cart before the horse. They want a permanent revaluation of the dollar first; it is the Government's policy to restore the price level first.

I regretted it as most unfortunate that President Roosevelt's advisers were able to persuade him to defer dealing with this fundamental until the N. R. A., the A. A. A., the R. F. C., and so forth, could be tested out. Whatever measure there is of disappointment in these administrative efforts can be largely accounted for by the failure to restore property values, to restore working capital, and to restore the volume of the medium of exchange in demand bank deposits which had been destroyed by contraction.

You cannot restore property values without restoring the money by which to restore property values. Property values depend absolutely upon the volume of your money.

Your power to coin money and regulate the value thereof, under the Constitution of the United States, is the power of regulating the value of money by regulating the supply.

The Governor of the Federal Reserve Board has very clearly pointed out to you all that is necessary to be done to give that power to the Federal Reserve Board. The control of the interest and discount rate, the control of the reserves, the control of the right to buy and sell bonds, that is the way the Bank of England regulates money in London, and has been doing for nearly 100 years. That is the way England checks itself from a monetary panic, by simply passing a resolution of the ministry, authorizing the Bank of England to issue unlimited legal tender money on sound assets other than gold. They cured the panic of 1847 in that way in a few days. They stopped the panic of 1857 in the same way. They cured the panic of 1866, when Overend-Guerney failed, in the same way, and when the Baring Bros. failed in 1890 they controlled the panic in that way. They do not fear that kind of panic any more, because they know they can control it, and they are now regulating the value of money in Great Britain by regulating the supply of the money.

They are doing the very thing that I am counceling now. Sweden is doing the same thing, and has regulated it with particular accuracy down to 1 or 2 percent. You have the greatest opportunity in the world now, by framing this bill properly and efficiently, so as to make your will control it, so as to have the Congress of the United States framing the policy and directing the policy of this country. To regulate the value of money, when you give this power, you ought, in my judgment, to put in this bill a mandate requiring the powers you grant to be used to restore and maintain the purchasing power of money along the lines of the Goldsborough bill which you passed by such a splendid majority, and which certainly excited my most ardent admiration.

The legislative mandate will remove the executive officers from the danger of being diverted from their duty by selfish advice or by political influence of any kind. The honesty of our officials can be depended upon when they have a clear instruction as to what to do. If they fail, the Congress would have the plainest evidence of it and could correct it.

While the demand bank deposit is about 19 times as important as pocket money, because checks transact 19 times as much business, our pocket money should be simplified by issuing only one form of paper money in which the note employed would not be described as a "promise to pay" (an artful device of selfish interest), but should be designated as so many dollars issued in pursuance to the constitutional mandate of article 1, section 8, clause 5, which authorizes Congress to coin money and regulate the value thereof.

The statute should declare the gold and silver in the Treasury to be available for the payment of foreign-trade balances, and in science, and in the arts, at a fixed price.

The fear that our dollars would not be kept at parity with gold has no real foundation, for it has been demonstrated by the Gold Standard Act of March 14, 1900, that a very small amount of gold, to wit, $150,000,000 in gold coin, has kept from 5 to 7 billions of currency at parity with gold, and without the employment of any of the gold reserve referred to. If, therefore, $150,000,000 of gold coin will keep at parity with gold 5 billions of paper money without impairment for 33 years, how long would 8½ billions of dollars maintain the parity of our paper money?

The question itself is obviously absurd. The same thing is true of silver. Now that our money is all legal tender, it not only is as good as gold, but it is better than gold, for it can perform services more economically than gold, more conveniently than gold, and when gold is desired for legitimate purposes it can command the supply of gold required. It isn't the gold in the dollar which gives it its value, but it is the demand for the dollar in the transaction of domestic and foreign business. The domestic demand for dollars in 1929, in checks alone, was over $1,200,000,000; more than 100 times all the monetary gold in the world then existing, and 300 times as much gold as we had in the United States; and, as a money metal in the United States, gold had even then a negligible use. It has no use now, because of the wisdom of Congress in taking public ownership of the gold supply and confining its use to domestic needs as a commodity and to the payment of foreign-trade balances. The form of money which I advise would greatly save expense and the cost and trouble of accounting. It would facilitate our business in a constructive manner.

Now, Mr. Chairman, that is all I have to say.

Mr. CROSS. Senator, one of the most vital things that we could do and do, I think, officially, is to stabilize the purchasing power of the dollar in harmony with some commodity index, covering some period, 1921 to 1929, or 1926, or whatever it might be. I have been thinking recently about the fact that England, ever and anon, let their pound slide down, unquestionably on purpose. They are getting an advantage in export trade as a result. Since she has not her pound stabilized, if we were to put a provision in this bill to stabilize the purchasing power of the dollar on some commodity level, would it not probably be wise to say that we must not let its purchasing power drop 2 percent below the line, but have a leeway for conditions which present themselves, where you could go 20 percent further? In other words, if England kept cheapening her pound, we would keep cheapening our dollar, and put the price level higher. Of course, she has got to reach a limit on that kind of thing some time, but it occurred to me if we were to stabilize on a fixed limit, now, say—and I am using England as an illustration—she might just cheapen her pound under our dollar, and in that way get an advantage on her exports.

Mr. OWEN. Mr. Congressman, what we need in our country is a stability in the purchasing power of money, so as to establish a fixed, an honest, and a just relationship between debtor and creditor, and so as to have a standard measure of value upon which manufacturers and merchants could depend.

Mr. CROSS. I understand.

Mr. OWEN. That is the great objective, and what England may do with a view to cheapening her pound, to expand temporarily her foreign commerce, should not concern us. What we want to do and what we need to do is to establish an honest, stable, permanent debt-paying purchasing dollar, and when we do it at home, Mr. Congressman, we will do far more than would appear to be the domestic result. We would, in that event, fix permanently the purchasing power of an ounce of gold, which is 35 times that stable index of $1, and therefore you would give a standard to the whole world, using gold as the basis of a stable measure of value. You could do the same thing with silver, by fixing a fixed relationship then afterwards between silver and gold, and we have enough gold and we can command enough silver to accomplish that purpose without difficulty. But our great problem is at home. Look at what has taken place in this country. If you could only visualize the 10,000 people who commit suicide annually under recent conditions, if you could visualize 13,000 armies of 1,000 each walking the streets of Washington, telling that pallid tale of distress and woe, you would realize the enormity of what has taken place in this country by the destruction of the medium of exchange; the destruction, therefore of all values of property and the destruction of employment.

Mr. CROSS. Now, another question, Senator. What do you think about putting an amendment in title II, providing for the Government to purchase the stock of the member banks in the Federal Reserve banks?

Mr. OWEN. All the values that are in the Federal Reserve Banking System have been created by the Government except $143,000,000.

Mr. CROSS. I know that.

Mr. OWEN. My own opinion is the Government of United States needs an instrumentality belonging to it, not belonging to somebody else. It is the private ownership of the stock of these banks which leads to their right to select the directors and the governor and the control, and when they control, they control the credit of the United States. They control the money of the United States, and, without knowing it, they have expanded our money and contracted our money in such a way as to make bull movements and bear movements, out of which the speculators profit, in both cases. I do not think that the banks should be charged with any willful purpose about it. They are just human beings, such as we are. They are following the line of their own interest, conducting the banking business for profit, and I think, gentlemen, the Government of the United States ought to go out of the banking business for profit and leave the banks to do the lending to the country, but the Government of the United States ought to control the volume of money, the supply of money, so as to give this country what President Roosevelt said we should have, money of a permanent, debt-paying purchasing power. When you have done that, you will have discharged your full duty, and this country will rise up to call you blessed, and if you do not, they will rise up and call you be-damned.

Mr. CROSS. That is what they are calling us now.

Mr. OWEN. That is what they are going to call you. Do not make any mistake about that. If you do not give this country immediate relief, something is going to happen to you.

Mr. CROSS. Here is another question, but I do not know whether it is very material——

Mr. OWEN. I have taken the liberty of talking very freely to you gentlemen, because I feel myself a sort of elder brother in talking to you, and I have been talking to you as a friendly counselor who has given a long study to the question of monetary science.

Mr. CROSS. What do you think of, instead of requiring the 40 cents in gold back of the notes, you require, say, 30?

Mr. OWEN. I did not quite catch your question, Mr. Congressman.

Mr. CROSS. I said, in place of requiring 40 cents of gold certificates back of the Federal Reserve notes, you require 30 in gold and 10 in silver. What do you think of that kind of a proposition?

Mr. OWEN. I think it is a joke.

Mr. Cross. Do you not think——

Mr. Owen. I am speaking seriously, Mr. Congressman. Permit me to say, we have something about 8½ billion dollars of gold, and a large amount of silver, but we have got what is far more than that—far more than that; we have got taxing power in the United States, representing the earning power of a very great industrial people, whose normal production is $90,000,000,000 and who could get into production 150 billions, if they were furnished with the proper supply of money.

Mr. Cross. Now——

Mr. Owen. Just a minute. I have not finished answering your question. I am going to answer it. Behind whatever money we issue would be, of course, the gold and silver controlled by the Government. The Government has taken over all the gold now, and the only use of gold now permitted by law is to pay international trade balances and for commodity purposes, making jewelry and in the arts and sciences, and at a fixed price of $35.

Now, Mr. Congressman, on the 14th of March 1900 we passed what was called the "Gold Standard Act", requiring that the gold dollar should contain 25.8 grains and nine-tenths fine, and that our paper money should be kept at parity with gold. To keep all the money at parity with gold, we put into the Treasury $150,000,000 of gold coin; and that kept our money up to 5 billion, and at the parity with gold, without using any of the 150 millions of gold at all. That is why I say it is a joke to talk about putting gold behind our money, when that is confined, in my way of thinking, to a reasonable base. We do not need any gold behind our money.

Mr. Cross. You have in this bill 40 cents in gold back of every note.

Mr. Owen. I say it is a joke just the same.

The Chairman. Under the Gold Standard Act provision was made for replenishing that fund.

Mr. Owen. Three-percent gold bonds.

The Chairman. At any time it might be depleted.

Mr. Owen. Three percent gold bonds. It never needed to be employed. The gold was never depleted. People did not want the gold. They wanted money. They do not use pocket money for transacting nineteen-twentieths of the business of the country, but they use check money, based on demand bank deposits. That is what they use. They are not thinking about gold and do not care anything about gold. It is only the bankers who do that with respect to gold and silver with the effect of confusing innocent men.

Mr. Cross. In other words, 40 percent gold back of the dollar here might as well be wiped out?

Mr. Owen. It might.

Mr. Hancock. Senator, do you not think that the administration, in keeping with its covenant, is making a serious and faithful effort to furnish the country with a sound and adequate currency system today?

Mr. Owen. I think that this bill is a tremendous step forward in the right direction, and I have every hope in the world that this bill will pass. I am only pointing out to you that you should add a mandate, such as the Goldsborough bill, which you passed 2 years ago, because without a mandate you will have the same thing occurring which occurred the last 2 years. You authorized three billions of bonds to be bought through the Federal Reserve banks—did you not?—as you authorized three billion dollars of currency to be issued; did you not? Congress authorized it, but it did not put a mandate on it, and it has not been employed, and the money available for business has been contracted instead of expanded. Do not underestimate the vast importance of this because it is a reality. By the sight of Government when the Government bonds are sold to the member bank, it does create a deposit. But up to this time approximately all those deposits which have been thereby created have been consumed by requiring the industrial elements of this Nation to a like amount of debts to the banks, and the loans to our industries have been decreased while the deposits have increased. The natural result has been to take productive capital from industry and transfer a credit to the payees. Do not make any mistake about that.

Mr. HANCOCK. Senator, I appreciate very much the constructive suggestion which you have made. I do not care to inject anything that smacks of politics in connection with the consideration of this legislation, but I have had in my mind for a good long time the significant difference in the language which our great President used at the time of his inaugural address and the platform adopted by the Democratic Party in Chicago. I understand that that platform, as you well know, recommended a sound currency system at all hazards.

Mr. OWEN. Yes; certainly.

Mr. HANCOCK. Mr. Roosevelt, however, in his inaugural address, referred to the same subject, and promised the people a sound but adequate currency system. That's what we need and must have, is it not?

Mr. OWEN. The words "sound money" have been unjustly given a double meaning. The words "sound money", as used by the advocates of the gold standard, mean gold money, redeemable in Government gold of 25.8 grains per dollar. That is what the standpatters mean by "sound money", but I do not mean that; but informed people mean sound money which has a uniform, debt-paying purchasing power. Mr. Roosevelt's interpretation of the word "sound" money is entirely correct, in my opinion. I certainly commend him for it.

I organized, or took part in organizing, the Sound Money League, in which I have been advocating just that kind of dollar, because that is the only sound dollar we could have.

Let me describe what took place with the gold dollar, because the gold dollar had the same purchasing power index as our other dollar had, and yet, in May 1920, the index was 60. In February 1933 it was 166. The variation was the variation between 100 and 278, showing that that was not sound money.

Mr. HANCOCK. Do you not think it is fair to conclude that, since the Governor of the Federal Reserve Board has come here with this bill and presented it so intelligently and so effectively, that it represents the President's sincere effort to carry out his pledge made in his inaugural address and that its general purposes have his blessings?

Mr. OWEN. I heard the evidence given for the first 2 days by Governor Eccles, and it was in accord with my own views. I sat in 2 days, listening to it, and I felt entirely in accord with it.

Mr. HANCOCK. Would not the Government, under this legislation, particularly title II, be in a position to furnish the country with a dependable, sound, and adequate medium of exchange, an obligation which it has never to this good hour discharged?

Mr. OWEN. Yes; but if the Government were to undertake to say to these privately owned Reserve banks, "I want you to buy five billions of gold bonds", that the privately owned Reserve banks would be in a position to raise a great outcry against compelling them to do that; whereas if the Government bought those banks, by a cross entry, of $143,000,000 on the books—and that is all it would take—it would be in the position of actual control and it would not take any money at all.

Mr. HANCOCK. Do you not also think that whatever authority may be vested with this sovereign power, some latitude of judgment and discretion should be left with the authority, or, in this legislation, the Federal Reserve Board?

Mr. OWEN. Certainly, the latitude of carrying out your will; but your will ought to be described so as to tell what you want. You ought to tell them plainly that you want them to bring back the dollar to the normal value, and keep it there, and when you do that you will have discharged your duty; and if you do not, I do not think you will have discharged your duty.

Mr. HANCOCK. Senator, what would you say is the normal level of the dollar?

Mr. OWEN. I would say 1926 is a reasonably normal level, because it is the same as the average 1914 to 1930, inclusive, and because it is the average of 1921 to 1929, inclusive.

Mr. HANCOCK. Must you not allow for at least normal economic changes in determining that level?

Mr. OWEN. Yes; certainly, and, more than that, I think the suggestion which has been made here is a good and wise one, to base the index upon basic commodities, and I think that that ought to be further discussed by the Board, and the Board will make reports to the Members of Congress at least once a year, and I think preferably every quarter, so that the Board would tell the Members of Congress what they are doing to carry out the policy of the Congress with regard to money, so frequently that they would never lose sight of their job; and their sole job, in my opinion, is regulating the volume and value of money. Your chief duty is to declare the policy—not necessarily the details.

Mr. HANCOCK. Do you not think that things other than commodities should enter into a determination of the price level?

Mr. OWEN. No; I think that is enough. They have had the Saurbek index in Great Britain for many years, and it served as a good enough level. The value of the all-commodity index is this: That it represents a value of all human labor for a period of 1 year, we will say, and that is comparatively stable in volume and in its essential usefulness, and if money is kept stable in relation to it you will have the greatest stability of which you are capable.

Mr. HANCOCK. One question, and then I am through, Senator.

Mr. OWEN. Yes, sir.

Mr. HANCOCK. With respect to purchasing the obligations now held by the banks in order to replenish the supply of money, you say that a transaction of that kind on the part of the Government will be similar to a transaction on the part of any bank. For instance, you used the First National Bank of Raleigh, N. C.

Mr. OWEN. I say that when the purchase by the Federal Reserve banks of United States bonds is made, it would be identical in character with that of the purchase of bonds by the First National Bank of Raleigh. They would give a book-entry credit against the purchase of the bonds. If they wanted that paid in money, they could get it, because the Federal Reserve banks can get all the money they require against bonds. People do not want pocket money. They want bank credit. That is what they want.

Mr. HANCOCK. I think I understand.

Mr. OWEN. That is what they need.

Mr. GOLDSBOROUGH. Senator Owen, do you remember going over a bill that I introduced early this session providing for the establishment of a bank which should absorb the national debt?

Mr. OWEN. By purchasing the bonds outstanding?

Mr. GOLDSBOROUGH. Yes.

Mr. OWEN. Yes; I do.

Mr. GOLDSBOROUGH. Do you remember the bill provided that the capital stock should be furnished by the Treasury?

Mr. OWEN. By what?

Mr. GOLDSBOROUGH. The capital stock of this bank should be furnished by the Treasury.

Mr. OWEN. Yes.

Mr. GOLDSBOROUGH. Money which was not then being used for support of other money, and that as the purchase of these bonds tended to raise the reserves of the banks the Federal Reserve Board was directed to raise their reserve requirements in order to prevent undue inflation.

Mr. OWEN. Yes.

Mr. GOLDSBOROUGH. All right. Now, then, my question is this: A gentleman who is to appear before this committee tomorrow characterized that bill in this language [reading]:

> Now, Mr. Goldsborough's proposition would have the Government paying off its investors not through money raised through borrowing or taxation but by means of paper money printed by the Government. Such money is in the nature of forged notes, forged by a Government against its people. He is asking the Government to go into the business of forging notes. If in his private affairs a man borrows at a bank or elsewhere and then finds it difficult to pay and gives a forged note or counterfeit money in settlement, he is put behind the bars. We demand that he live up to his contract and that he make his wealth with which to pay his debt. We do not allow him to issue forged notes or to set up a printing press to run off the necessary amount of notes to pay off this debt. In simple but accurate terms that is what Mr. Goldsborough and several others in Congress are proposing to do.

I would like to get your judgment as to the value of that statement.

Mr. OWEN. It has no value or it has no truth in it. The truth is that when the First National Bank of Raleigh buys $100,000 worth of Government bonds and gives a credit against them they give value for value, and the same thing would be true with regard to the Government of the United States in buying its own bonds through the Federal Reserve banks. They would give dollar for dollar value. If the public wanted legal-tender notes for it, they could get it; but they do not want legal-tender notes. The Government in buying its own bond of $1,000 and giving the equivalent for it, a sound bank credit convertible into legal-tender money, is giving full value. That is a very amazing statement you read. I cannot imagine any person informed with regard to monetary science would make it.

Mr. GOLDSBOROUGH. He is going to be seriously offered here tomorrow in opposition to the bill which we are here considering.

Senator, what argument can be made, if any—I do not know of any myself—but what argument can be made that money which is merely manufactured on the books of a bank, which really had nothing in comparison with what the Government of the United States has, that money manufactured on the books of a bank is more valuable and is of a higher degree of monetary consequence than money issued by the Government of the United States, that has behind it every resource of every individual in the country?

Mr. OWEN. Mr. Congressman, I do not sympathize with those who say that the banks make money out of nothing, because when a bank lends money, a certain amount of money, $1,000, say, they take a mortgage on my property worth $2,000, $3,000, or $4,000. They ask a larger amount of security than the loan ordinarily, and it is against that property of value that they issue this credit. The weak spot in it is that when they are called upon to liquidate that in pocket money, in currency, they have not got that to pay with.

What you say with regard to the Government is perfectly true.

Mr. GOLDSBOROUGH. I had reference to Government borrowing from banks. That is what I am talking about.

Mr. OWEN. The Government borrows from a bank by giving its bonds to the bank, and the bank takes the Government bonds and enters a book credit.

Mr. GOLDSBOROUGH. First the Government sends their bonds to the bank, and then the bank loans the Government the money, and the Government loans the money back to the bank and pays interest on it. That is substantially right?

Mr. OWEN. That is about right.

Mr. GOLDSBOROUGH. Is there any value created in the money which eventually goes into the market because the Government, instead of issuing this money directly, furnishes its bonds to a bank and has a bank set up a bookkeeping entry? Is there any more value to that money?

Mr. OWEN. No; that is self-evident. The question answers itself.

Mr. GOLDSBOROUGH. I know the question answers itself, but because it is contradicted so often it is worth while to state it.

I am through.

Mr. FORD. Senator, I want to ask one question.

Mr. OWEN. Yes, sir.

Mr. FORD. Assuming that the Patman bill becomes a law, what effect would that have on the country?

Mr. OWEN. It would have an effect on the country primarily of introducing that amount of pocket money. A large part of it, I assume, would flow back into the banks, and if they owed the Federal Reserve banks anything they would liquidate that debt to the Federal Reserve banks for that, but they do not owe the Federal Reserve banks anything but have large balances in the reserve banks now, and, therefore, that would add materially to the available amount of money in the country. That is my opinion about it. It would help substantially.

Mr. FORD. It would have a tendency to help business?

Mr. OWEN. It would substantially help the whole country. We are suffering from lack of money, and that is the only way we can do it. We have got everything else on earth. We have got the ablest people on earth, and our factories are running only one-sixth of their time. We have got splendid climatic conditions and our country is fertile, and we have everything on earth but money, but you cannot transact business without money. Civilization depends on money. If you have got to go back to bartering civilization would cease. Everybody knows that. It is self-evident.

Then the statistics which have been laid before you show that. I suppose you have seen these statistics and chart compiled by the Federal Reserve Bureau which shows completely the trouble. We have lost $20,000,000,000 of capital employed in production. We have lost 10 billion of time deposits, potential demand deposits, and approximately $10,000,000,000 of actual demand deposits which function as check money in business, and which have a turn-over 36 times a year.

Mr. FORD. Governor Eccles says that the 2-billion-dollar excess reserve is capable of supporting a 20-billion-dollar bank credit.

Mr. OWEN. That is a technical observation, meaning this: Under the present system of a ratio of 10 percent on the average of reserves against deposits, those reserves could be employed to expand 10 times. But the difficulty with our country has been that those reserves are entirely too small; that those reserves, instead of being 10 percent should be raised to a point where the banks would have no fear of our demand depositors. This should be made at least 50 to 100 percent, gradually and steadily raised, and in that way the banks would have no fear. That was explained very clearly by Professor Fisher and Mr. Hemphill a few days ago. I was sitting here and I heard their testimony. It was very clearly stated.

Mr. FORD. I am thinking this situation over: If a bank had to maintain a 100-percent reserve on its check deposits, what possibility or what opportunity for profit would there be in banking?

Mr. OWEN. The total amount of bank deposits in 1929 was about 55 billions. So that only 23 billions were demand deposits. All the balance was time deposits or savings accounts. And I think that this bill has some very valuable provisions in it, in providing that all bills of value, practically, shall be eligible; and I think it has a very important provision in authorizing the loans against real estate. When the banks have their fear of the demand depositors removed by a large reserve against their demand deposits, and it does not cost them anything to get the reserves, it will save the Government the interest charge of the bonds that are bought.

Mr. FORD. That is what puzzles me. Maybe I am dumb, but I am just trying to find out. A bank has $500,000 worth of demand deposits.

Mr. OWEN. Yes, sir.

Mr. FORD. It has to keep a $500,000 cash reserve against that; and where does it get the $500,000, unless the bank's owners put it up?

Mr. OWEN. The bank you speak of, with $500,000, has in its own vaults at this time probably $500,000 in Government bonds. All they have got to do is to sell those bands to the Federal Reserve bank that has a reserve of 100 percent against their deposits. Fifty percent, I think, should be enough, except for the principle involved in the proposition—the manufacture of money by the banks, which I think ought to cease.

Mr. FORD. Where would their income come from, if they sold their bonds for $500,000?

Mr. OWEN. At present they have 56,000,000 accounts. I they charged $1 a month for each account as a service charge, they would get twice as much as they do now for the bonds. I am giving you the facts with regard to it. They are entitled to be paid for the service they render.

Mr. FORD. Then why should the banks object to it?

Mr. OWEN. They do not understand it. They do not know as much as you think they do. I do not mean to criticize them, because I am very friendly with them. I do not feel any element of hostility to them. I think they are just as good as we are, and they have done the best they knew how, and I think they have proved a good alibi when 15,000 of them have died.

Mr. GOLDSBOROUGH. This point has been raised here by different members of the committee—and I do not agree with them at all, but it has been raised, and possibly you could throw some light on it; more light than I have been able to—that if banks were put on a 100-percent reserve, they would have only capital stock and surplus, and there would be a deficiency.

Mr. OWEN. That is not so. They would have their savings accounts and their time deposits as well, their real-estate loans and loans against both time deposits and excess demand deposits, and interest on their investments. When they render service, they are entitled to be paid for it and they ought to be paid for it, and they ought to be allowed to do so.

Mr. GOLDSBOROUGH. Do you not think, Senator, when it comes to payment of services, it would be economically sound to let the United States Government assume it, rather than the depositors themselves?

Mr. OWEN. That is a matter of policy. The banks are entitled to be paid for the services they render, I think.

Mr. GOLDSBOROUGH. So do I.

Mr. OWEN. They are not aliens. They are our own citizens. They are our friends and our brothers and they are handling the money which they have, and the money of our neighbors. We have no fault with them.

Mr. GOLDSBOROUGH. I want to ask one more question. It is getting late, and we do not want to hold here much longer. I have made this statement, Senator, in this committee and other places and from the floor of the House: That under our average 10-percent reserve system, that if every individual in this country had the financial genius of the senior Morgan, and the inventive genius of an Edison or a Ford, and the energy of a north German farmer, that there could be no permanent prosperity in this country, because as soon as they began to pay their debts, we would immediately have a deficiency of money and depression would be inevitable, because as soon as you begin to pay your debts you create a deficiency of money. Is not that right?

Mr. OWEN. Certainly that is right on your hypothesis. When you pay off these debts, upon which the money is based, of course you contract the money, and that is the whole point of this discussion. It is, that the United States Government should furnish the money, and that in order to furnish the money the money should be based either upon the outstanding public debt, or issued as a straight credit based on the taxing power. The Government must issues the money required, whatever it is. It must not be issued by the privately owned banks as a debt. The outstanding public debt can be used instead of the private debt for the issuance of money. That is a plain proposition, and I do not see how anyone can fail to see it.

It has the advantage of saving 3-percent interest and 5-percent amortization on a debt which will soon equal 36 billions, a saving of nearly 3 billions per annum. This saving is only a part of the benefit to the Government, for the national income would double when the national production doubles. The national revenues would double when the national production doubles. Why talk about trifles when this saving is before you?

Mr. HANCOCK. May I ask one question?

Mr. OWEN. Certainly.

Mr. HANCOCK. That statement which Mr. Goldsborough has just related, which he has also made on the floor of the House, has given me a lot of trouble in understanding.

Mr. OWEN. In what way?

Mr. HANCOCK. Well, if such a situation as he relates should ever come to pass in this country, under our present monetary system, why would anybody need any credit?

Mr. OWEN. You speak of this matter?

Mr. HANCOCK. I mean when all the debts were paid, both public and private.

Mr. OWEN. I do not infer that he meant all the debts were discharged. What Mr. Goldsborough really meant by it——

Mr. HANCOCK. I think I am quoting him correctly. His argument is predicated on our present monetary system, if I understood it correctly——

Mr. GOLDSBOROUGH. Starting with the debt we now have.

Mr. HANCOCK. Starting with the debt we now have, the people would get in such a position that they could discharge those obligations, that you would thereby automatically so contract your credit money that you would not have any——

Mr. OWEN. Let me explain that matter, if I may. What Mr. Goldsborough really means, I think, is this: That the private debts were the basis of the issuance of the money, and when those private debts are called in, those private debts are liquidated by checks on the demand bank deposits, and therefore it is retiring the money of the country. That is what he really means. He means that the money of the country is based on private debt.

Mr. HANCOCK. I think I understand his contention and I am trying to analyze it. I am wondering why it would not be a very fine thing if all the debts were paid, and everybody's property was clear. Why is not that a desirable goal to work toward?

Mr. OWEN. We have had a very fine thing during the last few years, the contraction of loans by 20 billions, the contraction of our money supply by one-half and of our national property values by half, or 200 billions.

The CHAIRMAN. He means after your debts are paid.

Mr. HANCOCK. Would not all of those assets against which this credit is issued be immediately available for currency or credits. That's my reasoning and I think it both logical and sound.

Mr. OWEN. When you liquidate the outstanding debts you of course bring on these conditions. When you restore the money which is based on those debts, by making new loans, you bring back the money and bring back prosperity again, because it is in that way that we have been creating money, and it is against that means that I am protesting, and suggesting that the money shall be based on the public debt, and not upon the private basis of debt, and thus make the money permanent in supply. That is the very point I am trying to make. I do not know whether I am intelligible or not, but I understand very clearly what I am trying to convey to you, and that is that the money which previous to 1929 was based upon private debt has been retired by the liquidation of the private debts, and that the future money should be based upon a public debt that cannot be retired by privately-owned banks. That is what I am trying to tell you.

Mr. HANCOCK. Senator do I understand that you would want the Government to always be in debt in order to provide a different basis for credit or money?

Mr. OWEN. No; that is not necessary, Mr. Congressman. This is the first step, but it is enough.

When the bonds shall have been bought by a Government-owned bank, they would offset the credits issued against them. The credits issued against them are credits by the United States not bearing interest, but functioning as money. This could be done without bonds. The Government could issue credit to a Government-owned bank even if it had no bonds, and furnish the money of the country in this way, by having those who wanted such money obtain it for actual money in any bankable form. There is nothing mysterious about this. Government money does not have to be in the form of $1 bills, used for pocket money. It can be for $100,000,000 credits added on the ledger of a Government-owned bank, of which the United States is responsible exclusively, without any private ownership whatever. The Government must have its own agency undiluted and uninterfered with by the specious plea of private ownership of the instrument through which the United States discharges its constitutional duty to issue money and regulate the value thereof.

While the reserve banks are in private ownership, it will be necessary to remember that the earnings on the bonds bought would belong to the member banks who owned the stock. Therefore, the savings to the Government, both of interest and amortization on these bonds, would not accrue, and the benefits arising therefrom in the matter of interest would go to the member banks in violation of the fundamental purpose of the Federal Reserve Act of 1913, which provided that all earnings should go to the Government of the United States, except a reasonable interest on the stock. This law was amended by the Seventy-third Congress to pass the profits to the surplus of the Federal Reserve banks. This, of course, must be changed in any event, in order to deal justly with the Government itself. When the Government owns the banks this difficulty vanishes, and the Government will get the benefit of both the interest and amortization payments, which would be necessary.

It is the first step to have the Government of the United States furnishing the money that the country requires, and the Constitution provides. You are required to coin money and regulate the value of it, and you can only do it by furnishing the supply of money. You can do that by a credit instrument from the Treasury of the United States, convertible into legal tender on demand, just as well as you can on bonds. Suppose the Treasury of the United States gave a credit note to the Federal Reserve bank, convertible into legal tender on demand. They are not going to demand legal tender because they do not want that much pocket money, but suppose they do that, they can use the credit to buy the bonds with anyhow. Can't they?

Mr. HANCOCK. Yes; maybe I understand your point. It is a pretty deep subject for me to comprehend. I will have to do some more thinking and studying. My mind is open, I am happy to say.

Mr. OWEN. I do not think it is deep, but the only thing is, it requires attention. You cannot understand anything without giving it some attention, and the life of a Congressman is so bedeviled by outside things, they are doing forty thousand things at once, and I wonder how they do go down deeply into a question of this sort.

Those who are opposed to the administration banking bill of 1935 will strenuously urge the importance of delay. They will offer no means of giving the country relief from its great distress. They will urge with learned words that a bank has a very delicate mechanism from which all sorts of unexpected results may follow unless the banking laws are framed by a committee of experts such as the economists' national committee on monetary policy, headed by Professor Kemmerer, Professor Spahr, Dr. H. Parker Willis, and others. These gentlemen will urge delay without offering any immediate remedy. They will insist upon letting nature take its course; letting the creditor take over the mortgaged property of the debtor at half its value. These gentlemen, whether consciously or unconsciously, voice the views of our leaders of finance, under whose guidance this country suffered the enormous losses inflicted for the last 15 years by its great depressions ignorantly caused by expansion and ill-considered contraction of our national money supply by privately-owned banks moved into action by propaganda.

These representatives of the views of financial leaders, and who generally owe their bread and butter to generous endowments, will also strenuously urge that the existing order of manufacturing and expanding money and contracting money by privately-owned banks is the only way; that no man can prevent bull movements or bear movements; that they are inevitable, due to the laws of human nature, and that the Government should let them alone.

They will denounce the idea of the Government performing its constitutional duty to coin money and regulate the value thereof, and they will denounce the present bill as setting up a supreme dictatorship in Mr. Roosevelt, who could, they assert, through the exercise of his political control of the Federal Reserve Board, dictate the conditions of life and death, not only to the banks, but to every business man in the country. They urge that this political control of the banking system, and the issuance and regulation of the value of money, would give the powers of life and death over business. But they fail to realize that the American people have their choice only between public control and private control. They fail to see that private control is swayed by press propaganda, from extreme optimism to extreme pessimism; from a bull market to a bear market, and that these conditions give the speculators, the moneychangers of the country, the opportunity of depriving uninformed people of the proceeds of their labor.

They oppose Congress exercising what they call "political control", which the Constitution imposes as a duty on Congress. Political control, when wisely exercised by Congress, would assure the most beneficent results when Congress, in exercising its political power and its political control, imposes a legislative mandate on the Federal Reserve Board and the Federal Reserve banks, requiring them by law to provide the country with an adequate supply of sound money of uniform debt-paying, purchasing power, as President Roosevelt promised the country.

Our dangerous expansion of credit preceding the recent depression was not in the commodity markets, or the field of production, for the general price level actually went down to 98. Our dangerous expansion was produced in making loans for unproductive or speculative purposes in the security exchanges, supplemented by about 3 billions of foreign money attracted by usurious rates on call on the stock exchanges. This forced market price of stocks far beyond a price justified by earning power. Our Government should have power to control such operations which are so dangerous to the public interest.

Such legislative mandate would deprive the Federal Reserve Board, or the President himself, of the power of using the system with partiality or partisan discrimination.

The Goldsborough bill of 1932, declaring the policy to restore and maintain the purchasing power of the dollar on the average commodity index of 1921–29, and directing the Secretary of the Treasury, the Federal Reserve Board, and the Federal Reserve banks to make effective this policy, is a complete answer to the argument that the present administration bill could be used for partisan or selfish political purposes, because it is only necessary to insert this legislative mandate to meet these charges of possible partisan partiality.

This Goldsborough bill passed as stated by a vote of 289 to 60; 172 Democrats and 117 Republicans supporting this benign, intelligent, and patriotic policy.

The opponents of the administration will urge that all will be well, and our country will be restored to prosperity, if we merely go back to the Gold Standard Act of March 14, 1900, a standard of weight and not of value; a standard which has fluctuated from an index of 145 in May 1913 to 60 in May 1920 to 166 in February 1933. Even Prof. Kemmerer, who is chairman of the economists' national committee on monetary policy, had this to say as president of the stable money league, in December 1927:

> * * * The world sooner or later must either learn how to stabilize the gold standard or devise some other monetary standard to take its place.
>
> There is probably no defect in the world's economic organization today more serious than the fact that we use as our unit of value, not a thing with a fixed value, but a fixed weight of gold with a widely varying value. In a little less than a half century here in the United States, we have seen our yardstick of value, the value of a gold dollar, exhibit the following gyrations: From 1879 to 1896 it rose 27 percent, from 1896 to 1920 it fell 70 percent, and from 1920 to September 1927 it rose 56 percent. If, figuratively speaking, we say that the yardstick of value was 36 inches long in 1879, when the United States returned to the gold standard, then it was 46 inches long in 1896, 13½ inches long in 1920, and is 21 inches long today.

This stable-money league was backed up by important names in the industrial and financial world such as Owen D. Young, Russell C. Leffingwell, John Hays Hammond, the late George Eastman, and Paul M. Warburg, Waddill Catchings, James H. Rand, Jr., Henry A. Wallace, Malcolm C. Rorty, Frederic A. Delano, Charles Evans Hughes, Elihu Root, Otto H. Kahn, Roland W. Boyden, and George M. Reynolds.

Mr. Hancock. I am sure all the members of the committee have enjoyed hearing you.

Mr. Owen. I enjoy it, I am sure.

The Chairman. We must thank you for your very able statement.

Mr. Owen. I thank you, Mr. Chairman, and the members of the committee.

The Chairman. We will adjourn until tomorrow morning at 10:30.

(Whereupon the committee adjourned until 10:30 a. m., Monday, Mar. 25, 1935.)

BANKING ACT OF 1935

MONDAY, MARCH 25, 1935

House of Representatives,
Committee on Banking and Currency,
Washington, D. C.

The committee met at 10:30 a. m., Hon. Henry B. Steagall (chairman) presiding.

The Chairman. The committee will come to order. We have with us this morning Mr. O'Neal, the president of the American Farm Bureau Federation.

We are glad to have you discuss this bill, Mr. O'Neal. You may proceed without interruption, as far as you see fit, after which the members desire to interrogate you.

STATEMENT BY EDWARD O'NEAL, PRESIDENT AMERICAN FARM BUREAU FEDERATION

Mr. O'Neal. Mr. Chairman and members of the committee, my name is Edward A. O'Neal. I am president of the American Farm Bureau Federation, with 35 State farm bureaus throughout the United States. Our headquarters are in Chicago, Ill., and we have a Washington office.

I am a farmer from Florence, Ala., and own and operate a 2,900-acre farm on the Tennessee River in north Alabama.

Mr. Chairman and gentlemen of the committee, the courtesy of Chairman Steagall and your committee in granting us two sessions to explain further our advocacy of the significant principles and applications of the commodity dollar is highly appreciated. Permit me to express my appreciation for this courtesy.

Under the leadership of your committee, Congress has made an excellent start, through the banking bill of 1935, in revising extensively some of the banking and monetary laws of our Nation. To keep abreast of this progress, I believe it is within reason and logic to include in this measure one of the most important aspects of monetary reform which we have had under consideration for 20 years.

I refer to the commodity dollar, frequently called "the honest dollar." The proposed banking act of 1935 provides more efficient and more adaptable banking machinery for the United States than we have ever had before. I stress the fact, however, that in the revision of this banking machinery we should not commit the unpardonable error of setting up an efficient banking machine without providing the proper kind of a dollar for this machine to handle.

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We have reached an important crossroad in our recovery program. We are confronted with decisions of national policy upon which the success or failure of the recovery program is predicated. Our problem cannot be cured by hysterical and demagogical panaceas. Neither can they be cured by any temporary or artificial means.

For example, to aid us in obtaining satisfactory prices for what we produce, so that we can become larger purchasers of commodities which others sell to us, we need a mechanism more permanent and more applicable than the tariff. This superior mechanism, the commodity dollar, will aid us in solving problems relating both to our domestic and foreign markets. Furthermore, that monetary reform which includes the commodity dollar is as broad as the Nation itself. There is nothing local or sectional in it. And, in addition, it ramifies itself into the international picture.

The problem for us to determine is this: What shall we do to raise commodity prices so as to bring economic recovery to all? Shall we accomplish this goal by a further devaluation of the dollar? Or, shall this recovery come through enormous outlays of Treasury appropriations for public works, supplemented by credit expansions? In which direction does the road to real recovery lie? This question is of vital concern to every American citizen and to every American industry. Upon the solution of this question is predicated the very security of our Nation.

Because the American Farm Bureau Federation has taken the leadership in the solution of our monetary problems, particularly in their effect upon commodity prices, I ask for the privilege of reading into this record the resolution adopted at the sixteenth annual convention of the American Farm Bureau Federation, held in Nashville, Tenn., December 12, 1934. The resolution, under the title of "Honest Dollar", is as follows:

Be it resolved, That we urge the President to make full use of the powers granted him to raise the price of gold to the limits prescribed by Congress, to the end—

1. That commodity prices may be raised in line with the debt level and fixed costs.
2. That all business may be increased with resultant increase in employment and decrease in the huge expenditures for relief.
3. That equities may be restored in farms, homes, and investments.
4. That homes and other buildings may be made possible.

Be it further resolved, That gold certificates be issued against the profit accruing to the Government in the revaluation of gold.

Be it further resolved, That we urge upon the President that he meet the too often demonstrated need for a sound and honest dollar that will have a stabilized purchasing power from year to year and from generation to generation.

This is not the first time an economic calamity has visited our Nation, for in a lesser degree it happened in 1837, 1873, and 1893, and it is high time that farm organizations secure legislation of a curative and preventative nature. Men live at most 60 and 70 years and unless we recognize the cause of depressions and fortify ourselves against their recurrence, the millions of boys and girls who are now growing into manhood and womanhood will be forced to spend 10 to 20 years of their lives in distress such as we are now experiencing.

On the completion of the reflation program we demand that the necessary legislation be enacted to establish the dollar on a commodity basis, and maintain it as a stable measure of value.

In my judgment, the most effective step to take at this time to expedite national recovery is to further devalue our dollar to a normal level, and restore a normal balance to our price structure. This will permit the production and exchange of goods and services on a normal basis. It will provide employment. It will bring about resumption of trade.

To accomplish these ends, the American Farm Bureau Federation proposes:

1. That the dollar be devalued by raising the price of gold, thereby reducing the gold content of the dollar, until the normal level of purchasing power is restored to the dollar.

2. That Congress establish, as the goal of our monetary policies, a scientific unit of value which will be constant in value, and which will serve as a fair measure of value for the exchange of goods and services, comparable to scientific units of weights and measures.

In explanation of these proposals, permit me to point out, first, why further devaluation of our dollar is needed; second, what benefits may be expected from such devaluation; third, why such devaluation will be more effective in hastening economic recovery than can be anticipated from other proposed measures of relief.

We have made splendid progress toward recovery. The crucial crisis confronting our Nation in February 1933, has passed. The purchasing power of farmers and workers has been greatly increased. Unemployment has been reduced somewhat. Industrial production and profits have expanded. Bank deposits have increased. In general, the economic picture today is much brighter than it was 2 years ago.

However, we face the sober fact that our Nation still has a long road ahead of it before it reaches the goal of real and substantial recovery. A major economic collapse today would entail much graver consequences than ever before because the public debt is far greater. Destruction of public confidence at this time would result in chaos.

Despite the increase in farm purchasing power, farmers today, as a whole, are receiving little more than a subsistence income. Their returns are far below what is necessary to enable them to purchase industrial goods in terms of a normal demand by agriculture.

Agriculture's total gross income in 1934 was approximately $7,000,000,000. This is still far below agriculture's income in 1929, which was $11,900,000,000, and a long ways from agriculture's income for 1919, which was $16,900,000,000. Farmers cannot repair their homes and farm buildings, cannot buy fencing material, cannot replace worn-out machinery, and cannot improve their farm lands adequately on the basis of the present farm income.

Industrial production, trade, and finance are still far below normal levels, according to various business indicators. The Department of Commerce's Survey of Current Business shows that department-store sales are only 61 percent normal, freight-car loadings are 61 percent of normal, crude-steel production is 52 percent of capacity, December 1934 factory pay rolls were 63.2 percent of normal, pay rolls in the wholesale trades were 64.8 percent of normal.

According to data published by the Federal Reserve Board for December 1934, the index of industrial production in the United States was 78 percent of normal; the index of marketings of agricultural products was 73 percent of normal. The index for 1923–25 equals 100.

Today's dollar is still too dear, in terms of goods and services, to permit a normal exchange. The purchasing power of the dollar is still too high to permit a normal interchange of goods. The result is a low level of production for industry and a high rate of unemployment. So long as the general price level of commodities remains low in relation to the dollar, farmers cannot make enough profits to absorb the goods which industries would normally produce. Under these conditions, industries cannot resume a normal level of production and thereby absorb the unemployed.

Since February 1934, when the dollar was devalued by raising the price of gold to $35 per ounce, we have had virtually a de facto stabilization of our currency, with the price of gold remaining at that level. During this period we have been consolidating the gains resulting from the devaluation of the dollar and the restoration of commodity prices, supplemented by other recovery measures.

Under the existing value of the dollar in relation to commodity prices, debts, and wages, we seem to have gone about as far toward recovery as is possible. Without further devaluation of the dollar, to restore commodity prices to normal levels, complete or permanent recovery cannot be obtained.

To stabilize our dollar permanently at the present level would be ruinous. It would result in freezing our economic structure on a maladjustment basis. Ultimately such maladjustment would destroy the recovery program. No hope for permanent recovery can be had in a stabilization program which includes, at one and the same time, a general commodity price level of 115, a farm price level of 107, a price level of 126 for industrial goods bought by farmers, and an industrial wage level of 188. Only when and if a fair and equitable adjustment is established for all these indices can there be a normal exchange of goods and services.

To substantiate my reasoning I want to read into the record a statement made by Dr. G. F. Warren, nationally known economist, in an address before the Association of Land Grant Colleges, Washington, D. C., on November 20, 1934. The statement follows:

> The only desirable price level is the price level to which the internal affairs of the Nation are most nearly adjusted. After 4 years of deflation there were only two possible ways to proceed. One was to lower those things that had not declined. The other was to raise those things that had fallen. Whenever prices rise raw materials rise more rapidly than manufactured goods. If prices rise high enough, raw materials become high in proportion to manufactured goods. Some persons have thought that reflation called for an increase in prices of monopoly goods and wages that had declined very little. In general, such increases are not sound economically and would not be expected to occur by committee action.
>
> While our prices of basic commodities have risen to the English level, English wages have been approximately stationary at the index figure which also held for this country before the recent advance. Recovery is aided by placing emphasis on volume of business and volume of employment rather than on wage rates and prices of manufactured goods when the volume of business and employment is abnormally low.

One of our most serious mistakes has been that we did not carry our monetary program far enough. We stopped too soon in advancing the price of gold, and in getting the dollar down to the proper level. As a result, basic prices were not raised enough to make farmers and producers of other basic commodities prosperous, or to give them sufficient buying power with which to purchase a normal volume of the goods of other industries.

Other nations have gone farther than we have in revaluing their currencies, and have consequently enjoyed a greater measure of economic recovery. The price of gold in the United States has been raised 69 percent compared to 190 percent in Japan, 116 percent in Argentina, 108 percent in Australia, 107 percent in New Zealand, 103 percent in Denmark, 93 percent in Finland, 76 percent in Sweden, and 65 percent in England.

Quoting Dr. Warren again:

> These countries that were forced to, or had the judgment to, start reflation first have fared best. Australia and the Argentine left the gold standard in 1929 and avoided a large part of the depression. England left the gold standard September 21, 1931, and avoided the worst part of the depression. The United States continued until our entire credit structure collapsed. After such a wreck, recovery is a slow and painful process.
>
> Had we followed the example of England in 1931, conditions would be very different. England had been working toward recovery for 3 years. We therefore had a much more serious injury to recover from, and about half as much time within which to recover.

Failing to compete the devaluation of our dollar to a normal level, we are still at a disadvantage with our competitors in selling our goods in foreign markets. For example, how can our wheat farmers hope to compete successfully in world markets with Argentina when she has devalued her currency 116 percent, compared to our devaluation of 69 percent, which enables her to undersell us?

So long as buyers of commodities in the world market can purchase exports of Japan, Argentina, New Zealand, Australia, Denmark, and our other principal competitors in such markets at lower prices than they can buy our goods, due to the higher value of our money, we will always be at a distinct disadvantage in selling our goods abroad.

The primary cause of the maladjustment of our price structures was the tremendous rise in the value of gold which led to the collapse of commodity prices. The investigations of Dr. Warren and Dr. Pearson have established conclusively the close relationship existing between gold and the commodity price level. These studies, covering a 75-year period prior to the World War, show that when monetary stocks of gold increased faster than the production of other commodities, prices rose; but when stocks of gold increased less rapidly than the production of other goods, prices fell.

From 1914 to 1928, world monetary stocks of gold increased about 38 percent and the world's volume of production also increased 38 percent. With the outbreak of the World War, the demand for gold was greatly lessened because most of the gold using countries left the gold standard.

According to Dr. Warren and Dr. Pearson, under this relationship we might ordinarily expect prewar prices. Actually, however, prices in terms of gold, throughout the world were 40 to 50 percent above the pre-war level. Obviously, if the entire world returned to the prewar gold standard, this price level could not be maintained in terms of gold. Therefore, when all the gold-using countries began to return to the gold basis, a collapse of commodity prices was precipitated.

On April 1, 1924, Sweden returned to the gold basis; Germany, late in 1924; Italy and The Netherlands on April 28, 1925; Belgium on October 25, 1926; and France on June 25, 1928. The increased bidding for gold, resulting from the action of these countries in returning to the gold basis, brought about a tremendous increase in the value of gold.

In the United States the value of gold began to rise in 1926. Between then and 1933, the value of gold more than doubled in our country. Since our currency was still on a prewar gold basis, this meant that other commodity prices, expressed in terms of gold, were cut in half.

Under these conditions, if we kept our currency at a prewar ratio to gold, we had to go either through a complete process of devaluation, or revalue our currency. There was no choice. We either had to devalue prices, wages, taxes, real-estate values, freight rates, utility rates, salaries, bank deposits, and practically everything else, or revalue our currency.

Unfortunately, we waited until the Nation was on the brink of ruin before we stopped this cruel and destructive process of devaluing of goods and services. As a result, our entire economic structure was completely dislocated.

However, prices of all commodities did not drop alike. According to data published by the United States Department of Agriculture, covering the period from 1929 to the spring of 1933, prices of various commodities dropped as follows: Agricultural commodities, 63 percent; agricultural implements, 6 percent; motor vehicles, 16 percent; iron and steel, 20 percent; automobile tires, 33 percent; textiles, 45 percent; food products, 49 percent. Fixed charges, such as debts, taxes, interest, utility rates, and other costs declined comparatively little. Basic commodities and raw materials suffered most. The prices of these commodities fell more rapidly and dropped much lower than the prices of finished materials.

The actions of President Roosevelt, in the spring, summer, and fall of 1933, in placing an embargo on gold exports, withdrawing gold from circulation, abandoning the gold standard, and devaluing the dollar by increasing the price of gold, stopped the deflation, started prices spurting upward, and gave a tremendous impetus to agricultural and industrial recovery.

His actions produced the greatest recovery of prices in any one comparable period in our history. Farm prices and prices of other basic commodities rose faster than the general commodity price level, thus tending to restore price equilibrium.

This process of readjustment of our general price structure has been deterred, however, by the de facto stabilization of our dollar during the past year. Until the dollar is devalued to a normal level in its relation to commodities, debts, and services we cannot expect the restoration of a normal balance in our commodity-price structure. Until we restore such a balance we cannot have a normal exchange of goods and services.

Now, I come to the question of whether devaluation of the dollar is an effective instrument in restoring a normal equilibrium to our price structure. The best evidence in support of this thesis is the record of what has happened to date as a result of such revaluation as we have had.

What would have happened if there had been no devaluation of our dollar? Supposing we had kept our dollar tied to gold at its pre-war value on the basis of $20.67 per ounce. According to the Sauerback-Statist index of wholesale prices for the United States, as revised by Warren and Pearson in Gold and Prices, at page 182, the average index of wholesale prices in the United States in terms of gold in December 1934 was 62 percent of the 1913 price level, or 7 points lower than in February 1933, when the index was 69.

In other words, if there had been no devaluation, and our prices were still based on the pre-war value of gold, our price level now would be lower than it was in February 1933, when the Nation was confronted with ruin. Instead of this situation our price level, in terms of our revalued currency, was 104 percent of the 1913 level.

Without reflation, it is doubtful whether our country could have withstood the shock of completing the paralyzing deflationary processes which were brought to a halt in March 1933 through the action of President Roosevelt in first abandoning the gold standard and later in revaluing our dollar. Without reflation the Nation would have faced bankruptcy.

In 1929 our total wealth was estimated at 362 billion dollars, and our total public and private indebtedness at 203 billion dollars, or 56 percent of our total wealth. Then came the terrific decline in commodity prices which forced down the values of property and securities until by 1932 our national wealth had shrunk to 247 billion dollars while our debt has decreased to about 175 billion dollars, or 71 percent of our total assets.

Warren and Pearson state that—

at the actual market prices in the winter of 1933 the property of the country was probably worth little more than debts. Such a condition of universal bankruptcy was worse than anything which had ever occurred in the United States.

How could farmers pay their debts or even buy the bare necessities of life with wheat at 15 and 20 cents per bushel, corn at 10 cents per bushel, eggs at 10 cents a dozen, butter at 15 to 20 cents per pound, and cotton at 5½ cents per pound? The decline in commodity prices destroyed farm buying power. This, in turn, cut off the market for the goods of the city, throwing millions out of employment. Great numbers of farmers and business men were thrown into bankruptcy by declining prices and high fixed charges.

The deflation of commodity prices inevitably brought about deflation of property and security values, wiping out equities back of loans, throwing banks into insolvency, demoralizing values generally until our whole financial structure collapsed. Banking and finance were paralyzed. Only the courageous and decisive action in abandoning the gold standard and in revaluing the dollar saved our Nation from absolute ruin.

On March 6 the gold standard was suspended but our dollar was pegged at its pre-war gold value in foreign exchanges by means of gold exports. On April 19 the pegging operations were stopped and the value of the dollar immediately fell, seeking its natural level of value in foreign exchange.

This ended deflation. Commodity prices immediately responded with a tremendous surge upward. Security values also soared upward under a tremendous volume of trading on the exchanges. Confidence once more had been restored to commodities and property. Orders for goods began to pour in; factories reopened, providing employment for millions of unemployed. At last the Nation was on the road toward recovery.

On May 12 the Agricultural Adjustment Act was approved by the President, including title III, the so-called "Thomas amendment", authorizing the President to devalue the dollar by changing the gold content up to 50 percent. On June 5 the President approved the act, canceling the gold clause in all public and private contracts.

During the late summer and fall of 1933 a reaction resulted from speculative activities and heavy buying of advanced requirements, which had forced prices upward farther than justifiable. Prices, particularly of basic commodities, slumped.

Up to this time there had been no actual devaluation of our dollar in the sense of reducing its gold content. The disastrous slump in prices in October warned of the necessity for further action in adjusting the dollar to a normal level of value. Accordingly, on October 22, President Roosevelt announced that, in furtherance of his previously declared policy of restoring commodity prices and establishing a stable unit of value, the United States was determined to "take firmly in its own hands the control of the gold value of our dollar."

To further this end he authorized the Reconstruction Finance Corporation to buy gold newly mined in the United States at prices to be determined from time to time and to buy and sell gold in the world market. Purchases of gold began on October 29. This action checked the decline in commodity prices.

On January 30, 1934, the President approved the Gold Reserve Act of 1934. On February 1 he issued an Executive order reducing the gold content of the dollar to 15 5/21 grains of gold nine-tenths fine, which was equivalent to changing the price of gold to $35 per ounce.

What was the result of these actions in revaluing our dollar? From February 1933 to February 1934 the price of gold in the United States advanced 69 percent above par and the wholesale prices of basic commodities, according to the Journal of Commerce Index, advanced 67 percent. What better evidence can I offer of the effectiveness of revaluation of the dollar in restoring commodity prices?

The restoration of commodity prices increased the buying power of farmers and other basic producers, stimulated factory production, and increased trade. Reference to a table which I will append to this statement, entitled "Percent of Change in Business Activity", shows the tremendous impetus given to business revival through dollar revaluation.

Net railroad operating incomes increased 193 percent. New orders for machine tools increased 473 percent. The operations of pig-iron furnaces increased 145 percent. Construction contracts increased 83 percent. Commercial failures decreased 56 percent. Faith and confidence returned to the people.

Our attempts to maintain our dollar at its pre-war value had imperiled our foreign trade. Our exports had slumped to extremely low levels. Most other nations had depreciated their currency, making it difficult for us to sell our goods in foreign markets and making it easier for other countries to sell their goods in our own markets, despite our high tariff barriers.

Revaluation of our dollar immediately stimulated our exports, and retarded the flood of foreign goods pouring into our own markets. During this 1-year period the value of our exports increased 60 percent. Our distinguished Secretary of State, the Honorable Cordell Hull, addressing our Nashville convention, called attention to this fact, saying:

> Now we all recognize that the dollar, being cheaper internally, was of the greatest aid to our exports—especially our agricultural exports—for foreigners then could obtain, at a lower rate of exchange, dollars with which to buy our goods.

Contrary to the dire predictions of the deflationists, the revaluation of our dollar did not destroy public confidence. It restored it. It did not undermine the public credit. It bolstered it. It did not ruin the market for stocks and bonds. It restored the value of stocks and bonds.

The value of all stocks listed on the New York Stock Exchange rose from $19,700,986,000 on March 1, 1933, to $36,348,748,000 on July 1, 1933, and to $36,657,647,000 on March 1, 1934, or an increase of 72 percent in the 1-year period.

The value of all bonds, not including Government securities, listed on the New York Stock Exchange rose from $10,793,948,000 on March 1, 1933, to $12,934,469,000 on July 1, 1933, and to $13,792,675,000 on March 1, 1934, or an increase of 29 percent in the 1-year period.

The increase in the values of these securities has helped to make safer the investments in life insurance, the collateral back of loans, and, therefore, the actual solvency of our banks.

Now, that the program of revaluating our dollar has succeeded so well to date, there should be no hesitancy in finishing the task. It is imperative that this be done so that prices can be brought back into equilibrium. As Walter Lippman points out:

> There is no other way that recovery will take place. Trade is an exchange of goods. If some products fall violently in price and others do not, the exchange cannot take place. To it [rebuilding the price structure] we owe what recovery we have achieved.

We recognize, of course, that revaluation of our dollar is not the sole cause of recovery. As Dr. Warren points out, there are five factors in determining the price level of commodities, the supply of and demand for gold, the supply of and demand for commodities, and changes in the prices of gold. Under the agricultural adjustment program, we are adjusting the supplies of commodities to market demands. The other factors influencing prices must be regulated through a monetary program.

To complete the task of national economic recovery, I earnestly recommend to this committee and to Congress the monetary program of the American Farm Bureau Federation, to which I have already specifically referred. That program calls for the regulation of the value of our money by establishing, first, a definite monetary policy, and, second, by creating the machinery with which to attain the objective desired.

The President now has the authority under the Gold Reserve Act to raise the price of gold from $35 per ounce to $41.34 per ounce. It would appear desirable to give the President further latitude in changing the price of gold, to meet any emergency that might arise, inasmuch as he has already used this power within 18 percent of the maximum limit, and there is still a considerable way to go yet before complete recovery is reached. Then, too, there is always the possibility of further devaluation by foreign countries, which would place us at a serious economic disadvantage.

The most eminent financial authorities tell us that, wherever a nation abandons the gold standard and adopts a managed currency, it can establish any price level it sees fit. On October 3, 1934, the New York Times carried a press dispatch from London, quoting a statement made by Neville Chamberlain, Chancellor of the Exchequer, in an address to London bankers, in which he said that Great Britain's program "has delivered the goods."

He told the bankers that England will keep the pound sterling independent of other currencies, and demonstrated how this program has operated to improve economic conditions in Great Britain. He emphasized the fact that it was not desirable to attach too much importance to the maintenance of sterling at any particular level. He declared, as quoted in this press dispatch:

> We never attempted, and are not now attempting, by means of an equalization fund, to fix exchange at a given point or to maintain it even within fixed limit of values in the face of and in opposition to seasonal or other powerful influences.

President Roosevelt has declared as the objectives of the administration's monetary policy, first, the reestablishment of the commodity price level to a normal level; and, second, the establishment of a commodity dollar that will be constant in purchasing power.

In his message to the World Economic Conference, on July 2, 1933, President Roosevelt said:

> Let me be frank in saying that the United States seeks the kind of a dollar which a generation hence will have the same purchasing and debt-paying power as the dollar value we hope to attain in the near future. That objective means more to the good of other nations than a fixed ration for a month or two in terms of the pound or franc.

In his radio address on October 22 he declared:

> Finally, I repeat what I have said on many occasions, that ever since last March the definite policy of the Government has been to restore commodity price levels. The object has been the attainment of such a level as will enable agriculture and industry once more to give work to the unemployed. It has been to make possible the payment of public and private debts more nearly at the price level at which they were incurred. It has been gradually to restore a balance in the price structure so that farmers may exchange their products for the products of industry on a fairer exchange basis. It has been and is also the purpose to prevent the prices from rising beyond the point necessary to attain these ends. The permanent welfare and security of every class of our people ultimately depend on our attainment of these purposes.

The declarations of policy of the President are in full accord with the policies and recommendations of the American Farm Bureau Federation for an honest dollar.

I have referred to the resolution adopted at the last annual convention of the American Farm Bureau Federation, urging the need for a sound and honest dollar. This resolution has been incorporated in bills introduced by Congressman Goldsborough at various times before this committee. One of these bills, reported favorably by this committee, was passed by the House of Representatives by an overwhelming vote, but killed by reactionary influences in the Senate. I can distinctly remember my standing before this committee, as far back as 1932, and pleading for this very same honest dollar.

In the last Goldsborough bill—H. R. 170—as well as in former ones, such as H. R. 8780, presented during the second session of the Seventy-third Congress, the policies of the American Farm Bureau Federation have been incorporated and to a large degree carried out in existing legislation. It is to the credit of this committee that it had the foresight and courage to fight for the Goldsborough bill.

As in the case of the Goldsborough bills, which for several years have been the basis of our legislative method for obtaining the commodity dollar, the so-called "Thomas amendment" to the Agricultural Adjustment Act, adopted May 12, 1933, during the extraordinary session of Congress in that year, has put into law most of the policies which the American Farm Bureau Federation up to that time, and the Goldsborough bills alike had advocated. For example, we have said for many years that there should be a revaluation of gold so that an ounce of gold would be altered in its value from time to time to keep it more in line with the index numbers of commodities. The Goldsborough bills introduced at various sessions of Congress have contained this provision. It has been accomplished through the Thomas amendment in a manner which permits the President to revalue gold.

To a certain extent President Roosevelt has revalued gold, but has not proceeded to the full extent as authorized in the Thomas amendment. This amendment also authorizes a larger circulation of well-secured Treasury bills and other obligations of the United States under safeguarded conditions as specified in the amendment. The American Farm Bureau Federation has advocated this policy also, and the Goldsborough bills, at different times, have contained provisions permitting the issuance of well-secured circulating media.

The Thomas amendment, as title III of the Agricultural Adjustment Act, further provides that the President can give greater recognition to silver than it has received since the demonetization era in the seventies of the last century. The Goldsborough bills have provided that gold bullion, silver bullion, or both should be kept in the Treasury vaults as the base upon which circulating media should be issued. This has been done.

In the Thomas amendment, the President was authorized, at his discretion, to set up and put into operation what is commonly known as the "commodity dollar." This has been the main objective of all of the Goldsborough bills for several years. The commodity dollar has been the central policy of the monetary reforms urged by the American Farm Bureau Federation for the last half decade. Although I rejoice in all the monetary reforms which have been put into effect I am not content, as the official spokesman for a great farm organization, with just a partial program. Our organization is asking that the entire program, as exemplified in our resolutions, policies, and recommendations, be put into effect.

The time is now ripe for Congress to exercise its constitutional mandate to put the desired monetary policy for this country into effect. Congress has placed discretionary powers in the hands of the President to control the value of the dollar. Legislation now is before this body proposing to enlarge the control of the Federal Reserve Board over the volume and price of credit. But no objective has been set as the definite goal of the Government's monetary and credit policies.

Therefore, I appear again before this committee to support H. R. 170, introduced by Congressman Goldsborough, respectfully insisting that the one great, outstanding feature of monetary reform which, in my judgment, is more important and will be more effective in raising commodity prices than all other monetary reforms we have thus far received, be put into practical effect by incorporating the principle of the commodity dollar as a part of the banking act of 1935.

On behalf of the American Farm Bureau Federation, I recommend that Congress definitely declare its policy by the establishment of the commodity dollar, restored to a normal value, and stabilized at that value on a basis which will enable it to function as a fair medium of exchange. Surely Congress will not permit the reoccurrence of those extreme fluctuations in the value of our currency which have caused alternating periods of inflation and deflation. Surely, we have learned our lesson during this depression from which we are just emerging. We must be convinced now that steps must be taken to prevent these economic catastrophes from occurring in the future.

The way now is open. Never before have we had a more favorable opportunity for establishing a stable medium of exchange. Gold has been withdrawn from circulation and is now held as a reserve back of our currency. It is now possible to regulate the value of gold, and hence the commodity price level, by varying its price in terms of gold from time to time. Now that gold is withdrawn from circulation it becomes a simple matter to change the gold content of the dollar merely by changing the price of gold expressed in dollars. It is no longer necessary to coin gold dollars. Change in the gold content of the dollar therefore can be adjusted without the mechanical difficulty involved when gold coins were in circulation.

I want to call your specific attention to that portion of H. R. 170 which describes the commodity dollar. It is section 4, on page 7 of the bill as printed. In discussing the declaration of policy relative to the commodity dollar, so ably presented in this section, it occurs to me that we should amend it at least in three ways. Then, when it is put into effect, it will work with that precision which we expect of it, in relation to improving commodity prices, and holding such prices at more stable levels than they have been held at in former years.

The first amendment that I wish to suggest deals with the year which should be used in measuring future commodity prices. The year 1926, as stated in the present bill, is not a very good yardstick to use in measuring or determining what our future prices should be. I confess that 1926 was a fairly good year for agriculture. But I remember also that cotton and tobacco, not to name any more crops, were not very profitable that year. It seems to me it is much safer to include a period of several years for determining what our commodity prices should be rather than by comparison with one particular year as being the desirable year.

Consequently, would it not be desirable to strike out the year "1926" and insert in lieu thereof "1921 to 1929, inclusive"?

The second amendment which I desire to present to the committee relates to the use of an index which is commonly known as the "one prepared by the United States Bureau of Labor Statistics." I am not opposed to the use of that index for certain purposes. But it has too many commodities in it which are under monopolistic control and which influence this index unduly. The index is not fluid and elastic enough to keep in step with the price changes experienced by some of our basic products and raw materials.

Therefore, it seems to me to be advisable to give the regulatory authority which is to administer the proposed act, whether it be the Treasury Department, the Federal Reserve Board, or a separate monetary authority, permission to formulate a special basic commodity index. Therefore I suggest that somewhat of the following language be included in paragraph (*b*) of section 4:

> An index of the purchasing power of the dollar shall be compiled by authority of the Federal Reserve Board, or the Secretary of the Treasury, to contain not less than 30 nor more than 50 major raw materials and basic products entering into commerce and industry.

It is well known that raw materials and the basic products, including more than agricultural materials and products, tend to fluctuate easier and with greater rapidity in price extremes than is true for some of the manufactured products now included in the seven or eight hundred commodities used by the Bureau of Labor Statistics in making up its commodity index.

Another reason which I submit for limiting the number of commodities is that too many of those now included in the list employed by the Bureau of Labor Statistics are monopolistically controlled. Such commodities do not properly reflect the true price situation of the raw materials that enter into these products, or of the basic products which they represent when offered for sale.

The amendment I have suggested would have the effect of making the commodity dollar mechanism very sensitive to price changes. If we should adopt a mechanism which would require revaluation of the dollar too often, as a method of keeping its purchasing power in line with the wholesale prices of the commodities used in the index, we might run into some danger of facing an impractical situation. I recommend, therefore, that the adjustment of the value of the dollar in relation to wholesale prices of commodities should be made virtually automatic to changes in the general commodity price level.

To make this plan automatic in its operations, may I suggest a third amendment, which might be known as "paragraph (d) of section 4", and which would read as follows:

> When this index of commodity prices fluctuates 10 percent above or below the average index of all commodities for the period 1921 to 1929, inclusive, the authority shall adjust the purchasing power of the dollar by increasing or decreasing the number of grains of gold in the dollar, or by increasing or decreasing the price of gold: *Provided*, That after 2 years from the date this act becomes effective the authority shall adjust the purchasing power of the dollar when the index of commodity prices fluctuates 5 percent above or below such index.

The purpose of this amendment is to provide a tolerance for 2 years of 10 percent above what I call the index of wholesale prices, or below that index; in all, a tolerance of 20 percent. It may be advisable to give the administrative agency of the proposed act some latitude in changing the value of the dollar. We do not want to revalue the dollar every time there is a variation of a trifling percent above or below the index.

To start with, 10 percent tolerance seems logical. After 2 years of operation, however, the tolerance should drop to 5 percent. Thereafter, if the prices on the commodities used should vary less than 5 percent from the commodity index, nothing would be done about it by the administrative agency. The administrative agency would adjust the purchasing power of the dollar only when there was a variation of 5 percent above or 5 percent below the index.

These amendments do not in the least change the basic principles of our declared policy for this monetary reform. They are merely designed to make it easier to administer the policy we advocate.

I believe the plan we are advocating is the soundest and most effective way to achieve the goal we have sponsored for a long time. It is the plan we have tried out so successfully during the past 2 years. It has proved its worth in our most severe financial and economic crisis. Any plan which can check the worst deflation in our history and bring about the greatest price restoration in the history of this country is not only worth continuing but should be perfected as a permanent monetary policy.

Adoption of this plan, which is most fundamentally sound, will go far in heading off movements for inflation by the printing-press methods. It is not necessary to discuss the disastrous results which always follow in the wake of inflation by the printing-press route. Yet, in view of the fact that many of our citizens are beset with financial difficulties, and are exorted constantly by demagogues promising easy money by the simple process of printing it, the movement for this unsound inflation may reach alarming proportions unless sound action is taken immediately to correct present maladjustments.

In conclusion, let me appeal to this committee and to this Congress and to the President to take speedy action in the completion of the declared monetary policy of this administration as voiced by President Roosevelt. I want to urge haste in restoring a normal balance to our price structure.

Our public debts have grown rapidly. Today 20 million people are on governmental relief. Ten million citizens are still unemployed. Our price structure is out of balance. It is impossible to resume the normal exchange of goods and services. To many of our distressed citizens, ready for desperate remedies, no matter how badly conceived they are, or how certainly they are doomed to failure, unsound and pernicious plans are being offered almost daily. The situation is a critical one and requires speedy action with which to meet it.

If this action is taken along the lines we recommend, farmers can once more buy the goods of industry. Producers of basic commodities, with profits in sight and orders contemplated, can resume normal operations. The unemployed can once more have the opportunity of going to work. Government unemployment subsidies can be eliminated. Increased income and increased property and security values will yield greater tax revenues, making it possible to balance the governmental budgets, and perhaps even begin paying off our accumulated debts.

The best way to prevent our country from being forced into extreme measures, either by the pressure of unbalanced budgets and unemployment, or by the popular clamor that may be aroused in support of ill-advised schemes, which will ultimately destroy our chances of immediate recovery, and possibly bring us to ruin, is to speed up the monetary program which President Roosevelt announced in 1933, and which has proved to be so potent in stimulating recovery to the degree in which it has been employed to date.

I thank you, Mr. Chairman, and gentlemen, for your patience in listening to me.

I submit the following tables as a part of my statement:

Percent change in business activity February 1933 to February 1934[1]

[From Gold and Prices, Warren and Pearson]

	February 1933	February 1934	Percent change
Machine tools, new orders, index	15	86	473
Net railroad operating income	$9,802,000	$28,700,000	193
Price second-grade rail bonds, percentage of par	25.7	71.22	183
Corporation profits [2]	$124,000,000	$315,000,000	154
Pig-iron furnaces in blast, capacity, long tons per day	18,910	46,260	145
Pig-iron production, long tons	554,000	1,264,000	128
Pneumatic-tire production, numbers	1,871,000	4,205,000	125
Automobile production, total number	107,000	235,000	120
Factory employment, Detroit, index	49.2	99.1	101
Crude-rubber consumption, total long tons	18,825	36,548	94
Contracts awarded, all types of construction	$53,000,000	$97,000,000	83
Pay rolls, factory, Pittsburgh index	26.4	46.5	76
Wool looms, carpets and rugs, percent capacity	23	40	74
United States stocks, total market value [3]	$22,694,000,000	$36,606,000,000	61
Value of exports, including reexports	$101,530,000	$162,805,000	60
Forest products, carloadings	13,800	21,800	58
Coke production, beehive and by-product, short tons	1,723,000	2,611,000	52
Paint sales, total (558 estab.)	$11,666,000	$17,715,000	52
Value of imports, total	$83,803,000	$125,292,000	50
Factory pay-roll index [4]	40	59.2	48
Contracts awarded, all types of construction, number	3,884	5,507	42
J. C. Penny Stores, sales	$8,455,000	$11,745,000	39
Mail-order and store sales	$26,194,000	$36,016,000	37
Factory employment, iron and steel industry, index [5]	48.9	66.4	36
Factory employment, nonferrous metas, index [5]	52.6	70.1	33
Newsprint consumed, short tons	116,307	153,958	32
Factory employment, lumber and by-products, index [5]	36.9	48.4	31
Shipments of cement, barrels	2,278,000	2,952,000	30
Factory employment, adjusted index [5]	61.7	78.4	27
Pittsburgh, index	57.6	73.4	27
Unadjusted, index	59.2	74.7	26
Bathroom accessories, production, number of pieces	121,070	147,407	22
Pullman passengers carried	952,000	1,132,000	19
Freight carloadings, total cars	492,600	577,200	17
Price high-grade rail bonds, percentage of par	81.92	95.19	16
Net demand deposits	$9,996,000,000	$11,398,000,000	14
Value, all listed American bonds except governments [3]	$11,791,000,000	$13,448,000,000	14
Electric-power production, kilowatt-hours [6]	6,297,000,000	7,049,000,000	12
Newspaper advertising, 52 cities, lines	72,539,000	80,788,000	12
Insurance written, total value	$609,725,000	$648,073,000	6
Freight car surplus, total	650,000	375,000	−42
Commercial failures, number	2,378	1,049	−56
Liabilities, total	$65,576,000	$19,445,000	−70

[1] Date taken from Survey of Current Business, April 1934, vol. 14, no. 4, and other issues.

[2] The March quarterly figures are used. The datum for March 1934 was obtained from a letter from Alfred Inge. It is a prliminary figure.

[3] Data from New York Stock Exchange Bulletin, vol. IV, no. 2, pp. 3, 8, February 1933; vol. V, no. 2, pp. 3, 8, February 1934. The figure for the all American bonds except Governments is obtained by subtracting the total market value of United States Federal and Sub-Government bonds from the total market value of all American listed bonds.

[4] Federal Reserve Board unadjusted index.

[5] Data from Federal Reserve Bulletin, vol. 20, no. 6, pp. 326 ff., June 1934.

[6] Revised series, Survey of Current Business, p. 38, May 1934.

Index numbers of the price of gold in various countries, February 1933–November 1934

[Par=100]

Country	February 1933	November 1934
Czechoslovakia	100	120
Austria	100	127
India	141	165
England	142	165
South Africa	144	167
Canada	120	165
Sweden	147	176
Finland	169	193
Denmark	176	203
New Zealand	178	207
Australia	179	208
Argentina	165	216
Japan	240	290
United States	100	169

Changes in average prices of identical basic commodities in various countries in currency and in gold from February 1933 to February 1934

[From Gold and Prices, Warren and Pearson]

Country	Number of identical commodities	Percentage change in currency prices	Percentage change in the price of gold	Percentage change in pr. es in terms of gold
France	21	+5.5	0	+5.5
United States		+64.2	+69	+2.8
Italy	20	+1.9	0	+1.9
United States		+69.6	+69	+ .4
Belgium	9	+3.3	0	+3.3
United States		+69.6	+69	+ .4
Holland	16	+16.7	0	+16.7
United States		+78.5	+69	+5.6
Switzerland	22	+7.9	0	+7.9
United States		+80.4	+69	+6.7
England	22	+13.5	+13	+ .4
United States		+73.4	+69	+2.6
India	13	+1.6	+14	−10.9
United States		+64.2	+69	−2.8
Canada	17	+40.4	+40	+ .3
United States		+78.3	+69	+5.5
Czechoslovakia	23	+6.8	+11	−4.7
United States		+69.1	+69	+ .06
Japan	10	+20.7	+16	+4.1
United States		+63.9	+69	−3.0
Austria	22	+15.6	+25	−7.5
United States		+81.8	+69	+7.6
Germany	23	+13.8		
United States		+73.8	+69	+2.8

Mr. O'NEAL. Mr. Chairman, may I also be allowed to put into the record a statement of policy of the National Agricultural Conference, a group which is composed of the National Grange, the American Farm Bureau Federation, the National Cooperative Council, Farmers National Grain Corporation, a cooperative and a representative of American Association of Agricultural Editors.

I would like, if I may, to have permission to put that in the record.

The CHAIRMAN. Without objection, it is so ordered.

(The statement above referred to is as follows:)

STATEMENT OF THE NATIONAL AGRICULTURAL CONFERENCE

To the President of the United States, Congress of the United States, Secretary of Agriculture, Secretary of Interior, Governor of Farm Credit Administration, and Administrator of the Agricultural Adjustment Administration:

Restoration of farm buying power by the regulation of the value of money, and by the Agricultural Adjustment Administration, Farm Credit Administration, and other agencies has been the most potent of all recovery measures.

Agriculture can be of more powerful assistance to national recovery as rapidly as restoration of its prices to parity brings about a normal balance of income between city and country.

We urge intensification of present efforts to increase farm income. Every item of national policy should be carefully weighed as to its effect on agriculture. Such policies as price fixing in industry and unduly high wages on public works tend to retard recovery. We commend steps that have been taken to correct these policies.

Artificial and excessive limitation of production by industry and labor, with the help or permission of government, coupled with shrinkage in foreign markets, has forced agriculture to curtail its production in order to exist.

The policy must continue until other factors have demonstrated their ability to raise and sustain farm prices. We urge that all possible efforts be made to develop foreign trade, develop industrial uses of farm products, raise quality of standards, reduce distribution costs, all to the end that farm income may be increased without further curtailment of production.

We favor the continuance of farm-production control for the time being, and urge simplification of present plans and especially the correction of inequities in allotments.

Further increase in farm prices until they reach parity, and reduction in industrial prices which higher production will make possible, are the most important measures of recovery and reemployment, and should be pushed forward with the whole power of the administration.

To aid in carrying out the above declaration of policy, we favor the following objectives:

With regard to the Agricultural Adjustment Act and its administration, we recommend:

1. Authority to make benefit payments in kind.
2. Remove the present requirements to make benefit payments when processing taxes are imposed.
3. Strengthen the marketing agreement and licensing sections of the act by clarifying the provisions with respect to interstate commerce, and by authorizing the Secretary to prescribe licenses for the enforcement of marketing agreements adopted only by producers.
4. Modify the definition of "parity" to take account of taxes, interest, and labor costs.
5. Authorize the use of cooperatives in the handling and disposal of surpluses to the extent of which they are capable.

L. J. TABER,
Master of the National Grange.
EDW. A. O'NEAL,
President, American Farm Bureau Federation.
M. W. THATCHER,
Washington representative Farmers' National Grain Corporation.
JOHN O. MILLER.
President, National Cooperative Council.
CLIFFORD GREGORY,
Representative, American Association of Agricultural Editors.

Mr. GOLDSBOROUGH. Have you any information as to the attitude of the Farmers' Union as to the suggestions you have made this morning?

Mr. O'NEAL. Congressman Goldsborough, the Farmers' Union was invited to sit as a member of the farm-conference group, but refused on the premise that they could not go along with us unless we were against something, unless we were against the Agricultural Adjustment Act and agreed to come out against it they would not cooperate with us.

We have asked them on several occasions if they would come into the farm-conference group, because they represent many farmers in the country. Through what is known as the "Farmers' National Grain Cooperative" there are 7 or 8 or more farmers' union States of the far West which cooperate with the grain group. In other words, they have several farmers' union leaders in our members, not as a national farm union group, but as part of one of the national cooperatives.

Mr. GOLDSBOROUGH. I heard your statement up until the time you said what you were going to recommend, when I had to temporarily leave the room. Did you intend to suggest to the committee how you think, or how your organization thinks your suggestions, if adopted by the committee, should be incorporated in the bill? Will your suggestions replace any title of the bill, or will they consist of additional titles?

Mr. O'NEAL. Congressman Goldsborough, of course, that is at your option or the option of the committee. We suggested it as an amendment of section 2, or at any place where you think it should go. We definitely want it as a part of the bill, but anywhere you think it should go. We offer it as a suggestion which we think will make the bill really worth while.

You not only want to set up this machinery, but you want to be able to handle the machinery so it will be effective. Without any criticism of the bill at all, we think, in order to make it complete, it should contain this amendment.

Mr. FORD. You set up the income of the farmers in 1918 as $18,000,000,000; is that correct?

Mr. O'NEAL. 1919, $16,900,000,000.

Mr. FORD. And you set up the farmers' income in 1929 as $11,000,000,000?

Mr. O'NEAL. Yes, sir.

Mr. FORD. And in 1934 as $7,000,000,000?

Mr. O'NEAL. Yes. sir.

Mr. FORD. Do you not think the income of the farmers in 1918 was largely influenced by the fact that there was a tremendous foreign demand for cotton, corn, wheat, and tobacco?

Mr. O'NEAL. Yes, sir; that was a great factor.

Mr. FORD. And the lack of income in 1934 is measurably due to the fact that there is no longer any foreign demand for those products; and also, did not the refusal or inability of foreign governments to pay their debts have some effect on the situation?

Mr. O'NEAL. You know it is mighty hard to ask the farmer why he did not pay his debts.

Mr. FORD. I did not mean the farmers.

Mr. O'NEAL. I think it was because of the great lack of buying power in those nations, and because we have become a creditor Nation. Those people are hungry over there, and if they had the money to buy they would buy.

If we had a tariff system that would allow us to trade and a monetary policy that would help us in trading, as I said in my statement, I think there would be a different situation.

But I have shown that we have had quite an increase in foreign trade under the present monetary policy. But if you go into any little corner store down town you will see goods marked "Made in Japan" on the counters. If you go to some of our eastern cities you will find agricultural commodities that have come in from Europe.

Mr. HANCOCK. Do you think that the Banking Act of 1935 should contain a declaration of policy?

Mr. O'NEAL. Yes, Congressman; I think it should define our monetary system as well as furnish the machinery for handling sound money.

Mr. CLARK. Have you seen the proposed amendment that Governor Eccles presented as a suggestion to this committee?

Mr. O'NEAL. I do not know that I have. There have been so many suggestions, and the testimony is so voluminous, that I do not know whether I have seen that or not.

Mr. GOLDSBOROUGH. The suggestion was as to a declaration of policy.

Mr. O'NEAL. I have not seen it. I would be very happy if he would adopt ours, which has been so effective.

Mr. CLARK. Of course, he does not believe, if I understood his testimony correctly, that through monetary control alone you could bring about a stable price level. As I recall, his amendment declares it to be the legislative policy to bring about a stable price level, full employment, and stable business conditions, insofar as it can be done through monetary action. I was wondering what your position would be as to that.

Mr. O'NEAL. That is fine. I hope the distinguished Governor, whom I have not had the pleasure of meeting, could recommend ours. That was the purpose of the Goldsborough philosophy, as proved by this administration, and it has certainly shown what it will do. There is no question about that.

It seems to me that the distinguished Governor of the Federal Reserve Board cannot afford to miss overlooking what other great nations are doing today. In other words, we are not so awfully smart after all. The other fellows got to this before we did and they have had some remarkable results. It seems to me that should furnish a precedent for the Governor of the Federal Reserve Board.

Mr. CLARK. He has no objection to a declaration of policy, only he does not believe that you can put a specific declaration in the bill, that you must leave some latitude, rather than try to fix any one year as the desirable year to aim at as far as the price level is concerned. I believe that is your suggestion, too.

Mr. O'NEAL. Our suggestion is the period from 1921 to 1929.

Mr. CROSS. I want to get your reaction to this thought. I am of the opinion that the Federal Reserve Board, while I have great faith in the present Governor, that Board, according to my view of the situation, are naturally inclined, judging by the previous testimony of members of the Board, to have the idea that they are to look after the banking of the country. The banking of the country is a private moneymaking institution, after all is said and done. They do not feel, it seems to me, that they have a direct responsibility for stabilizing the value of money, or regulating the value of money, and furnishing the country with an adequate medium of exchange. So I think it would be far better if there were an independent agency representing Congress, furnishing the country with an adequate medium of exchange, whose prime purpose is that not of the business of banking, or dealing with so much with banking. What do you think of that?

Mr. O'NEAL. Sometimes I frankly feel that the Federal Reserve Board, from my observation as the head of a farm organization and a private citizen, has not loved agriculture very much, and has not served banking very well. That would be my answer.

In other words, I was thinking, whatever the wisdom of your committee might decide, of the sort of authority you have, that you should follow the Constitution, and really coin money and regulate the value thereof, and keep it in the hands of an agency that serves the people of the United States, and no particular group.

Of course, the bankers have their rights as public servants, but at the same time, no Congress or President should take away the constitutional authority given you gentlemen here to regulate money.

I think I will have to ask you to excuse me now, Mr. Chairman, as I have to go to the White House. If I may be excused, I would like to leave, and let you hear some of the other witnesses. I will be glad to come back this afternoon, if you like. But we have a couple of other farm witnesses here, including Mr. Sexauer, of the Dairymen's League of New York, who will speak for the Cooperative Council, and Mr. Ed Foster, of New York, who will speak for the American Farm Bureau Federation, as the secretary of the New York State federation. So may I ask you to excuse me at this time, as I am due at the White House at 12:15 o'clock.

The CHAIRMAN. We will excuse you now. We thank you for your assistance to the committee.

STATEMENT OF FRED H. SEXAUER, PRESIDENT DAIRYMEN'S LEAGUE COOPERATIVE ASSOCIATION, NEW YORK CITY

The CHAIRMAN. We have Mr. Sexauer of the National Cooperative Council, whom we shall be glad to hear.

Mr. SEXAUER. My name is Fred H. Sexauer. I am president of the Dairymen's League Cooperative Association, representing the National Cooperative Council. In presenting a brief statement which I have here I will be very glad to have anyone ask any questions about it as it is read or afterwards if they so desire.

The CHAIRMAN. You may proceed.

Mr. SEXAUER. The National Cooperative Council, which is the organization which I represent here today, is composed of the large national commodity organizations handling such commodities as cotton, milk and its products, citrus and deciduous fruits, field seeds, rice, livestock, nuts, poultry, tobacco, vegetables, melons, wool, and associations of organizations purchasing farm supplies. In addition it has as associated members several State agricultural councils and State associations of cooperative organizations. These national associations are in turn made up of several hundred territorial cooperative associations. Thus, in total representation, the National Cooperative Council represents a large percentage of the total cooperative business in the United States.

(A list of the member organizations is as follows:)

MEMBERS OF NATIONAL COOPERATIVE COUN

CITRUS FRUIT DIVISION

California Fruit Growers Exchange, Box 530, Station C, Los Angeles, Calif. (including 230 cooperatives): Mutual Orange Distributors, Redlands, Calif. (including 30 cooperatives).

COTTON DIVISION

American Cotton Cooperative Association, 535 Gravier Street, New Orleans, La.
- Alabama Farm Bureau Cotton Association, Montgomery, Ala.
- Brazos Valley Cotton Cooperative Association, Bryan, Tex.
- California Cotton Cooperative Association, Box 416, Bakersfield, Calif.
- Georgia Cotton Growers Cooperative Association, 746 Glenn Street SW., Atlanta, Ga.
- Louisiana Farm Bureau Cotton Association, 535 Gravier Street, New Orleans, La.
- Mid-South Cotton Growers Association, Box 44, Memphis, Tenn.
- Mississippi Cotton Cooperative Association, Jackson, Miss.
- North Carolina Cotton Growers Association, Raleigh, N. C.
- Oklahoma Cotton Growers Association, Oklahoma City, Okla.
- South Carolina Cotton Growers Cooperative Association, Columbia, S. C.
- South Texas Cotton Cooperative Association, Corpus Christi, Tex.
- Southwestern Irrigated Cotton Growers Association, El Paso, Tex.
- Texas Cotton Cooperative Association, 1100 South Ervay Street, Dallas, Tex.
- West Texas Cotton Growers Association, Abilene, Tex.

DAIRY DIVISION

National Cooperative Milk Producers Federation, 1731 Eye Street NW., Washington, D. C. (consisting of the following member organizations, together with approximately 900 affiliated local cooperatives):
- Berrien County Milk Producers' Association, Benton Harbor, Mich.
- California Milk Producers' Association, 947 Maple Avenue, Los Angeles, Calif.
- Cedar Rapids Cooperative Dairy Co., 560 Tenth Street SW., Cedar Rapids, Iowa.
- Challenge Cream & Butter Association, 925 East Second Street, Los Angeles, Calif.
- Champaign County Milk Producers. 24 Taylor Street, Champaign, Ill.
- Colorado Dairymen's Cooperative, Inc., 642 Lawrence Street, Denver, Colo.
- Connecticut Milk Producers Association, 450 Asylum Street, Hartford, Conn.
- Consolidated Milk Producers for San Francisco, 740 Pacific Building, San Francisco, Calif.
- Cooperative Pure Milk Association, Plum and Central Parkway, Cincinnati, Ohio.
- Coos Bay Mutual Creamery Co., Marshfield, Oreg.
- Dairy and Poultry Cooperatives, Inc., 110 North Franklin Street, Chicago, Ill.
- Dairymen's Cooperative Sales Association, 451 Century Building, Pittsburgh, Pa.
- Dairymen's League Cooperative Association, Inc., 11 West Forty-second Street, New York, N. Y.
- Des Moines Cooperative Dairy Marketing Association, 1935 Des Moines Street, Des Moines, Iowa.
- Dubuque Cooperative Dairy Marketing Association, Inc., 1020 Central Avenue, Dubuque, Iowa.
- Evansville Milk Producers' Association, Inc., 214 Boehne Building, Evansville, Ind.
- Falls Cities Cooperative Milk Producers' Association, 229 Bourbon Stock Yards Building, Louisville, Ky.
- Georgia Milk Producers' Confederation, 156 Alabama Street SW., Atlanta, Ga.
- Illinois-Iowa Milk Producers' Association, room 24, Schmidt Building, Davenport, Iowa.

National Cooperative Milk Producers Federation, etc.—Continued.

- Indiana Dairy Marketing Association, Muncie, Ind.
- Inland Empire Dairy Association, 1803 West Third Avenue, Spokane, Wash.
- Interstate Associated Creameries, 1319 Southeast Twelfth Avenue, Portland, Oreg.
- Inter-State Milk Producers' Association, Inc., 219 North Broad Street, Philadelphia, Pa.
- Land O'Lakes Creameries, Inc., 2201 Kennedy Street NE., Minneapolis, Minn.
- McLean County Milk Producers' Association, 411–413 North Center Street, Bloomington, Ill.
- Maryland and Virginia Milk Producers' Association, 1731 Eye Street NW., Washington, D. C.
- Maryland State Dairymen's Association, 810 Fidelity Building, Baltimore, Md.
- Miami Valley Cooperative Milk Producers' Association, 136–138 West Maple Street, Dayton, Ohio.
- Michigan Milk Producers' Association, 406 Stephenson Building, Detroit, Mich.
- Mid-West Producers' Creameries, Inc., 907 Lemcke Building, Indianapolis, Ind.
- Milk Producers' Association of San Diego County, 354 Eleventh Avenue, San Diego, Calif.
- Milk Producers' Association of Summit County and Vicinity, 145 Beaver Street, Akron, Ohio.
- Milwaukee Cooperative Milk Producers, 1633 West Thirteenth Street, Milwaukee, Wis.
- National Cheese Producers' Federation, Plymouth, Wis.
- Nebraska-Iowa Non-Stock Cooperative Milk Association, 2410 Dodge Street, Omaha, Nebr.
- New England Milk Producers' Association, 51 Cornhill, Boston, Mass.
- Northwestern (Ohio) Cooperative Sales Co., 2221½ Detroit Avenue, Toledo, Ohio.
- O. K. Cooperative Milk Association, Oklahoma City, Okla.
- Peoria Milk Producers, Inc., 208–210 East State Street, Peoria, Ill.
- Pure Milk Association, 608 South Dearborn Street, Chicago, Ill.
- Pure Milk Producers' Association, 853 Live Stock Exchange Building, Kansas City, Mo.
- Pure Milk Products Cooperative, 110 East Main Street, Madison, Wis.
- Richmond Cooperative Milk Producers' Association, 605 East Canal Street, Richmond, Va.
- St. Joseph, Mo., Milk Producers' Association, 403 Ballinger Building, St. Joseph, Mo.
- Sanitary Milk Producers, Room 609, Chamber of Commerce Building, 511 Locust Street, St. Louis, Mo.
- Scioto Valley Cooperative Milk Producers' Association, 303 Grand Theater Building, Columbus, Ohio.
- Shelby County Milk Producers' Association, 1039 South Bellevue, Memphis, Tenn.
- South Texas Producers Association, 912 Bankers Mortgage Building, Houston, Tex.
- Stark County Milk Producers' Association, Canton, Ohio.
- Tillamook County Creamery Association, Tillamook, Oreg.
- Tulsa Milk Producers' Cooperative Association, 1120 North Boston Street, Tulsa, Okla.
- Twin City Milk Producers' Association, 2402 University Avenue, St. Paul, Minn.
- Twin Ports Cooperative Dairy Association, 6128 Tower Avenue, Superior, Wis.
- United Dairymen's Association, 635 Elliott Avenue, West Seattle, Wash.
- Valley of Virginia Cooperative Milk Producers' Association, Harrisonburg, Va.

DECIDUOUS FRUITS DIVISION

American Cranberry Exchange, 90 West Broadway, New York, N. Y.:
- Growers Cranberry Co., 730 Drexel Building, Philadelphia, Pa.
- New England Cranberry Sales Co., 9 Station Street, Middleboro, Mass.
- Wisconsin Cranberry Sales Co., Wisconsin Rapids, Wis.

California Fruit Exchange, box 2038, Sacramento, Calif. (including approximately 300 local deciduous fruit cooperatives).

DRIED AND CANNED PRODUCTS DIVISION

California Prune and Apricot Growers Association, San Jose, Calif. (including 30 local cooperatives).

Hillsboro-Queen Anne Cooperative Corporation, 31 South Salvert Street, Baltimore, Md. (including 10 local units).

Sun-Maid Raisin Growers of California, Fresno, Calif.

FIELD SEEDS DIVISION

Egyptian Seed Growers Exchange, Flora, Ill.

GRAIN DIVISION

American Rice Growers Association, Lake Charles, La.

LIVESTOCK DIVISION

National Livestock Marketing Association, 160 North La Salle Street, Chicago, Ill. (consisting of the following livestock marketing associations serving nearly 1,000 livestock shipping associations):
- Chicago Producers Commission Association, Union Stockyards, Chicago, Ill.
- Eastern Live Stock Cooperative Marketing Association, Inc., Baltimore, Md.
- Evansville Producers Commission Association, Evansville, Ind.
- Farmers Union Live Stock Commission Co., South St. Paul, Minn.
- Illinois Live Stock Marketing Association, 608 South Dearborn Street, Chicago, Ill.
- Intermountain Live Stock Marketing Association, Denver, Colo.
- Iowa Live Stock Marketing Corporation, Des Moines, Iowa.
- Michigan Live Stock Exchange, Detroit, Mich.
- National Order Buying Co., 85 East Gay Street, Columbus, Ohio.
- Oklahoma Live Stock Marketing Association, Oklahoma City, Okla.
- Pacific States Live Stock Marketing Association, San Francisco, Calif.
- Peoria Producers Commission Association, Peoria, Ill.
- Producers Commission Association, Live Stock Exchange Building, Indianapolis, Ind.
- Producers Commission Association, Sioux City, Iowa.
- Producers Commission Association, 100 Live Stock Exchange Building, Kansas City, Mo.
- Producers Cooperative Commission Association, Live Stock Exchange Building, Cleveland, Ohio.
- Producers Cooperative Commission Association, 1139 William Street, East Buffalo, N. Y.
- Producers Cooperative Commission Association, Live Stock Exchange Building, Cincinnati, Ohio.
- Producers Cooperative Commission Association, Union Stock Yards, Pittsburgh, Pa.
- Producers Live Stock Commission Association, National Stock Yards, Ill.
- Producers Live Stock Commission Co., Springfield, Ill.
- Producers Live Stock Marketing Association, South St. Joseph, Mo.
- Producers Live Stock Marketing Association, Louisville, Ky.
- Texas Live Stock Marketing Association, Fort Worth, Tex.

NUT DIVISION

California Walnut Growers' Association, 1745 East Seventh Street, Los Angeles, Calif.
National Pecan Growers Exchange, Albany, Ga
National Pecan Marketing Association, Macon, Ga. (including 25 regional pecan cooperatives).

POULTRY DIVISION

Idaho Egg Producers, Caldwell, Idaho.
Northwestern Turkey Growers Association, Salt Lake City, Utah
- Colorado Poultry Association, Grand Junction, Colo.
- Cloud Peak Cooperative Association, Sheridan, Wyo.
- Idaho Egg Producers, Caldwell, Idaho.
- Nevada Turkey Growers Association, Fallon, Nev.
- Northern Montana Poultry Growers Association, Havre, Mont.
- Oregon Turkey Cooperatives, Inc., 1319 Southeast Twelfth Avenue, Portland, Oreg.
- San Juan Turkey Growers Association, Allison, Colo.
- Southern Montana Turkey Growers Association, Bozeman, Mont.
- Utah Poultry Producers Cooperative Association, Salt Lake City, Utah.
- Washington Cooperative Egg and Poultry Association, 201 Elliott Avenue, West, Seattle, Wash.

Pacific Egg Producers Cooperative, Inc., 178 Duane Street, New York, N. Y.:
- Pacific Cooperative Poultry Producers, 360 East Ash Street, Portland, Oreg.
- Poultrymen's Cooperative Association of Southern California, 1513 Mirasol Street, Los Angeles, Calif.
- Poultry Producers of Central California, 840 Battery Street, San Francisco, Calif.
- San Diego Cooperative Poultry Association, 50 Twenty-second Street, San Diego, Calif.
- Washington Cooperative Egg and Poultry Association, 201 Elliott Avenue, West, Seattle, Wash.

Utah Poultry Producers Cooperative Association, Salt Lake City, Utah.

PURCHASING DIVISION

Cooperative G. L. F. Exchange, Ithaca, N. Y. (including more than 100 local units).
Eastern States Farmers Exchange, Springfield, Mass. (serving a number of local units).
Farm Bureau Services, Inc., 221 North Cedar Street, Lansing, Mich (serving nearly 100 local units).
Fruit Growers Supply Co., 607 South Hill Street, Los Angeles, Calif. (serving 230 local cooperatives).
Indiana Farm Bureau Cooperative Association, Farm Bureau Building, Indianapolis, Ind. (serving nearly 100 county cooperatives).
Ohio Farm Bureau Service Co., 620 East Broad Street, Columbus, Ohio (serving 50 local units).
Producers Cooperative Exchange, Glenn Building, Atlanta, Ga.
Southern States Cooperative, Inc., Richmond, Va. (serving a number of local units).
Union Oil Co. (cooperative), North Kansas City, Mo. (serving several hundred farmers' oil cooperatives).
West Virginia Farm Bureau Service Co., 756 Empire Bank Building, Clarksburg, W. Va. (serving a number of local cooperatives).

TOBACCO DIVISION

Eastern Dark Fired Tobacco Growers Association, Springfield, Tenn.
Maryland Tobacco Growers Association, Conway and Charles Streets, Baltimore, Md.
Northern Wisconsin Cooperative Tobacco Pool, Madison, Wis.
Virginia Dark Fired Tobacco Growers Marketing Association, Farmville, Va.
Western Dark Fired Tobacco Growers Association, Murray, Ky.

VEGETABLES AND MELONS DIVISION

Eastern Shore of Virginia Produce Exchange, Onley, Va.
National Fruit and Vegetable Exchange, Hudson Terminal Building, New York, N. Y.:
- Austin Fruit Association, Austin, Colo.
- The Blanca Vegetable Growers, Inc., Blanca, Colo.
- Cassia Potato Growers Association, Burley, Idaho.
- Central Strawberry Cooperative Association, Hammond, La.
- Conejos County Vegetable Growers Cooperative Association, La Jara, Colo.
- Currituck Mutual Exchange, Inc., Currituck, N. C.
- Fruitland Fruit Association, Fruitland, Idaho.
- Gem Fruit Union, Inc., Emmett, Idaho.
- Growers Trading & Supply Co., Hotchkiss, Colo.
- Idaho Agricultural Industries, Caldwell, Idaho.
- Illinois Fruit Growers Exchange, Centralia, Ill.
- Kaw Valley Potato Growers Association, Topeka, Kans.
- Lafourche Truck Growers Cooperative Association, Lockport, La.
- Maine Potato Growers, Inc., Fort Fairfield, Maine.
- Manatee County Growers Association, Bradenton, Fla.
- Michigan Potato Growers Exchange, Cadillac, Mich.
- Minidoka Potato Growers Association, Rupert, Idaho.
- Mississippi Vegetable Exchange, Inc., Crystal Springs, Miss.
- The Mountain Fruit Co., Cedaredge, Colo.
- Mushroom Growers Cooperative Association of Pennsylvania, Kennett Square, Pa.
- The Paonia Fruit & Supply Co., Paonia, Colo.
- Rio Grande Valley Citrus Exchange, Inc., Weslaco, Tex.
- St. James Truck Growers Cooperative Association, Convent, La.
- South Texas Vegetable Association, Corpus Christi, Tex.
- Standard Growers Exchange, Sanford, Fla.
- Surface Creek Fruit Growers, Inc., Austin, Colo.
- Terrebonne Cooperative Association, Houma, La.
- Union Fruit Co., Paonia, Colo.
- Utah Fruit & Vegetable Growers, Inc., Salt Lake City, Utah.
- Valley Vegetable Cooperative Association, Weslaco, Tex.
- Wenatchee-Okanogan Cooperative Federation, Wenatchee, Wash.
- Wet Mountain Valley Vegetable Growers, Inc., Westcliff, Colo.

WOOL DIVISION

National Wool Marketing Corporation, 281 Summer Street, Boston, Mass.:
- American Mohair Producers Cooperative Marketing Corporation, Uvalde, Tex.
- Arizona Wool Growers' Association, 134 South Central Avenue, Phoenix, Ariz.
- California Wool Marketing Association, 405 Sansome Street, San Francisco, Calif.
- Central Wool Marketing Corporation, 281 Summer Street, Boston, Mass.
- Colorado-New Mexico Cooperative Wool Marketing Association, Durango, Colo.
- Colorado Wool Marketing Association, 236 Continental Oil Building, Denver, Colo.
- Cooperative Wool Growers of South Dakota, Brookings, S. Dak.
- Eastern Idaho Wool Cooperative Marketing Association, Box 550, Pocatello, Idaho.
- Illinois Live Stock Marketing Association, 608 South Dearborn Street, Chicago, Ill.
- Indiana Wool Growers' Association, Lemcke Building, Indianapolis, Ind.
- Iowa Sheep & Wool Growers' Association, 313–17 Southwest Fifth Street, Des Moines, Iowa.
- Kentucky Wool Growers' Cooperative Association, Lexington, Ky.
- Lone Star Wool-Mohair Cooperative Association, 9 East Concho Avenue, San Angelo, Tex.
- Michigan Cooperative Wool Marketing Association, 221 North Cedar Street, Lansing, Mich.

National Wool Marketing Corporation, etc.—Continued.
Midwest Wool Marketing Association, 140 Main Street, Kansas City, Mo.
Mid-Texas Wool & Mohair Marketing Corporation, Menard, Tex.
Minnesota Cooperative Wool Growers' Association, Wabasha, Minn.
Montana Wool Cooperative Marketing Association, Helena, Mont.
Nevada Wool Marketing Association, Elko, Nev.
New Mexico Cooperative Wool Marketing Association, Albuquerque, N. Mex.
New York State Sheep Growers' Cooperative Association, Inc., Penn Yan, N. Y.
North Dakota Cooperative Wool Marketing Association, Fargo, N. Dak.
Oregon-Washington Wool Marketing Association, 509 Miller Building, Yakima, Wash.
Sonora Wool & Mohair Marketing Corporation, Sonora, Tex.
Southwest Texas Wool & Mohair Marketing Association, Del Rio, Tex.
United Wool Growers' Association, 6 East Lee Street, Baltimore, Md.
Utah Wool Marketing Association, 408 Vermont Building, Salt Lake City, Utah.
Western Idaho Wool Marketing Corporation, 209 McCarty Building, Boise, Idaho.
Wisconsin Cooperative Wool Growers' Association, Portage, Wis.
Wyoming Wool Cooperative Marketing Association, McKinley, Wyo.
Pacific Cooperative Wool Growers, 1205 Northwest Davis Street, Portland, Oreg.

ASSOCIATE MEMBERS

Agricultural Council of California, 603 Plaza Building, Sacramento, Calif.
Arkansas Council for Agriculture, 524 Post Office Building, Little Rock, Ark.
Idaho, Cooperative Council, Boise, Idaho.
Mississippi Cooperative Council, care of Mississippi Cooperative Cotton Association, Jackson, Miss.
Missouri Cooperative Council, care of W. W. Fuqua, Rural Route, Columbia, Mo.
Oklahoma Agricultural Cooperative Council, Stillwater, Okla.
Oregon Cooperative Council, Corvallis, Oreg.
Pennsylvania Association of Cooperative Organizations, Shippensburg, Pa.
Texas Cooperative Council, 1100 South Ervay Street, Dallas, Tex.
Washington State Agricultural Council, Wenatchee, Wash.

Mr. SEXAUER. In large part these organizations are nonprofit membership associations. Their interests range from the basic commodities, such as cotton and wheat, to the finished products, such as milk, butter, nuts, citrous fruits, vegetables, and so forth. Just so the interests represented by the National Cooperative Council range from problems of raising commodity prices to problems of increased purchasing power for consumers in order that finished commodities such as milk, nuts, fruits, and vegetables may have a constant and expanding market.

By and large these organizations, insofar as they represent the membership of the associations, have little interest in banking as such or in money as such. They do, however, have a vital interest in the economics of money and the relationship between money and price levels, the relationship between money and employment and the relationship between money and purchasing power.

The interests of the cotton and wheat farmer are largely tied up in the relationship between prices in the United States and prices abroad. The interests of the livestock, fruit, nut, and milk farmer are intimately tied to the standard of living, purchasing power, and total income of the Nation.

In presenting the National Cooperative Council's position on the economics of money to this committee today, we desire to approach that subject from the angles of the various interests within our association. The relationship between money and cotton and money and wheat have been presented more effectively than I could possibly present it, by Mr. O'Neal, of the Farm Bureau Federation, who comes from the cotton South and who represents so much of the grain-growing West.

The relation between money or the value of money and the relation between gold or the value of gold and these latter commodities is such a direct one that it is easy to trace. Over any extended period of time that relationship can be charted with great exactness. The effect of the value of money or the value of gold is not so directly ascertainable when applied to such commodities as milk, nuts, fruits, and so forth. A correct appraisal of the relationship between the value of gold and these commodities leads one through the various steps by which a change in the price of gold affects basic commodity prices, how basic commodity prices in turn affect business, how business in turn affects employment, how employment in turn affects wages, and how wages in turn affect purchasing power and the standard of living. From there the steps involve the relationship between the items of wages, purchasing power, and the standard of living on the one hand and the sale of these finished agricultural products on the other.

Fortunately the record of the past 2 years is sufficiently clear so that a cold analysis can be made of the happenings during that period. On April 19, 1933, this country finally and completely went off the gold basis. The dollar price of gold in the free markets of the world rose rapidly from that date until July 17. During that period basic commodity prices rose even more rapidly, first being pushed upward by the increase in the dollar price of gold and then being accelerated by the confidence that through this gold price movement prices would continue to rise for some time and business continue to improve.

The hope that business would improve was justified by the trend of business and industrial production during that same period. Were one to chart the rise in the price of gold and the rise in basic commodities together with the percentage of increase in business during that same 3-months' period, the three lines would be surprisingly parallel. They could not be exactly parallel for no one can chart the vagaries of human nature.

During this time employment rose rapidly as did also total wages and purchasing power. This was a period when on the part of some there was fear of extreme inflation. For the most part, however, it was a period during which there was a regeneration of confidence and a feeling that we were well on our way out of depression.

During this period from April 19, to July 17, there were many cross currents of opinions, ideas, and conjectures. There was a conflict between those who felt we should return to the old price of gold and those who felt the price of gold should be further increased. Those who looked forward with confidence to the future and felt that gold prices would further increase were optimistic.

May I make it clear at this point that during this period the only prices that were materially increasing were the prices of basic commodities, not the prices of finished products. The prices of finished products had not fallen to any material degree but the prices of basic commodities were only 40 percent of what they were during the period of 1921–29. Inequality of price rise between basic commodities and finished products was very disturbing to some who did not understand that basic commodities had fallen more than finished products. Possibly as a result of this disturbance, there issued from Washington about July 20 an announcement, roughly to the effect that a great social program was to be put into effect. This program was to eliminate the chiseler, the price cutter, and the sweatshop; in addition, the intimation was that the problem would be handled through other means than through increasing and regulating the price of gold. As a result, confidence was shaken. The price of gold declined. Business activity faltered. Executives turned their attention to other matters than their businesses. Commodity prices began to decline. This decline in basic commodity prices continued until October 22. Gold in the meantime recovered some of its price until in October it stood approximately where it had on July 20. Commodities had declined to a point where they were almost exactly in line with the price of gold in the world market.

On October 22 the President announced that control would be taken of gold and that price levels would be reestablished on approximately the 1926 level. Gold again advanced in price in an irregular fashion, continued that advance until February, at which time power was given to the President to establish the price of gold, and on January 31, 1934, he did so establish that price at $35.

During the period of declining commodity prices and declining gold prices, business suffered a severe relapse. Immediately following the announcement of the President on the 22d day of October business again increased at a rate almost parallel to the increase in the price of gold. Commodity prices started an irregular trend upward which trend reached its high point at the time when the President fixed the price of gold at $35 an ounce. With only minor fluctuations in the meantime, the average price of basic commodities remained at the higher price level until the time of the drought of this past year.

From an economic and statistical viewpoint it is evident that basic commodity prices, business activity, employment, and purchasing power are extremely sensitive to changes in the price of gold and receive an upward impetus each time the price of gold is moved upward.

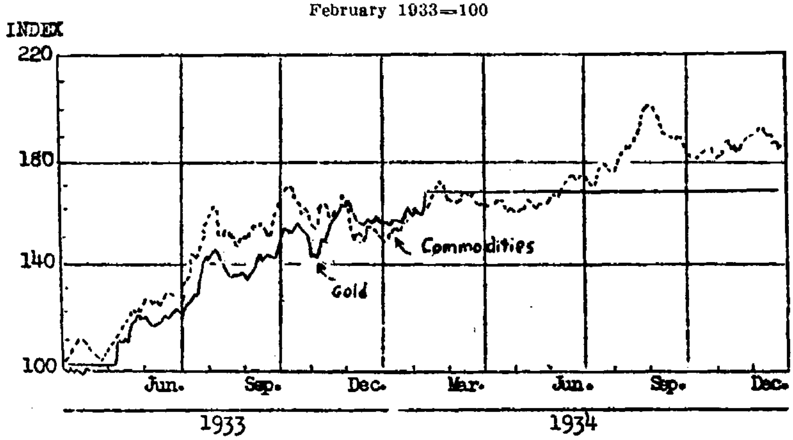
I will be glad to submit charts proving almost any of these statements if you desire to have it done. I have tried not to make any statement here which could not be pretty definitely proven statistically, and attached I have charts based upon statistical data to prove the points made.

The prices of commodities, such as butter—we represent milk—are sensitive to many influences but are particularly sensitive to employment conditions. While a change in the price of feed grains may increase cost of production and through this the price of butter, the long-time effect is for the butter price to follow a course very definitely parallel to total wages and total employment. From the viewpoint of the producer of butter, it is highly desirable that a good wage income be maintained, not on the part of the few but on the part of the many. Any program which tends to raise the wages of the few and dispossesses more and more people of their jobs is in nowise beneficial to the producer of butter. I assume this must also be true of all finished agricultural products, such as nuts, oranges, apricots, vegetables, and so forth.

Here is a chart.

DAILY PRICES OF GOLD AND PRICES OF BASIC COMMODITIES
February 1933 to December 1934

February 1933=100



Basic commodities represent the Journal of Commerce Index of 30 Basic Commodities as drawn from a chart by G. F. Pearson of Cornell University.

The credit for any information which I may have on this problem belongs primarily to Dr. Warren and Dr. Pearson, of Cornell University, whom I have known for a period of 18 years. During that period they have never hesitated to predict continuously and specifically as to price trends. Immediately following the World War they pointed out to me that a price decline was inevitable and pointed out the time at which that price decline would take place. When questioned as to the reason for their prediction they pointed out that after every major war, prices of basic commodities seek a level which can be very closely ascertained by weighing the total volume of world production against the total quantity of world gold.

During the period from 1921 to 1929, when most people were saying we were in a new economic era, when under the leadership of the Federal Reserve, managed by such men as Mr. Strong, control of credit was being used to maintain average prices at a fairly constant level, these two men were continuously saying that prices of basic commodities would decline at least as low as the pre-war level unless there was a repricing of gold in terms of our currency. Dr. Warren was in my office one day in the year 1930 and I asked him how long this so-called "depression" was likely to last. His reply was:

> This in my opinion is the depression which we have discussed for so many years, and insofar as business is concerned it will last from 6 to 10 years and insofar as agriculture is concerned it will last 20 years unless we are able to bring about a repricing of gold to adjust the price of basic commodities back to their previous level.

That was the prevailing state of mind in 1930.

The National Cooperative Council's position is that the prices of commodities which farmers and other basic producers create are so low as to bring about a disequilibrium between the prices of basic commodities and the prices of finished goods, wages, taxes, fixed charges, and costs based on guaranteed profits such as railroad rates, electric-light rates, telephone rates, and so forth. A lack of balance also exists between basic commodities and prices of goods in closely controlled industries such as steel and textiles.

The position of the National Cooperative Council is that the only way in which purchasing power can be reestablished to provide a good market for such finished products of agriculture as nuts, milk, fruits, and vegetables, is through the increased purchasing power brought about by complete employment of labor. This complete employment of labor cannot be brought about unless industry is speeded up. Industry in turn cannot be speeded up unless, by raising the price of gold, there is created among the producers of raw materials, purchasing power sufficient to bring the price of these raw materials to a point where the producers of such are able to buy, first, the services of the Government as evidenced in taxes; second, the services of controlled industries, many of whose rates are established by Government sanction; third, the services of labor maintained by organization; and fourth, the finished products which are the result of all these.

So long as this disequilibrium exists between the price of basic commodities and those items of fixed charges, such as wage rates, taxes, controlled products, and finished goods, the National Cooperative Council feels that there can be no material return to prosperity, business activity, employment, purchasing power or the free movement of finished commodities produced by farmers.

An examination of the record will show that only three times in the last 4 years has there been any trend toward equilibrium among prices. One period was during the last few months of 1932 and most of 1933 when wages and finished product prices were declining rapidly and bankruptcies were taking place in wholesale numbers. Undoubtedly a continuation of this program, if the country could have stood it, would have brought about deflation of capital, reduction of wages, shrinkage of finished product prices and a greater equilibrium between finished products, fixed charges, and raw materials. This would have been equilibrium but equilibrium at its worst. At no time has the National Cooperative Council been in favor of such a program.

The only other times during which the trend was toward equilibrium between prices, wages, and fixed charges, were during those two periods, April 19 to August 1, 1933, and October 22, 1933, to January 31, 1934, when rapidly rising prices for gold were causing rapidly rising prices for basic commodities.

Again I repeat that a complete and cold examination of the record will show that at no other times has there been anything but increasing disequilibrium between the component parts of our economic society. The National Cooperative Council feels that equilibrium between prices of basic commodities, taxes, fixed charges, and wages must be reattained. Furthermore, it can see no way in which this can be accomplished other than through increasing the price of gold. There is nothing in the record of the past year to alter the council's opinion in this respect.

Evidence of the soundness of this program of maintaining the price level through increasing the price of gold in the currency of any country can be found in those countries which have effectively increased the price of gold. Such action stopped the decrease in business activity and started the given country upward with increased business activity, increased employment and in most cases with an increased rate of production in the heavy industries.

I believe you will find this to be true of England, who went off the gold basis 2 years before the United States. From that time her condition steadily improved until today it is better than in 1929. Sweden, who went off the gold basis and has been managing her currency and maintaining prices well above the previous level, has virtually no unemployment. A similar situation will be found to be true of Argentina, Australia, Brazil, New Zealand, Denmark, and Japan, all of whom have a more depreciated currency than we, countries whose price of gold in terms of their currency is higher than ours in terms of our currency.

These countries, many of which produce agricultural commodities for export in competition with the United States have, almost without exception, a higher price of gold in their currency than has this country. New Zealand, Australia, and Denmark, although tied to the British pound, have depreciated their currencies to an extent 25 percent greater than have we.

Argentina has—even the past Saturday—depreciated its currency to an even greater extent, as has also Brazil. To put the United States producers of butter on a competitive basis with New Zealand and Australia, it would be necessary to have the pound at least at a ratio of 6.07.

The net result of this is that in those raw material producing countries their price level is 25 percent nearer to their debt level, to their fixed charges, and to their labor cost than is ours.

Such a situation puts this country and its raw material producers at a tremendous disadvantage in foreign trade. Denmark, New Zealand, and Australia are all competitors with this country for markets for butter. Australia is a competitor with this country for markets for wool. Other English dependencies are competitors with us for markets for cotton.

There are those who maintain that the average price level can be raised and maintained through the use of credit and credit inflation. This may or may not be true, I do not attempt to say. The National Cooperative Council maintains, however, that any rise in the average price of goods brought about through credit inflation will not increase the price of basic commodities in this country, except insofar as it raises world prices in terms of gold. Such a situation leaves farmers in the same disadvantageous position that they were in during the period 1922–29.

Prices of the finished goods which they must buy reflect the full effect of the credit expansion, but the prices of the basic products which they sell are benefited only to the extent of the domestic market. Credit inflation of this type cannot affect the world price of basic commodities and thus cannot aid the exporter of farm products. Accordingly farmers, in their dealers with the rest of industry find themselves approaching the same state of price inequality which in the past forced many of their number to lose their farms and homes. The hundreds of thousands of foreclosed farms, the thousands of closed banks all through the Middle Wect bear testimony to the dangers to such a situation.

It is the opinion of the National Cooperative Council that a return to these unfortunate conditions can best be avoided through raising prices of basic commodities by the method already described, namely, increasing the domestic price of gold.

The council do not attempt to determine what kind of bank bill should be passed for handling money as a commodity. They are primarily interested, as I stated in the beginning, in having a policy established which will so regulate the economy of money that it will maintain a commodity price level that will bring about employment, that will bring about a relationship between basic commodity prices and finished goods and wages such that there can be a proper exchange. When that is done we feel it will not make much difference, some difference but not much difference as to the type of banking structure, that once we have reestablished an equality between basic commodity prices, not only farm products but the basic commodity prices, wages and finished goods, that will bring about a free exchange of these, then you gentlemen will take care of the banking situation.

Mr. FORD. The previous speaker referred to Japan's valuation policy as though it had been a wise policy. Japan apparently adopted the policy on the lines of the greatest production possible within Japan, her purpose being apparently the expanding of her exports, which is very successful, but it seems to me that even a superficial study of the subject of conditions in Japan shows that she has adopted this policy without any concern as to the standard of living of her people, and while she has been able to export a great many commodities at a low price, under the price of the yen, which has resulted in her goods being bought all over the world, she has been successful in that, but if a person takes into consideration what is happening in Japan, I do not believe that anyone, at least in the United States, will have the temerity to say that living conditions in Japan as we know the conditions from reports are anything that any nation ought to seek.

Mr. SEXAUER. I think in the major premises we would agree with you that there should be no desire to talk about living conditions in any country upon the basis of Japan's living conditions. There is this point, however, that is often lost sight of. Japan has only revalued to the point where her prices are back to the average of the 1922–29 level. In other words, Japan has brought back within her country an equilibrium between prices. Her whole industry is on a low basis but she has brought back an equilibrium in her prices and every one is employed—I will admit at low wages, but at no lower wages than previously, nor have living costs gone up in Japan. In other words, she has brought about an equilibrium.

There is a great deal of discussion about warfare and depreciation in currency and the idea that too much depreciation of currency is bad for a nation. I assume that is true, but on the other hand there is a correct point in depreciation of a nation's currency which brings about equilibrium in business conditions. Once that is reached that country is in the best situation. The country that can reach that point and stay there longest can educate all the rest of the countries. But on a cold analysis of the situation you will find that Japan in her currency has gone back to an equilibrium that no other country yet has. That is a question of warfare and depreciation of currency, perhaps, and the sound thing is to get back to a level of values, and Japan is forced out into the open, but up to the present time Japan has depreciated her currency so that the price of gold has been raised 190 percent.

Mr. BROWN of Michigan. What is that in American figures?

Mr. SEXAUER. It would be equivalent to our putting gold on that basis.

Mr. FORD. What is the yen now to the dollar?

Mr. SEXAUER. I can find that for you here. You mean what the depreciation would make it to the dollar?

Mr. BROWN of Michigan. Thirty-five?

Mr. SEXAUER. If you figure our present dollar is 59 cents, previous gold value, that would bring it down to 40 cents. It raises the price of gold to probably $60.

Mr. BROWN of Michigan. Fifty dollars now?

Mr. SEXAUER. I will point out that that program, in the minds of the farm organizations, would be extremely dangerous if there were not tied to it a provision, as a result of our investigation, for increased prices of goods in terms of gold throughout the world, and if that brought about steadily increasing prices and inflation of a different character, I believe the farm organizations, and particularly the council, would be in favor of lowering the price of gold or increasing the gold content to stop inflation, which some might say would threaten. In other words, use that as a method of adjusting rather than a method of raising.

Mr. BROWN of Michigan. Do I understand that Japan is now virtually equalizing the amount of the tariff which we have against their products?

Mr. SEXAUER. In subsidies?

Mr. BROWN of Michigan. Yes.

Mr. SEXAUER. I could not answer that question.

Mr. FORD. She has done it by cutting the yen, which was normally 50 cents, so that now it is 31 or 33; therefore you get more yens for a dollar.

Mr. SEXAUER. Quite often those who discuss the farm organizations' position run off into the development of foreign markets, and while most agriculture wants to develop foreign markets, we are far more interested in the internal price level because the facts are these, that when you develop the internal price level approximately or more nearly to what it ought to be, immediately business starts an improvement, and the moment business starts you have a tremendous increase in imports and exports regardless of what the exchange rate may seem to be at that moment. For instance, between the 19th of April and the 1st of August there was a tremendous increase in the production of automobiles, and consequently a tremendous increase in the importation of rubber, and a tremendous increase in goods made of rubber that people buy and you might have exports to England through that exchange. That immediately stimulates business because that in itself stimulates imports and exports. There are those who say that the minute a country depreciates its currency it puts other countries at a disadvantageous position, but the fact remains that our exports to Japan are greater since they depreciated their currency than before.

Mr. FORD. The reason for that is that they sold us more goods and therefore are able to buy more goods.

Mr. SEXAUER. Partly so. They sold our people more goods and were willing to take more of our raw materials.

Mr. CROSS. There is one thing I want to make clear, and that is this question of purchasing power. The higher the price of gold per ounce in relation to the monetary unit, the less purchasing power of the monetary unit?

Mr. SEXAUER. That is right.

Mr. CROSS. And the lower the price of gold per ounce in relation to the monetary unit the greater the purchasing power of the monetary unit, because we heretofore have been talking about the purchasing power of the dollar being small.

Mr. SEXAUER. That is right. There is this compensating thing, that the higher price of gold, the higher the prices of basic commodities, but fortunately that is not reflected in higher prices in finished commodities to any material degree. When gold was going up 69 percent, basic commodities went up 67 percent—I do not find those figures here right at the moment, but as a result the cost of living went up not over 5 percent until that time came when we boosted things artificially that increased the cost of living. For instance, when leading business men got together and raised the price of lumber it was not contemplated in the monetary program because it was never intended to raise the prices of other than basic commodities.

Mr. CROSS. That was the monopolistic feature.

Mr. SEXAUER. It did some other things. They raised the price of wages. Some people say that is a good thing and I do not disagree, but as an organization employing 3,000 people this is what that did. We have no profits, a cooperative organization with no profits but employing 3,000 people. Wages were increased by the N. R. A. to the extent of $200,000. There was no place to get that, no business, nothing we could do about it except to take it out of the producer or the consumer.

Then it becomes a tax on the producer of milk in our organization and we had to immediately set out to find a way to relieve the milk producer of that and did it by plant consolidation and more efficient operation until we got rid of enough men so that the milk producers got the proportion they formerly did, and that meant total wages of the same amount but it meant many of the men were unemployed. We immediately made some consolidation. Farmers wanted to build and improve houses and other buildings. They are not building and improving houses and farm buildings, since prices of finished products such as lumber and cement have been artificially advanced. This means that a great many men are not employed.

The same thing applies to commodities which we bought in our business. Milk bottles immediately went up $1 a gross. That has to come out of the consumer who gets the milk or the producer insofar as our distribution is concerned because we have no profit. It was on the very day that that happened that business began to go down hill, right after the 1st of August. That was no strange thing. It happens that the statistician in our organization wrote an article on the divergence between two policies, one of raising prices of basic commodities and what that would mean, or raising the finished products and what that would mean, and this happened in August 1933.

I only cite this to point out that the program of the national farm organization on revaluation, increasing the price of gold, reducing the gold content of the dollar, put three million men back to work before any other program got to work and the minute it got working it affected our business, and if you go into it you will find exactly what happened, that there was a tremendous expansion of our business in all our departments, and on the 19th of April, when we went off the gold basis, a complete embargo, I had said get ready to expand business.

But on the 1st of August I called them together and said we cannot expand business unless we have purchasing power.

Mr. CROSS. In other words, N. R. A., as you see it, is a bad thing?

Mr. SEXAUER. I only repeat what our farmers say and they say it is bad.

Mr. WOLCOTT. I wish we might get again that point of the relationship of gold valuation to the price commodity index. We have been told by most of the economists who appeared before us that there is no relationship between devaluation of gold and the commodity price level, the retail commodity price level. But it has a noticeable influence on our foreign trade.

Mr. SEXAUER. I would be very glad to discuss that. I have here a chart which I will pass around.

Mr. WOLCOTT. I think the members of the committee will recall, some time after the devaluation because there was no reaction on the domestic market the question was asked of Mr. Morgenthau, Secretary of the Treasury, as to what the policy of the Department was going to be if prices kept going down in the face of the devaluation policy, and that is when he made that famous remark, that is, the Secretary of the Treasury: "We are on a day-to-day basis." They did not know at that time what they would do from day to day. Since then economists who have been before us, if I understand them correctly, have credited the rise in commodity prices to other influences and have given no credit whatsoever to the devaluation of gold as applied to the domestic prices.

Mr. SEXAUER. I would like to distribute this chart and then I will tell you a personal experience about economists.

Mr. WOLCOTT. We have had some experiences.

Mr. GOLDSBOROUGH. They do not ever agree.

Mr. SEXAUER. I had this experience that is illuminating and might in the course of time mean quite a lot. I might tell you I studied Dr. Warren, who has predicted for years and he was the only economist I ever knew from my early farm days through the war up to this time when I am the head of an organization doing a business of $65,000,000 a year—he was the only economist I knew who could predict accurately, and he alone continued to predict for me what was going to happen. I attribute a large part of our success in our program to his predictions.

This happened to me. One day I sat in the office of Dr. Warren and Dr. Myers stepped into the office at noon and said: "We have a luncheon engagement", and they suggested I go with them. I said, "What is it?" "It is a meeting of the economists of the university." I was very glad to go because I had never met any of the other economists. I spent about an hour at that lunch. This was in September 1932. We had that little rise in prices and business activity, and the discussion drifted to prices and business, and as I sat there man after man said: "This depression has taught us one thing and that is, the things we say will be so today will not be so 2 weeks from today. We cannot predict as to the future; no one knows the course of things." We have to follow a plan to drag in business, every thinking business man and cooperative farm leader must plan and must predict. Going across the campus I said, "I do not understand this." I repeated to them what I said to you.

It was then I got my first insight into economics. Drs. Warren and Myers said economics has been only a philosophy. Men philosophize about this and about that, take facts and put them together and say this is so, and it has only been within the last 50 years that there has been academic research into economics.

Suddenly I saw what it meant. I knew that the College of Agriculture had the largest volume of research material on prices and economics there was in the world. I knew that and I imagined that everyone else knew the same thing.

I knew they maintained a statistical research organization that cost them $50,000 a year. I assumed other economists did the same thing. Suddenly I discovered that 90 percent of the economists of the country are still philosophers and only 10 percent of them are scientists.

Mr. Wolcott. My experience with economists in general is that early in their study they come to a certain conclusion and then in their writings and in their research from then on they endeavor to substantiate those early conclusions that they have come to in the beginning.

Mr. Sexauer. That is right. I do not know whether you have ever read this book I have here, entitled "Gold and Prices." It is valuable. It is Dr. Warren's new book.

Mr. Wolcott. This has a great deal of interest. Professor Pearson was here last year and the monetary authority people told us very definitely that all prices, external and internal, wholesale prices and retail prices, were tied to the price of gold, and I think that Professor Pearson was the only economist who appeared before us who would not at least say that the volume and velocity had some influence on retail and wholesale, gold, and commodity prices. He said that volume or velocity had no relationship whatever, no influence on prices.

Mr. Sexauer. That is probably why they charted in here the relationship between prices and velocity of money and I think probably that statistical research on that item will prove that as prices went up velocity followed, but when we started N. R. A. and business declined velocity went down. Velocity follows business. Business does not follow velocity.

Mr. CROSS. What is the title of that book?

Mr. SEXAUER. Gold and Prices.

Mr. WOLCOTT. That is the second edition of the book?

Mr. SEXAUER. The last edition, in the last few days. I will be very glad to give any man on the committee a copy of this book who will read it. This is an up-to-date issue which brings the thing past where the other stopped up to within 2 or 3 months.

Mr. WOLCOTT. Does this book attempt to explain why that previous philosophy was incorrect?

Mr. SEXAUER. Perhaps I should have gone into that—that previous philosophy was not incorrect. That philosophy was correct. If you will look at this chart here you will find that the increase in the price of gold before the President revalued it, that little increase which came from the middle of December until the first of February—that it was only an increase in the price of gold of maybe 5 or 10 percent. During the period before Congress passed the law determining the policy, from the 19th of April when we went off the gold basis, gold increased in price from $20.67 to approximately $32 or $33, and the increased price the President put on gold was not more than $3. Everybody expected prices to have a 69-percent increase after the President started to reprice gold. It had already had a 60-percent increase and there was only room for an additional 7-percent increase.

If you will look at this chart showing the price of gold and the prices of commodities, you will note every time we started to increase the price of gold there was a direct and definite relationship in your price increases, the price of gold and the increase in the prices of commodities. When the President started to increase the price, the day we went off the gold basis, when we embargoed gold on the 19th of April, the price of gold began to work up and the commodities went up, too. That edict increasing the price of gold only affected it 5 or 10 percent and consequently affected commodities by that much and this will follow every time the price of gold is changed. Between the 19th of April, the gold embargo, and February 1, during that period you will find there was 69-percent increase in the price of gold and approximately 67-percent increase in the price of basic commodities, not all commodities but basic commodities.

Mr. WOLCOTT. If we knew surely that was the controlling influence, I think we would probably solve this problem.

Mr. SEXAUER. That is right.

Mr. WOLCOTT. So, taking that into consideration, after we devalued gold we started to pump credit in, and pumped a billion dollars of credit with the idea that we would increase velocity and give acceleration to currency and credit, and we adopted the policy of the A. A. A. and N. R. A., everything designed to bring the price commodity level up to the 1926 basis. Now, I am not certain, and I have not talked to anyone else that is certain whether devaluation of gold has caused prices to go up or whether this policy of having adopted the economics of scarcity as against the demand has caused the price to go up, but if we could determine once and for all whether it was the economics of scarcity or whether the devaluation of gold has caused the increase in prices of commodities, I think we would have our feet at least upon some ground, but we do not know that. If we throw overboard the A. A. A. and the N. R. A., I think we are all fearful that our judgments of the relationship between the devaluation of gold and the commodity price index may not be well founded, and if we stabilize gold I am not so sure that the other would have that influence because on your chart here after March 1, 1934, gold tapers off and has remained constant ever since at 35.

Mr. SEXAUER. That is the fixed price.

Mr. WOLCOTT. But the prices of commodities have fluctuated so that since 1934 the price is wholly out of proportion to gold. There must be some other influence.

Mr. SEXAUER. There was another influence there. The dust clouds from the West signifying droughts started commodity prices upward along about the middle of June. Those commodities that went upward are the farm products, not copper or zinc, but they are farm products primarily raised in the West and from that point on they went up until the peak. That was the drought. Here is a curious thing. We have finally got to the point where we do not think we will have a shortage of food before the next harvest and we will see a curve of commodity prices that is right back to the gold price—that is the drought effect—down to the gold level.

The CHAIRMAN. I want to ask you particularly about wheat and cotton, the effect of the gold proposition in relation to the other factors.

Mr. SEXAUER. It is almost definitely chartable. Again this is somewhat of a scientific process and I am not familiar with all the details. At a given amount of scarcity and changing prices, there is a certain definite amount of change. This is a relationship between supply and demand. When a certain amount of scarcity affects the crop so much as 20 percent, decreases of that amount in the crop total may affect the price 40 percent, and there is a distinct curve of relationship. If you take that curve of relationship on cotton and wheat, the scarcity and supply and demand, and apply that all together with the effect of revaluation, you will just about get the prices you now have. There is a joint relationship in the price of cotton between the A. A. A. program and repricing of gold. To the 6-cent price of cotton add 69 percent due to rise in price of gold; deduct from this, 7 percent to offset the further rise in the world value of gold, and whatever is the price of cotton above that figure may be attributable to the A. A. A.

The CHAIRMAN. Take the case of cotton. I do not know but what with the curtailment of production we shall still have an enormous quantity of cotton on hand above the amount being consumed.

Mr. SEXAUER. Of course, Mr. O'Neal can discuss the matter of cotton far better than I can. I might go through the realm of cotton and find something to criticize, some farm activity, but my primary purpose here is to define and offer something.

The CHAIRMAN. There is no harm in criticizing anyone.

Mr. SEXAUER. This cotton situation was discussed completely with the agriculture committee of the Chamber of Commerce. It seems to me that when a price of 12 cents was established by the Government and the world price was only 11½ cents, and the world supply of cotton was already high, that there was a supply which we could not export. The Farm Board bought up the wheat. The Farm Board bought wheat and in buying wheat held that wheat above the world market. The result was that Canada shipped wheat to all the other countries of the world while we were piling up our surplus. We got all the wheat on the world's market and could not ship it.

The CHAIRMAN. I do not know that I quite get what you have in mind as to the effect on the price of cotton of the gold policy.

Mr. SEXAUER. The gold policy affected the price of cotton just this way. The price of gold affected the price of cotton. The price of cotton went down 7 percent in terms of gold. Cotton went up 69 percent in terms of our currency due to revaluation. Then we plowed up some cotton and prices were raised some more. There is a definite relationship between the two. Neither one can claim all the credit. Now, a curious thing has happened.

The CHAIRMAN. I am wondering if the scarcity factor would exercise the same influence in the case of cotton, where you still had an enormous stock on hand, that it would have on a commodity like wheat where it would come well within the limit.

Mr. SEXAUER. I think that does not enter into it. There is 6-cent cotton in terms of gold, using the gold basis. Cotton has changed in price in terms of gold less than 2 cents.

The CHAIRMAN. You account for that by a factor other than the gold product?

Mr. SEXAUER. The 2 cents; yes.

The CHAIRMAN. The other 4 cents you account for by the gold policy.

Mr. SEXAUER. Sixty-six percent of 6 is 4, roughly speaking.

Mr. CROSS. As to the gold price, here is what I am thinking of. Suppose it takes 100 bushels of potatoes to do the people in this room, to feed them, and out yonder there are 120 bushels, 20 bushels more. Everybody scrambles to sell his potatoes because he knows he has a surplus and the price will not shoot up until you destroy the surplus, and when there are only 99 bushels we begin to grumble and the price shoots up. But you get a tremendous surplus of cotton, 10,000,000 bales surplus, we will say, and destroy 2,000,000 bales. You still have 8,000,000 bales hanging over. What effect would destroying the 2,000,000 bales have upon the price when you still have 8,000,000 bales?

Mr. SEXAUER. The actual records show that the effect of destroying the 2,000,000 bales on the world's market, the Liverpool market, in terms of gold value, is about 2 cents. This chart shows it, insofar as the price of cotton moves up or down in terms of gold, so many ounces of gold.

Mr. CROSS. I can see the gold effect, but I do not see if you have 8,000,000 bales how that effects the world's price when you have that surplus. Of course, as long as we loan 12 cents on it, they have to go out in Brazil or Egypt or India and buy cotton. But I do not see how that affects the world price until you whip out good competition with the rest of the world on it. I see how gold will affect it, our monetary unit. For instance, the price of cotton is 5 cents, that is, at the old value of the dollar, 23.21, and I think if you put it up 2 cents the price would immediately go to 10 cents.

Mr. Sexauer. In our currency?

Mr. Cross. Sure.

Mr. Sexauer. The 2-cent price would be changed.

Mr. Cross. No.

Mr. Sexauer. That is right. Destroying 2,000,000 bales of cotton changes the price just as much as you think, and what 2,000,000,000 people in the world think it should be changed. If we all think there is a shortage the price will go up, and just as soon as we find there is no shortage then it will come down.

Mr. Cross. Are you familiar with what happened in France when she devalued her franc, in other words, made 5 francs out of 1? Did the price go back where it was before, 19 on what was 10, or did the price multiply itself by 5 at that time?

Mr. Sexauer. France did not do that. France went to the point where her money was less than 20 percent. Then prices went up proportionately. She let her franc drift and the franc drifted to a point where it was worth less than 20 percent and arbitrarily one day she said, it will be 20 percent. You must measure from the time she first went off the gold basis to when she finally fixed her prices. There is definitely a relationship between the prices of the average basic commodities throughout the world in terms of gold. The gold values of commodities in England, France, Sweden, Australia, and the United States are within 4 or 5 percent of being the same. The price in terms of currency in those same countries changes exactly with the change in the price of gold in terms of currency of each country.

Mr. Wolcott. I cannot understand when Belgium had 290 milligrams of gold in their monetary unit, 4½ grains, Belgium devalued her Belga and made 7 out of 1, less than half a grain, and yet she is in distress again and talking about going off the gold standard, whatever gold standard they are on. If you put the price up, I do not see why she is so badly affected again.

Mr. Sexauer. Let us take France. I have that information. I have not the information from Belgium but I have some on France. This is primarily a question of unemployment. The factor that causes social disturbance is unemployment, and unemployment has definite causes. Back in 1932 when we were way down in the depths and had between 11 and 12 million people unemployed, France on the basis of the same population—she has one-third of the population we have, using League of Nations figure—and when we had 12,000,000 unemployed on the basis of the same population, multiplying the number of her unemployed by 3, she had 888,000. But what France was affected with was the increase in value of gold that took place between 1930 and the present time, due to the world-wide depression in all the other countries without revaluation.

Gold should have buying power today about what it had before the war, but we are hoarding it so much that our price level in terms of gold purchasing power is about what it was before the war.

France went through the situation in 1932 comparatively well. The increased buying power of gold since has dragged her down until today I do not know just what her position is in terms of employment, but it is not good.

She is going down because we have dragged her down by our depression. Up to the time when we got so far in the depression, France's situation was relatively good, 1,000,000 unemployed against the comparative figure of 10,000,000. I would expect the same situation in Belgium, that Belgium had been dragged down by the world depression. When we have something like 40 percent of the business of the world in this country generally, and only do half of what we normally do, that means a 20 percent loss of world business which means that there is no normal flow of commerce between other countries. Belgium being primarily dependent on imports and exports obviously is tremendously hit by that and hit by the decline of the price level brought about by excessive appreciation in currency and the excessive increase in the purchasing power of gold.

That is philosophy.

Mr. WOLCOTT. With respect to what we were talking about, the philosophy of credit, I think very possibly the emphasis is that the philosophy means availability of credit, because the effect of the increase in the Federal Reserve bank reserves to $2,400,000,000, is velocity of credit. That is available credit. That does not show velocity as not being used.

Mr. SEXAUER. May I illustrate that in our own business? I have to use some philosophy. Our organization has a line of credit in the banks of New York City and can go to any large bank in New York City and borrow a million dollars on our note. That is available credit. There is no velocity of credit there. That is a desire on their part to loan money. It is lack of a desire on our part to borrow. Why don't we want to borrow? Without any question it is because we do not see how we can expand our business under these conditions. On April 19 I thought we could. From April 19 to August 1 I said, "we will expand business"; we are going to have more employment because of this rise in commodity prices. The minute something was done that squelched that I said, we do not want to borrow money.

The velocity of credit was growing in that period. Our credit remained. Our credit was as good the middle of August as at first, but we did not want to do it.

Mr. WOLCOTT. You had no desire to use it in that situation.

Mr. SEXAUER. Yes. It was not the velocity of credit, but the velocity of money in the business we were in.

Mr. WOLCOTT. There was credit available to whip the depression?

Mr. SEXAUER. It might whip the depression as far as business is concerned, but as long as our currency is tied to a fixed amount of gold, corn, wheat, cotton remain fixed to the world's level of prices. You may by velocity of credit raise the price of finished products, but farm products will stay down, and if you go back to the 1922–29 period you will find that the purchasing power of farmers broke down. The reason for that was the rapid expansion of the credit policy that made business active for a time and kept the average of prices up but the farm prices down and the net result was that by and by most of our people in the West went busted and mortgaged their farms, the banks went busted and some people thought it was the bankers' fault.

Mr. WOLCOTT. I have read that approximately 55 percent of the purchasing power of the Nation is ordinarily in the hands of the farmers.

Mr. SEXAUER. I think that could be substantiated but I think you would have to figure it on the basis of income from the basic commodities; it is not the total income, Mr. Wolcott.

Mr. WOLCOTT. As far as round figures are concerned, that is approximately correct.

Mr. SEXAUER. I would say yes, but it would be subject to a considerable argument and some people would say wages are purchasing power and others would figure on production of basic commodities and purchasing power on that basis. You probably can substantiate it.

Mr. WOLCOTT. That is all.

The CHAIRMAN. The committee will recess until 3 o'clock.

Mr. SEXAUER. Here are some groups of figures and I will just leave these charts for each member.

(Thereupon, at 1 p. m. the committee recessed until 3 p. m.)

AFTER RECESS

Upon the expiration of the recess, the hearing was resumed.

The CHAIRMAN. Before we begin with Mr. Foster, I will ask him to yield to Mr. O'Neal, who desires to read a telegram to the committee.

STATEMENT OF EDWARD A. O'NEAL—Resumed

Mr. O'NEAL. Mr. Chairman, among the farm witnesses that we asked to come today to help us present our case, was a very distinguished man, who could not come, but he sent the following telegram, which I would like to read.

(The telegram is as follows:)

MIAMI BEACH, FLA., *March 25, 1935.*

E. A. O'NEAL,
American Farm Bureau, Washington, D. C.

Greatly regret my inability to reach Washington in time to appear before the committee which will discuss today the monetary problem. It is supremely important that we immediately adopt a managed currency. Recently I returned from Europe where I made a careful investigation of economic conditions. Everyone knows that the gold-bloc countries, those still clinging desperately to a fixed price for gold, are in extreme distress. Deflation in those countries is still going on and the end is not in sight so long as they fail to recognize that gold has tremendously increased in value and that in exchange for gold today one must give much more of any commodity. In other words, the increased value of gold made things cheap, depressed prices. On the other hand, the British Empire which has been wisely managing its pound sterling is enjoying great prosperity and is happy that it has a monetary unit varying from day to day sufficient to stabilize prices. I talked with many British leaders of industry, banking, and finance and found a great unanimity of opinion, that Great Britain would not for a long, long time, if ever, abandon its managed pound and return to a fixed gold standard such as prevailed before many countries of the world abandoned the gold standard. For 100 years we have had a commodity dollar but the base has been a single commodity, gold.

We should have instead a monetary unit based on a large number of commodities. The average value of these commodities would not fluctuate so violently as has the value of the single commodity, gold. A few months ago I was in Argentina and saw the prosperity that country is enjoying because it has recognized the increased value of gold and devalued the peso sufficiently to compensate for the change in the monetary base. The Argentina farmer is getting a high price for his products and in spite of the tariff might sell wheat even in America at a profit in competition with the American farmer. The situation is so plain that it seems strange that we as a Nation have been so slow to adopt the policy which is working so well in other countries. Sweden and Australia present more evidence which we should recognize. The American farmers seem to understand the gold question better than our bankers or our business men. I hope your efforts before the committee on banking will be successful and that you succeed in arousing members of Congress to an appreciation of the vital importance of adopting a managed currency so that we may stabilize prices, prevent great fluctuations and the recurring depressions which have raised havoc with our whole economic situation. Another collapse of prices which might come with the further rise in the value of gold under our present monetary system would bring us a greater disaster than we have yet experienced and might threaten all our institutions and democracy itself. It would be a great tragedy if Congress should fail to enact legislation that will give us relief and protection for the future. We must end the "money illusion" which already has almost destroyed us.

FRANK E. GANNETT,
President the Gannett Newspapers.

That is from Mr. Frank E. Gannett, president of the Gannett newspapers.

Now, Mr. Chairman, there is one other witness that we were to have today, and I am sorry that he could not come; Mr. Louis J. Taber, of the National Grange, and I would like to ask the privilege that he may file his statement later. He regrets his inability to be here.

The CHAIRMAN. All right. Without objection, that will be done. Now, Mr. Foster, you may proceed. Give your initials, and your connections.

STATEMENT OF E. S. FOSTER, OF ITHACA, N. Y., GENERAL SECRETARY NEW YORK STATE FARM BUREAU FEDERATION

Mr. FOSTER. Mr. Chairman——

The CHAIRMAN. We would be glad to have you discuss this bill, Mr. Foster, and you may have such time as you wish without interruption. I suggest that you indicate to the committee when you desire to be interrupted.

Mr. FOSTER. All right.

Mr. Chairman and members of the committee, I have prepared a rather voluminous statement here that runs about 20 or 25 pages, and I hesitate to ask your committee here this afternoon for permission to read that.

The CHAIRMAN. I suggest to you that you read so much of that statement as you desire to read to the committee, and any further part that you wish incorporated in your remarks may appear consecutively, without having to read it in full.

Mr. FOSTER. All right, thanks. I think I choose to file the brief, if possible, and merely extemporize here for a few minutes.

The CHAIRMAN. Without objection, that will be done.

(The brief referred to is as follows:)

HIGHER COMMODITY PRICES AND STABILIZED PURCHASING POWER OF THE DOLLAR ARE THE GREATEST NEEDS OF AGRICULTURE

Most farmers are agreed that steps should be taken by the Federal Government to correct and prevent the hazardous conditions which result from wide fluctuations in the purchasing power of the dollar. Farmers have long experienced rise and fall in commodity prices, and they recognize the absolute necessity of developing a system to correct this condition, to bring about greater stability in our economic life.

In the first place, why are farmers so vitally interested in this problem of stabilizing the dollar? The answer to that question is to be found in all the things that have happened to us and to agricultural countries of the world since 1920. The great wars of modern times have been financed by a resort to inflation. After every one of these wartime inflationary periods we have experienced violent deflation in the final analysis. The general level of commodity prices that is driven away up during the inflation periods goes into an equally violent collapse when the current is reversed and deflation sets in. In the last episode the turn came in 1920, and the wreckage resulting from that headlong plunge of commodity has strewn our land for 15 years.

When prices rise the man to profit first is the producer of raw materials. Likewise, he suffers first and most severely during declining prices. Farm products are basic in nature, and naturally they are extremely sensitive to changes in price levels.

When deflation overtakes a community the bottom drops out of all primary products, raw materials, and especially those having the broadest markets. Those producers whose income depends upon these things see their income wiped out. They are unable to meet even current obligations, let alone paying debts of longer standing—debts contracted back under a higher price level. Thus, one of the unfailing effects of such a deflation period is a great mass of unpayable debts. The whole community is waterlogged by an overwhelming burden of debt. The farm business is sunk; and taxes, as well as private debts, become uncollectible.

It is unnecessary to recite the details of this chapter of history we have just been living through. The story of all the thousands of failures in farming, of foreclosures, of bankruptcy, and of general poverty is familiar to all. Already it has been with us for half a generation and the end is not yet.

In few words, this is why the farmer is interested in the problem of price level and consequently of money. It is because he has always been and will always be one of the keenest sufferers from the ravages of these great deflation periods. The whole community suffers in these times, but it is on the farmer that the blow falls first and most severely.

WHAT CAN BE DONE TO HELP THIS SITUATION?

In attempting to correct the wide fluctuations which take place in commodity prices, it is first of all necessary that we recognize the factors which determine price levels. Great confusion seems to exist among individuals as to just what these factors are. Some claim that changes in the price level just automatically happen. Some say that over and under production is the cause. Some claim that bank credit, with its contraction and expansion, is the major factor. Some say that foreign trade, or the lack of foreign trade, is responsible. Some say that gold is the important factor.

Scientific research shows clearly that gold is the most potent of all factors in governing the rise and fall in commodity prices. The evidence clearly indicates that the violent world-wide ups and downs in commodity prices during the last 20 years have been due primarily to changes in the value of gold.

Gold is a commodity just the same as wheat, or copper, or rubber, or any other commodity. Its value is subject to the same forces of supply and demand as any other commodity. The supply of gold is a relatively stable thing, but the demand for it varies widely. When the western nations abandoned gold during the war and ceased to bid for it, the value of gold went down, and commodity prices rose to an index of 220 in this country.

After the war many of the European countries that had abandoned the gold standard began a mad scramble to place their currencies back on the gold basis. As a result, the value of gold rose abruptly, and commodity prices fell with extreme violence down to an index of about 150. Eventually they went down to 87.

The war-time inflation was a phenomenon of the gold-using countries, and so was the post-war deflation. It was the gold-standard country whose prices marched up the hill and then marched down again. The silver-using countries did not go through this experience. China did not have our war-time inflation nor our post-war deflation. It seems clear that these wide fluctuations in commodity prices have been due to sudden changes in the world's demand for gold.

The value of gold is determined by the world forces, and no one country can control it. Neither we nor any other country can control the purchasing power of an ounce of gold.

The price level of commodities is determined by the relationship which exists between the supply of and demand for commodities and the supply of and demand for gold and the price of gold.

There is a widespread belief that the expansion of bank credit, currency excess reserves, and/or velocity will raise commodity prices and gold is of little or no consequence.

There is a fundamental relationship between corn and hogs, between corn and cotton, and between gold and cotton. When a nation is on the gold standard an exchange of a bank check or paper money for cotton is an exchange of a given weight of gold for a given weight of cotton. With gold at $35 per ounce and cotton at 10 cents, a bale of cotton is worth 1.43 ounces of gold. Expanding bank credit, excess reserves, velocity, and the like cannot materially change this ratio.

When the dollar price of gold is suddenly changed, the amount of gold to buy a bale of cotton does not change, but the price of cotton does change. The advance in the price of gold is equivalent to reducing the gold content of the dollar and, if the ratio of gold to cotton does not change, the ratio of the dollar to the cotton does change, and this is the dollar price of cotton.

The price level of a country is the product of the world level of commodity prices in gold and that country's price of gold.

The world level of basic comodities in gold in six countries fell from 135 to 62 percent of pre-war, and for the past 17 months has been very stable, varying from 62 to 64. In February 1933 basic commodities in the world were 67 percent of pre-war and 30 basic commodities in the United States were 66 percent of pre-war. In January 1935 the basic commodity index was 112 and had advanced about as much as the price of gold would call for. (66×1.69=112)

Our price level is a product of the world level of commodity prices in gold and our price of gold. We cannot control the world price level, but we can control our price of gold and thereby control our price level.

Since the United States is on the gold standard, it follows that the United States cannot keep its price level far out of line with the world level of prices in gold by the discount rate, by velocity, by greenbacks, by silver certificates, by Federal Reserve notes, by unbalanced budgets, by confidence, by public works, by tariffs, by quotas, by crop destruction, or by giving away money. This is regardless of how meritorious or injurious any of these may be from other standpoints. No country can keep its price level far out of line with the world level and no country has been able to strikingly affect the world level of prices.

It is definitely recognized that change in the price of gold in the United States has been a potent factor in raising commodity prices. It is also recognized that further use of the existing power to raise the price of gold can be a material influence for a further upping of commodity prices.

COTTON

Most of the advance in the dollar price of cotton since February 1933 has been due to the rise in the price of gold. From February 1933 to March 18, 1935, prices of cotton at New York were 6.1 and 10.65 cents per pound. The price of cotton has advanced 75 percent, slightly more than the 69 percent advance in the price of gold. In terms of the old gold dollar the price of cotton in the United States has risen 3 percent. In February 1933 the price of cotton at Havre, France, was 209 francs, and on March 18, 1935, cotton was worth 222 francs, or cotton had advanced 6 percent at Havre. France is on the gold standard and there is no question but that cotton in gold has advanced only 6 percent. Therefore, the 75 percent advance in the price of cotton is largely attributable to the depreciation of the dollar—the 69 percent advance in the price of gold.

The price of cotton in the United States is a product of the world price of cotton in gold and the dollar price of gold in the United States. If the world gold price of cotton did not change and we raised the price of gold from $35 to $45 an ounce, the price of cotton at New York would be about as follows:

Price of gold	Price of cotton	Price of gold	Price of cotton
$35	$10.3	$40	$11.8
36	10.6	41	12.1
37	10.9	42	12.4
38	11.2	43	12.7
39	11.5	44	13.0

The advantage in the price of gold from \$20.67 to \$35 is a 69 percent change. All commodities rose from 87 to 115, or a 32 percent increase. All commoditites did not rise by the full amount of the 69-percent advance in the dollar price of gold because of the Bureau of Labor index of all commodities was not completely deflated in February 1933. Therefore, the answer to the latter part of the question, "How much would it be necessary to raise the price of gold to bring the general prive level to that of 1926", involves an analysis of prices, basic commodities which were completely deflated.

In February 1933 our index of 30 basic commodities was 66 percent of prewar and at present is 112, and is in adjustment with the depreciation of the dollar (66×1.69=112). If our basic price level was in adjustment with the world level of basic commodities in February 1933 and if the world value of gold does not change, a price of gold of \$45.68 would be required to bring basic commodities into line with the 1926 level. (146+66=2.21×\$20.67=\$45.68)

If basic commodities were brought to the 1926 level they would have to rise 121 percent from the low of February 1933. All commodities would rise by a smaller percent, 68, because they were in a state of incomplete deflation in February 1933.

If commodity prices in gold throughout the world should rise 10 percent and this was reflected in our basic price level, a \$41.34 price of gold would bring basic commodities and all commodities to about the 1926 level (146÷73=2.0×\$20.67=\$41.34).

If commodity prices in terms of gold throughout the world should rise 15 percent, about a \$39.69 price of gold would bring basic and all commodities to the 1926 level (146÷76=1.92×\$20.67=\$39.69).

If commodity prices in terms of gold throughout the world should rise 20 percent, a price of about \$38.24 would be required to bring basic and all commodity prices to the 1926 level (146÷79=1.85×\$20.67=\$38.24).

If commodity prices in terms of gold throughout the world should rise 25 percent, a \$36.38 price of gold would bring basic and all commodities to the 1926 level (146÷83=1.76×\$20.67=\$36.38).

If commodity prices in terms of gold throughout the world should rise 30 percent, a \$35.14 price of gold would bring basic and all commodities to the 1926 level (146÷86=1.70×\$20.67=\$35.14).

But while we cannot control the world value of an ounce of gold, we can measurably control the internal value of the dollar by either changing the price of gold or flexing the number of grains of gold in the dollar, thereby controlling our domestic price level of commodities. This has been demonstrated conclusively since the spring of 1933. While the dollar was tied to gold in the fixed quantity of 23.22 grains, our commodity prices were firmly lashed to these tremendous swings in the world's value of gold. Following 1929, when that world value of gold finally soared to the highest level of modern times, we saw our commodity prices conversely go down to depths at which equities were wiped out, our farms and industrial business were paralyzed, our banks ruined by the thousands, and our whle economic life reduced to the verge of chaos. But once our dollar was cut loose from that fixed quantity of gold, prices of our basic commodities instantly moved upward and our farmers and producers generally were once more given a fresh breath of life.

The farmers of this country are convinced that a basic remedy for this whole trouble is to free the American dollar from these disastrous swings in the world value of gold. They are convinced that the chains by which the dollar is linked to gold must be flexible enough so that they will not periodically throttle the internal prices of the products of our farms and factories.

Mr. Frank A. Vanderlip said the other day before the Senate Agricultural Committee that our gold dollar of a fixed number of grains is not a measure of value at all, it is merely a measure of weight. He is right. We are convinced that what is needed above all else is to establish a domestic measure of value, one that will have a fairly constant purchasing power one month with another and one year with another. We are convinced that President Roosevelt was taking the soundest and most forward-looking position possible when he said in his message of July 3, 1933, to the London Economic Conference, "Let me be frank in saying that the U. S. A. seeks the kind of dollar which a generation hence will have the same purchasing and debt-paying power as the dollar value we hope to attain in the near future."

The farmers certainly have as great a stake in this proposition as any group. We have been among the worst sufferers from the old monetary system whereunder our internal prices have been wide open to the wild swings in world value of gold. If the American farmer and the American manufacturer and worker could be assured that the general level of commodity prices would be relatively stable over long years in the future, the greatest single hazard in our productive life would have been removed.

VARIOUS GROUPS MUST BE IN BALANCE

It is impossible for business to progress unless all groups are in reasonable balance. The so-called "delicate economic balance" existed during the period 1910–14. At that time little was heard about the need for farm relief and little was heard about the high cost of living. Farm taxes and farm wages were in proper adjustment with commodity prices and earnings of factory workers were also in proper adjustment.

Because of the declining value of gold which followed 1914, commodity prices increased rapidly. By June 1917 the price level of 30 basic commodities had reached an index of about 225 compared with an index of 100 during the 1910–14 period. Taxes, interest, farm wages, cost of living, the articles farmers buy, and the hourly earnings of factory workers lagged far behind the commodity price levels. It was then that we heard much about the high cost of living for city workers found their income far out of balance.

By 1920 things were getting back in a fair state of adjustment and our delicate economic balance was being restored. Then came an increase in the demand for gold, with a tremendous increase in its value. This resulted in a drastic lowering of commodity prices and by February 1933 we found that our economic balance was in the worst possible condition of maladjustment. The price level of 30 basic commodities sank to little more than one-half the 1910–14 level. The price of all commodities fell far below the 1910–14 level, while the prices received by farmers for food products fell to one-half the 1910–14 level. In February 1933 the index number of the articles farmers buy stood exactly at the 1910–14 level, while farm taxes and interest payments dropped but little below the high of 1920. While hourly earnings of factory workers had dropped considerably in 1933, still these wage rates were almost double that which prevailed in 1910–14.

In September 1934 we find that the prices of 30 basic commodities and all commodities were slightly above the pre-war level, while the prices received for food products were closely approaching an index of 100. In September 1934 hourly earnings of factory workers reached a new high, with an index of about 240.

It makes little difference over a long period of time to what level we stabilize prices, provided of course that all groups are in proper adjustment. It is impossible to bring down the level of fixed costs, including debts, freight rates, and the like, to the level of commodity prices, therefore the only sensible and logical thing to do is to raise commodity prices in line with fixed costs and debts.

Much progress has been made since March 1933 in raising commodity prices by adjusting the purchasing power of the dollar. We still have considerable distance to travel in bringing commodity prices in line with the level of fixed costs and debts. Unless this is accomplished there is little hope for farmers, regardless of all the many programs that might be undertaken in his behalf.

When prices are in proper adjustment, with fixed costs and debts, they should then be held at that point through stabilization of the purchasing power of the dollar.

A STABILIZED DOLLAR THE REMEDY OF THE GREAT EVIL

What is the so-called "commodity dollar"? In few words, it is a dollar that contains an amount of gold that will buy a given quantity of commodities at all times. It is a dollar that will vary slightly from time to time in the number of grains of gold that it contains, but will be stable in the actual quantity of things that it will buy.

It is not the intention here to discuss the technical details by which such a currency system would be set up, but it may be noted that the adjustment of such a dollar should not be left to political influence, nor even to fallible human judgment. Its adjustment should be made virtually automatic to changes in the commodity price level. An accurate and comprehensive index of commodity prices would be set up by the Government. Then a governmental monetary authority or similar body would be charged with the duty of keeping the gold content of the dollar adjusted to counterbalance exactly any wide fluctuations in the price level.

To the farmer, to the worker, to the man on the street, these automatic changes of a few grains in the gold content of the dollar would mean practically nothing; he would pay no attention to them. The thing that he would know and that would be all-important to him is that his money would be dependable. His dollar would buy substantially the same amount of things in general next month, next year, and 10 years hence as it will buy now.

That kind of a dollar would allow us to enter into long-time contracts with complete assurance. It would absolutely prevent the situation where, because of rising prices as in 1915 to 1920, the creditor gets back actually only part of his loan; or, because of falling prices, as after 1920 or 1929, where the debtor is pressed beyond endurance and becomes wholly unable to pay. It would free us from these terrible deflation experiences which have overtaken us five times in the history of this country and each time have wrecked the fortunes and lives of a whole generation of hard-working people.

Attention should be called to the fact that a commodity dollar in the United States is no new thing, for today we actually have a commodity dollar; but unfortunately our dollar is based on just one commodity, namely, gold. To emphasize the fallacy of basing the dollar on just one commodity, it is only necessary to review what has happened over a long period of time in connection with the changing value of this commodity.

From 1814 to 1843 the value of gold rose 170 percent. From 1843 to 1872 it fell 39 percent. From 1872 to 1896 it rose 97 percent. From 1896 to 1914 it fell 34 percent. From 1914 to 1920 it fell 58 percent. From 1920 to 1934 it rose 281 percent.

If we ask any group of men to name the period when we had the greatest inflation in this country, about 9 out of 10 would answer by stating that we had our greatest inflation when greenbacks were issued. That answer would be wholly wrong, for our greatest period of inflation took place in 1896 to 1920 as a result of the extreme decline in the value of gold.

To base our dollar on a single commodity, which fluctuates so violently in value over a period of years, is extremely hazardous to the producers of commodities and therefore hazardous to our whole economic well-being.

It is interesting to compare the fluctuation in value of numerous commodities which took place from 1873 to date. In spite of the fact that the value of corn has been rising, it has been more stable over this long period than has the value of gold. The value of hides has been about as variable as the value of gold. The value of lard has been much more stable than gold. Although the value of pig iron has declined about 0.4 of a cent per year, it has been more stable than the value of gold. The value of copper is about as variable as the value of gold, while cotton has been more stable. Over this long period of time the value of wheat has been considerably more stable than the value of gold. Therefore, it is evident that as far as stability of purchasing power of the dollar is concerned, it would be better to have it hooked to wheat instead of gold in case we adhere to a one-commodity balance.

When we combine the values from 1873 to date of eight commodities—namely, corn, wheat, cotton, pig iron, copper lard, hides, and gold—we find that the combined value of these eight commodities has fluctuated but relatively little. What we need is a multiple commodity dollar in order that we may avoid the wide ranges in value which are bound to result in a single commodity.

Farmers have long recognized the wisdom of diversity in farming as a means of avoiding the hazards which frequently result in single-crop farming, just as in investments have long recognized the soundness of multiple investments. Exactly the same principle applies to the dollar.

It is sometimes charged that the proposal to reflate commodity prices in line with the level of debts and fixed costs, and then to stabilize the purchasing power of the dollar by means of a commodity dollar which would be controlled by the price level of numerous basic commodities, is wild, radical, and an untried scheme.

It is sometimes argued that it would keep the foreign exchanges in confusion, etc., etc. But such contentions lose their force in the light of the experience of other countries as well as our own in the last few years. England's experience alone supplies the answer to all that sort of talk.

England found in 1931 that she could not continue the process of deflation. She did follow it, in fact, until her industries and agriculture were paralyzed and her gold reserves exhausted. Then, in September 1931, England cut the pound loose from gold. The simple legislative act under which this was accomplished went through both Houses of Parliament on September 21, 1931. It repealed "Subsection 2 of section 1 of the Gold Standard Act of 1925", which was the subsection making British currency redeemable in gold. This law and the subsequent Finance Act of 1932 thus suspended redemption in gold and established a so-called "Exchange Equalization Fund" (of ultimately some 350 million pounds) which was to be used in the stabilization of the foreign exchanges. The legal sanction was very simple indeed.

Great Britain cut her pound loose from gold 3½ years ago. She has never since that time tied it up to gold. She maintains her free gold market in London where gold is bought and sold subject to all the free play of world influences. The English fiscal authorities have proved themselves thoroughly able to manage the pound, obviously with the fixed objective of keeping their commodity price level stable. They have not worried as to whether the theoretical content of the pound was 100 grains or 90 grains from day to day or from week to week. As a matter of fact, what they actually did over the long period was to raise the price of gold from 85 shillings an ounce to 143 shillings, which is simply another way of saying that they devalued the pound by about 40 percent.

England has demonstrated conclusively that a currency can be managed, that the theoretical gold content of the monetary unit can be changed frequently and that the commodity price level can thereby be fairly well stabilized. There are still persons in England who call this radical and who decry it as an experiment, but the weight of British opinion apparently is now firmly against going back to a pound of fixed gold content, and certainly it is dead against going back to a pound of the old gold parity.

What England has done with the pound has not been confined in its effects to that small island. A substantial part of the modern world is linked in its commercial and financial affairs to the sterling mechanism and has followed closely the lead of sterling. That includes Finland, Norway, Sweden, Denmark, Ireland, Canada, India, Australia, New Zealand, Bolivia, Argentina, and Brazil. In those so-called "sterling countries" which are predominantly agricultural, such as Argentina, Australia, and New Zealand, the effects of this monetary policy have been strikingly helpful. They have raised and stabilized their internal commodity prices. They have started agricultural production and incomes back upon the road toward recovery once more, and likewise general business activity.

OUR PROGRESS UNDER THE THOMAS AMENDMENT

Little time need be spent in pointing out the progress that has been made in restoring economic balance as a result of the Thomas amendment. When the gold standard was suspended internally and externally by unpegging the dollar in terms of foreign exchange, commodity prices advanced immediately and substantially in the United States.

That cutting of the dollar loose from a definite amount of gold in March and April of 1933 was like cutting the noose from a strangling man. Within a year after February 1933 the depreciation in the value of the dollar had been equivalent to a 69-percent advance in the price of gold. Within that same period the New York Journal of Commerce price index of 30 basic commodities had advanced 63 percent. Most of the rise in prices actually came in the first 7 months.

The Federal Reserve Bulletin of June 1933 carried an interesting study of the price of cotton, lard, silver, copper, tin, and rubber. There you have six basic commodities which include representative leaders among our domestic export and import items. The study showed that these commodities advanced 60 percent from March 1 to June 1, 1933. American prices responded at once when the dollar was freed from the pressure of the high world value of gold.

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The previous speaker has outlined at length the economic improvement which has resulted in many lines of business since we left the old gold standard early in 1933. He has pointed out that industrial employment has improved, that pay rolls have increased, that bankruptcies have declined, that foreclosures have diminished, that tax payments have improved. The whole economic picture changed for the better beginning almost identically with the abandonment of that old dollar of the fixed weight of 23.22 grains of gold.

Farm people feel that some of the other steps taken later on in the recovery program, well intentioned though they were, were unfortunate and tended to nullify some of the good effects of the new gold policy.

The dollar has again been rigidly tied up to gold at $35 an ounce since February 1, 1934. This means that our internal commodity prices are again linked up directly to whatever deflationary forces still exist in the high world value of gold. We feel that it is a mistake to tie the dollar to gold in a fixed ratio at $35 an ounce upon the same principle that it was a mistake and became a calamity at $20 an ounce.

In conclusion we would do well to recall that America's experiences with these great deflationary episodes resulting from a rise in the value of gold have been progressively worse. The deflation following the Civil War was worse than that which took place after the War of 1812. This latest one, since the World War, has been worse than any of its predecessors.

Our farm people are convinced that the one thing which did most to improve our economic condition has been a revaluation of the dollar. What has been done along this line constitutes the longest single step made since the founding of this country toward the establishment of something like a scientific currency mechanism. We are convinced that Congress should take the remaining step necessary to establish economic balance by raising commodity prices in line with debts and fixed costs through adjustment in the purchasing power of the dollar, and that economic balance be maintained through a commodity-dollar mechanism.

I pointed out that I am secretary of the New York State Farm Bureau Federation, and operate a potato farm in Washington County, N. Y. Unlike Mr. O'Neal I am a small farmer, while he is a large one. I have been working very intimately and closely with farmers during the past 10 years, and am in contact with them nearly every day, and my contacts lead me to conclude that the greatest need of the farmers at the present time is a raising of commodity prices to bring about balance between various groups, and then a stabilization of the purchasing power of the dollar to ward off the disastrous ups and downs in commodity prices that get us into so much trouble.

I think that at the outset it is necessary for us to recognize what makes price levels. There has been a great deal of research in connection with this subject, and this research leads to the fact that commodity prices are determined by a formula which is the supply of commodities and the demand for commodities in relation to the supply of and the demand for gold and the price of gold.

We hear a great many different theories as to what makes price. Most of them are based on theory, and there is little research to substantiate other than the theory that price is a result of the relative values existing between gold and commodities.

There have been some charts placed on your desk during the noon hour, and I would like to refer to a few of these charts, and if you will turn for the moment to the one numbered 17, which is on the back of the pack, I think that we can see some interesting relationship between gold and commodity prices since March 1933.

Now, perhaps there are a few of those sets of charts that fail to have this little chart attached to the back, no. 17.

I wish that we had the charts which precede this, dating back in economic history for about 156 years, showing that during that entire time there has been an extremely close relationship of the value of gold to the prices of commodities. However, we have it only from March 1933.

You will note that as the administration changed in March 1933, there was practically no change in the price level of basic commodities. Following the bank holiday, and the time when we suspended gold payments, we began to get a rapid rise in the price of gold, and by July 1, 1933, we had made remarkable progress, and you will note that the increase in the price of gold practically parallels the increase in the price level of 30 basic commodities.

We travel on through the summer of 1933 with ups and downs, both in the price of gold and in the price of commodities, and then we arrive at the point where, as was pointed out this morning, a few retarding things came into the field. However, our price of gold and the price of the 30 basic commodities have held a very, very close relationship. We got over in February 1934, and the price of gold flattened out at $35 an ounce, and it has held that ever since.

Now, about June and July 1934, we began to read much in the newspapers about the drought in the West and the shortage of certain basic crops as the result of the drought, and we saw prices on the Chicago exchange jump rapidly, due to the fact that a number of those farm commodities are figured in this group of basic commodities, and we got a substantial rise in the basic commodity price level during July and August 1934.

However, the shortage from the drought was not quite as severe as the public was led to believe, and the scare got over somewhat and prices started back down.

I wish that we had this chart brought up to date. We have it in our office at Ithaca brought up to date, and today the lines are practically coinciding again.

Mr. CROSS. Have you a list of those commodities that you used?

Mr. FOSTER. I have not them here. I can furnish you with them. There are iron, tin, copper, wool, cotton, corn, and a whole group of those basic products. I would be very glad to furnish that list to the committee.

So, we have lots of evidence that the two things run together, the price of gold and the price of basic commodities.

Now, if you will turn to chart 1 in the same group of charts, we have the price of raw materials in six countries expressed in pre-war gold currencies. You will note the tremendous fall from 1929 down to date. If we were to plot the increase in the value of gold, we would have just exactly the reverse of that. So, if we will take our pencils and start in the lower left-hand corner and go up toward the upper right-hand corner, we would have what has happened to the value of gold.

Leaving the chart for just a moment, the commodities listed in that group of 30 basics include the following: Wheat, corn, oats, rye, barley, flour, beets, pork, lard, eggs, butter, cheese, sugar, coffee, cocoa, cotton, print cloth, wool, silk, burlap, copper, tin, zinc, lead, silver, hides, rubber, linseed oil, turpentine, and petroleum. That is the group of the 30 basics.

Turning back again to the charts, and to page 1, we find what has happened to commodity prices in six countries, expressed in gold. The value in gold is just the reverse of that other chart.

Now, it seems to me that that is very distinct evidence that the gold program has worked. I cannot point to any more telling evidence than the relationship which the chart on page 17 here shows:

Mr. GOLDSBOROUGH. I wonder if I might interrupt.

Mr. FOSTER. Certainly.

Mr. GOLDSBOROUGH. I have something on my mind that I intended to ask the other two witnesses after they had finished, and then I forgot it.

I notice that your chart goes way up to 138 in 1929, for raw materials. Now, I do not remember that after 1920 the prices on basic commodities, so far as the farmer was concerned, were ever particularly satisfactory. So far as wheat, corn, and cotton are concerned, I do not remember that they were anything like 138 in 1929, from what I knew about it.

Mr. FOSTER. Those particular commodities that you just mentioned now, I think, were not. The general trend of basic commodities has been pretty much down ever since 1920. They have had their ups and downs, but the trend has been down, with a very severe fall following 1929.

Does that clear up that point, Congressman?

Mr. GOLDSBOROUGH. You see, you have a line there that indicates that the prices were satisfactory. It is my recollection that they were not satisfactory insofar as basic farm products were concerned at any time after 1920 and up to the present time. That is my recollection, and it is rather distinct.

Mr. FOSTER. I think that you are quite right. There has been a lot of farm commodities in there that were classed as raw materials, that were too low in price compared to the fixed costs of the farmers in that period.

The CHAIRMAN. And our tariff comes into that calculation, because some of our farm products are protected by tariffs, where some others are not.

Mr. FOSTER. Correct. There is a number of raw products in here, however, that enjoyed pretty good prices during those good industrial days up to 1929. In other words, some of the raw materials that went into industrial products were in quite big demand at that time.

If you will just turn to page 2 in that group of charts, there is some more evidence there of what happens in connection with the gold program. England got a jump on us by quite some extent in revaluing her currency. You will note that in 1931, when England revalued, it practically stopped the downward line in the commodity price level. They flattened it out very much, while the United States, clinging to the gold at $20.67, had a constant fall in commodity prices way down to March 1933 and when we revalued we immediately shot back in line with prices in England.

Mr. GOLDSBOROUGH. I approve of devaluation very fully and heartily, but some of the arguments are not entirely clear to me. It seems to me that when you reach the point of devaluation where you have a satisfactory supply of money, this race for devaluation between the exporting countries is more or less of a trading proposition and it becomes a matter of who can set the pace from day to day. Naturally that has to be limited, for if we deflate more than England, and then England should deflate more than we do, and then France should come along and deflate still more, that sort of a thing has to come to an end some time.

I am wondering if you could go into that and explain on what theory this devaluation is proceeding. Of course, we cannot, as a matter of propriety, base valuation on a mere matter of horse trading, don't you know, from day to day. We have to have a basic principle to guide us, and the only basic principle that I know anything about is putting more money in circulation.

Mr. FOSTER. I will try to answer your question, Congressman. I am not an economist, but I will answer it from a layman's point of view.

I think that devaluation purely from the point of view of attempting to build a world trade is futile, because there is no end to it. If you carry it on far enough, you have what we might term zero with the rim knocked off. It gets to be absolutely zero.

It seems to me that the sound point in the thing is that we have to revalue far enough to raise prices sufficiently where the producers of basic commodities in this country can cover their debt and fixed cost levels, and have some money to spend on top of that for the industrial products that they need, and, with the stepping up of general business, it puts us in a position to import the things that we need. We need a tremendous lot of rubber and that type of thing in this country, and as we step up our business internally and raise our internal prices, it puts us in position to deal with other countries.

Mr. GOLDSBOROUGH. Let us assume that we had reached the point where further devaluation internationally is economically unsound and impossible in this country; then, of course, other commodities will gradually be raised in price until your basic commodities, relatively speaking, are no better off than now or have been in the past.

Is that not so?

Mr. FOSTER. Devaluation will help the producers of basic commodities first, and much more rapidly than any other group.

Mr. GOLDSBOROUGH. But devaluation will lose its usefulness, of course, to the farmer when it has acted on other commodities to the full extent, just as it has on the basic commodities. Is not that true?

Mr. FOSTER. Of course, it will not act on other commodities nearly to the extent that it will on basic commodities.

Mr. GOLDSBOROUGH. But ultimately it will.

Mr. FOSTER. I think not.

Mr. GOLDSBOROUGH. I do not see how you can help it.

Mr. FOSTER. There are a lot of commodities that are under more or less monopolistic control, the prices of which are set pretty much by monopolies.

Many people refer to the fact that the price level of all commodities has not kept pace with the 69 percent that gold has been increased in price, and the reason for that is that a lot of the commodities listed in the general commodity group never fell very much. For example, steel rails all during the depression held at their old level. The price was pretty much set by monopoly, and that is true of shoes, very largely, in comparison to leather.

Mr. GOLDSBOROUGH. I can understand the value of revaluation as a trading proposition. I thoroughly understand that England got off the gold standard long before we did, and we here in Congress begged the folks down town to do something about it, to let us do it, but they would not do it, but what I am trying to gather from you right now is whether, in your judgment, the economic value to this country of devaluation is not bound ultimately to cease, because if each exporting country gets into a race as to who can devalue the most, it gets to be a farce after a while.

Mr. FOSTER. I would answer that by saying that if we devalue to the point where we raise basic commodities back in line with fixed costs and debts, and then should we peg our dollar to a definite amount of gold, which in the future would make it subject to the world changes in the value of gold, over a long period of time that would not gain too much, but we will gain if we can adjust our revaluation so that basic commodities are in line with debts and fixed costs, and then set up a mechanism to maintain equilibrium in there, and stability in prices. Then we can win.

Mr. GOLDSBOROUGH. That had not been mentioned before by any of the witnesses, don't you know, and it should have been, because a great many members of this committee feel that this horse race of devaluation seems in the end to be a futile proposition.

Mr. FOSTER. Let us turn to page 2 of the group of charts now, showing the relationship of commodity prices between England and the United States following 1931, when England devalued and prevented further deflation, and when we continued as we were, and then our coming back in line with the Englishmen when we did our revaluing.

There is one thing that is pretty certain, and that is that we cannot get our prices expressed in terms of gold out of line with world prices in gold. In England, back in March 1933, it required 1.794 ounces of gold to buy a bale of cotton. Now, today it requires, in England, 1.792 ounces of gold to buy a bale of cotton. So, in England today, cotton is selling just about the same as it was in March 1933, in terms of ounces of gold.

In the United States, in March 1933, it required 1.693 ounces of gold to buy a bale of cotton. Today in the United States it requires 1.614 ounces of gold, so that cotton today in the United States, expressed in terms of gold, is almost identical in price with that of March 1933.

The CHAIRMAN. That would seem to indicate that the drift in cotton prices has been the result of our gold policy.

Mr. FOSTER. In the United States?

The CHAIRMAN. Yes.

Mr. FOSTER. That is the way I would interpret it.

Mr. CROSS. The trouble with it has been that we have taken one commodity, gold, and attempted to put everything at the mercy of that one commodity; that is, all of the other commodities at the mercy of gold.

Of course, gold costs a dentist just as much uncoined as it would if it were coined.

You referred to the price of cotton in England. The price of cotton in England, in so many ounces of gold, is the same as it is here, but, as to your monetary unit, it depends on how many grains of gold you have in it.

Mr. FOSTER. Expressed in terms of dollars, we made a nice gain in the United States, but, expressed in terms of ounces of gold, our price today is practically the same as it was in March 1933.

Mr. FORD. A bale of cotton will not buy more gold abroad today than it would then.

Mr. FOSTER. That is right, but you can exchange it for more dollars in this country.

Let us turn to page 3 of that chart for just a moment, on which there are two charts, the upper right-hand chart showing the practice in six gold-bloc countries, and then comparing France with that, showing that prices expressed in gold in one country keep in line with prices expressed in gold in other gold-bloc countries.

Down in the left-hand corner we have an example of what happened in Denmark. Up until 1931, Denmark's prices were following those in the six countries. Then they turned upward.

Mr. WOLCOTT. Do you not think that market operations might have had the same effect as increasing the price of gold? Do you contend that this whole price structure is tied up with the price of gold?

Mr. FOSTER. Yes.

Mr. WOLCOTT. Do you not think that the open market operations of the Federal Reserve Board have some relationship there?

Mr. FOSTER. I think maybe a little bit, temporarily, but I think that they are only temporary.

Mr. WOLCOTT. These charts look familiar to me. I think that they are about the same charts as Professor Pearson had before the committee last year.

Mr. FOSTER. Yes.

Mr. WOLCOTT. I called his attention to the fact that in 1932 there was quite a perceptible rise in the commodity price index, and it seems to me that he replied that it was due to the open market operations of the Hoover administration that the prices started going up.

Mr. FOSTER. I do not know. I cannot answer that.

Mr. WOLCOTT. I can cite his testimony. I asked him this:

> About the middle of 1932, I would say in July—

That should have been August—

> there was quite a perceptible increase in the prices of common stocks of the United States, and then they leveled off and started down again. How do you account for that?

His answer was:

> That was the attempt of the previous administration to raise commodity prices.

Then I asked him if that was as the result of the open-market operations, and he said "yes."

At least the open-market operations are recognized as useful.

Mr. FOSTER. There was some pegging of wheat about that time. It probably brought that up to some extent.

Mr. Wolcott. I thought that that was a remarkable concession on his part, because he had told us very definitely that nothing mattered except the rise and fall in the price of gold.

Mr. Foster. It seems to me that anything that tends toward being monopolistic in nature, such as the steel men have been able to do in holding the price of steel rails up, that where that can be accomplished, it is naturally a factor in holding the price up a little, but the hazardous thing about that is that it reduced volume at a tremendous rate for the particular commodity concerned. It seems to me that equalization of groups is the immediate goal that the farm people at least have been working toward for a long time.

Let us turn to page 10 in the set of charts. The first chart indicates the condition that we were all familiar with from 1910 to 1914.

Mr. Goldsborough. What is the number of that chart?

Mr. Foster. It is on page 10. It is in pencil at the bottom.

From 1910 to 1914 is a period that we are all familiar with, when we were supposed to have the rather delicate economic balance that caused all groups of people to be reasonably happy, finding the various things flattened out at an index of about 100.

By June 1917 we had an entirely different picture, at the bottom of the page, with the 30 basic commodities responding very rapidly to the price raise which followed 1914, the basic commodities going up faster than anything else when prices rose. We found that all commodities made a very substantial increase but not as large as the basic commodities, because they are not as sensitive during periods of price rises as are the 30 basic commodities.

Then we next find the farm food prices going up very rapidly, of course, because food was in much demand during that war-time period, and food prices respond rapidly as prices advance, and that is the time when we heard so much about the high cost of living and when the papers were filled with the "H. C. L."

Farm taxes did not come up very fast; interest payments did not come up very fast; farm wages did not come up very fast; and way over on the right-hand corner you will find the average earnings of factory workers, which came up slowly until 1917. The people working in the factories had a hard job of it to buy at the high prices of commodities.

Now turn to page 12, and there we find the condition that existed in April 1920, with the 30 basic commodities clear up to about 250—all commodities well up to that line—and see what had happened to hourly earnings by that time. Farm taxes came up, interest payments came up, and we were attempting to seek equalization again, or reach equalization, about 1920. We did see various things getting back pretty much in adjustment.

Then, by February 1933, at the bottom of the page, we find an extremely serious condition from the farmers' point of view as well as from the point of view of other groups, with the 30 basic commodities sinking down to little more than one-half of the pre-war level, with farm food prices sinking just about to one-half of pre-war, and with farm taxes remaining at an index of about 160, with interest payments at about 175, and farm wages came down very, very rapidly, because the farmers did not have anything to pay them with, and the hourly earnings came down to quite some extent, however stopping at about an index of 175.

Now, if we turn back to the page marked "11", we find the condition that existed in September 1934, after we had had some revaluation. We find there that the 30 basic commodities had gotten up. The index line of 100 was for all commodities. Farm food very closely approached it, and it is closer today than it was in September. Retail food has not gone up so very much, although we hear quite a good deal about retail food being so high. The articles that the farmers buy have gone up to quite some extent but not nearly as fast as farm food prices.

The interesting thing to note here is that farm taxes are still indexing at about 155, interest payments at about 160, and the hourly earnings of factory workers have gotten clear up to about 240 at the present time. You will notice that that has gone up very, very rapidly since the previous charts that we were looking at here for February 1933. Wage rates have increased materially in some industrial lines and, we claim, have gotten up to a point so that they are higher now than they ever have been.

Now we are getting back toward a much better balance than we had in February 1933, but we have to go some more yet.

Mr. Brown of Michigan. I think that you ought to explain this more fully. The term "hourly earnings" is rather confusing to me. It is hard to say that wages are higher today than they ever were. Do you mean the hourly wage or the flat day's pay?

Mr. Foster. No; I mean the hourly wages of the factory workers.

Mr. Brown of Michigan. Of course, that does not give any indication of the total wages paid.

Mr. Foster. No. If we had a figure on here showing what we might call the "gross wages" of all earners, we would find that they have not come up anything like it is claimed here they have come up.

Mr. Brown of Michigan. Could that be attributed to the National Industrial Recovery Act—that increase in hourly pay?

Mr. Foster. I do not know what that would be attributable to. I would imagine from what contact I have had with quite a number of industrial men that that certainly has been somewhat of a factor in there. There has been a tendency to shove wage rates up and to cut hours.

Mr. Cross. I do not know how far wages have gone up over the country as a whole, but they have not gone up down in Texas. If anything, they are lower today than they ever were.

Mr. Foster. Farm wages have been lagging behind.

On this chart, September 1934, farm wages are just about on the same line as farm food for the United States. Farm wages never got as high in the index as farm food, but they are again about the same level. Farm wages have made quite a little come-back but no such come-back as industrial wages.

The important thing seems to be balance between these various groups for distribution of income, and a good many people think that instead of raising the prices of basic commodities there we ought to tear down these other things. That is just a tremendous job that will probably never get accomplished while many of us are alive, because to do that we first have to get fixed costs way down, which means tremendous cutting of all types of mortgages, all types of debts. It means tremendous cutting of taxes; it means tremendous cutting of wages way down, and that type of thing just cannot be done. If it is attempted, and it is attempted to carry it through to a conclusion, it is bound to result in tremendous disorder if not a good many cracked skulls, and it just is not a practical thing to do.

The only practical thing to do seems to be to raise these other groups up to a reasonable level of balance, and that can be done. There is plenty of evidence that a lot of progress has been made toward that goal, but we can see clearly that there needs to be some more progress made yet. Commodity prices should, by all means, be raised above their present levels. Otherwise the producers of basic commodities, and especially farm commodities, cannot possibly cover their debts and their fixed costs and have anything to spend.

Now, we have talked here about the desirability of equalization in regard to the various groups; and if and when we can get into a stage of higher, desirable, economic balance, we then ought to set up some type of mechanism to keep ourselves as nearly as possible at that level. Certainly history shows that the system that we have followed in the past has led us into long periods of prosperity and long periods of depression, time after time, and that the worst part of it is that each one seems to get a little bit worse than its predecessor.

We should not let that condition run on as we have. There must be some means of controlling it, and steps should be taken just as soon as possible to develop some system of holding ourselves in balance, once we attain that balance.

I have a few more charts here; but, unfortunately, I think that I only have 10 of them; but I would like to have you look at them for just a second.

The CHAIRMAN. Do you think that we are in a situation now where we could satisfactorily set a goal and a definite point at which to arrive?

Mr. FOSTER. That is a hard question to answer. As I said before, I am not an economist, but I think it is awfully difficult to arrive at any place unless we have a goal toward which we are trying to arrive. So I think that we ought to set up our goal; we ought to set it up something on this basis and follow it as a policy that we are going to get commodity prices back in line with the average which existed between 1921 and 1929, and then hold them at that point as nearly as possible.

I think that we ought to have that as a goal. I know that it would put a lot of heart into the farmers.

The CHAIRMAN. You do not mean certain commodities, but you mean the general level?

Mr. FOSTER. That is correct.

The CHAIRMAN. A sort of an equilibrium?

Mr. FOSTER. That is correct.

The CHAIRMAN. And yet you tell us that the gold policy can be so managed as to accomplish a part of that but that it can not be successfully employed to effect the entire situation?

Mr. FOSTER. I do not know that I get your question quite clearly there. What I mean to convey is that as far as commodities as a group are concerned, if we take the average of, say, the 30 basics we can very definitely affect that average, either raising or lowering through the one program.

For any specific one commodity in that group, we may not be able to govern that thing for any one year by gold.

The CHAIRMAN. If I understand the situation, you say that we can, by the regulation of our gold valuation, accomplish the adjustment of the prices we may desire as to basic commodities, but not as to all commodities or finished goods.

Mr. FOSTER. Well, I do not know that I have the question in mind quite straight yet.

One thing I have tried to bring out here is that any raising of the price of gold, or devaluing the dollar, will send the basic commodities up in price much faster than all commodities, because in the entire group of commodities—and we have something over 700 of them—we have a lot that are just like steel rails, the price of which is set by a board of directors. In other words, it is a monopolistic control pretty largely, and not free to play in markets, so that with any raising of the price of gold, the price of things that did not come down certainly should not be raised. There are a lot of those 700 commodities which, during the deflation, came down but relatively little.

The CHAIRMAN. Yes; but if the policy has a general effect, the result would be necessarily to raise the price of all commodities.

Mr. FOSTER. Let us see. For all commodities the increase since March 1933 has been approximately 32 percent, and for the 30 basic commodities the increase has been approximately 67 percent.

The CHAIRMAN. So your theory is that you may continue your operations until you reach a balance between the two?

Mr. FOSTER. Or a reasonable balance; that is right.

Mr. CROSS. In that connection, I might say that some years ago I sold cotton at 42 cents a pound, so that a bale of cotton would buy 11½ ounces of gold. I think that in 1932 I sold cotton for about 5½ cents, so that a bale of cotton would buy about an ounce of gold.

When wheat was down, I sold it for about 20 cents a bushel, which would take 100 bushels of wheat to buy an ounce of gold. When wheat was $3 a bushel, it took about 7 bushels to buy an ounce of gold, and that will run true when it comes to cattle and wool, because I know especially about those two, because I raise and sell wool and cattle.

So I imagine that on most basic commodities, at least agricultural commodities, it turned that kind of a somersault, and it shows you what gold has done; it had increased purchasing power enormously, for we were on the gold standard then.

Mr. GIFFORD. I want to inject a question.

This variable dollar has always interested me very much. I once tried to figure out how much of my income I spent for life insurance, for taxes, for travel, and for other things, and I found that the amount spent for commodities was a very small percentage of the dollar.

Mr. FOSTER. I do not know that I caught what you were saying. Is it your point that the rise in basic commodities does not influence the individual consumer very much? If so, it does influence tremendously the producer of those commodities.

Is that the point you had in mind?

Mr. GIFFORD. The point is that we are willing to pay more for our commodities, but what have you done to real-estate values, and to my insurance and taxes, for instance, and to all of these other things, which do not seem to have been helped by these methods?

Mr. FOSTER. The way they are helped seems to be this; that had we continued the deflation which we were in, and had not attempted revaluation, the life insurance which I hold and you hold, and the property which we hold would probably be worth a whole lot less today than it actually is. In other words, we have retained a lot of the values of the things that practically every man is interested in, such as insurance, land, and that sort of thing.

Mr. GIFFORD. But that is very indirect.

Mr. FOSTER. It may be indirect, but it seems to me that that is so.

Mr. GIFFORD. We are willing to give you a high price for your commodities, but if you are going to manipulate the dollar so that it will hang the rest of us, we are then not so much interested.

Mr. FOSTER. I do not think it would hang anybody, but that it would save a lot of people.

Mr. GIFFORD. As Mr. Goldsborough says, when you get the dollar down to 10 cents, where will you be?

Mr. FOSTER. I think that that would be wholly unwise, and I see no real reason for ever attempting it to the point where it would be destructive. I think that it would cause so much internal difficulty to do that, that it would be impossible to carry on.

Mr. GIFFORD. Are you trying to prove that the overproduction of basic commodities can be overcome by any manipulation of the dollar?

Mr. FOSTER. That brings up the point, first of all, as to whether or not we have excessive overproduction. We certainly know that we have excessive underconsumption in nearly all lines. We certainly have the farms for all industrial products, and we know that in the cities there is a great underconsumption of many farm products, so that it is difficult to say that we are really smothering any surpluses.

Mr. GIFFORD. My sympathy is with you if you want to get your commodities up, but it is not with you where I am made to sacrifice 30 percent of my holdings.

Mr. FOSTER. I do not think that it would be a sacrifice, but a gain.

Mr. CROSS. As I understand it, you want a dollar bill that will do justice to all at the present time. You want a dollar that, regardless of the number of grains of gold in it, whether it is 10 grains or some other figure, is neither feeble nor healthy, but a dollar with 10 grains in it that will buy as much as those dollars bought that had 22 or 23 grains in them at the time I loaned money to you—a dollar that will buy just about all the things that I need to live on, as the dollars that I loaned to you did?

Mr. FOSTER. We want the type of dollar that will buy the same quantity of things 10 years from now that it will buy today, if we do it on the right basis.

Mr. WOLCOTT. That is, a commodity dollar?

Mr. FOSTER. A commodity dollar; and in that connection there is one thing that I think we ought to keep in mind. We talk about a commodity dollar. We already have one today. We have had a commodity dollar for years in this country, but it is a one-commodity dollar. It has been tied up with gold, and based entirely on that.

Mr. WOLCOTT. That is the point that I would like to clear up with respect to this whole situation. The criticism of our present system, or past system, is that we have been tied up with gold, and yet Professor Warren, Professor Pearson, and yourself, and all of the other people that I have heard that advocate gold deflation, still keep that dollar tied to gold. So I cannot appreciate the argument myself, where you denounce the gold standard, and at the same time say that you have to tie to gold, because if the gold dollar was wrong in 1926, as they claim it was, and you want to return to the 1926 standard, what difference does it make whether we devalue to a 59-cent dollar or a 50-cent dollar, as far as those arguments are concerned, so long as they are tied to gold, and we have the same influence in the world market as we would if we had a 100-cent dollar?

Mr. FOSTER. When we are tied to a definite weight of gold, we are subject to the world-wide increase in demand for gold. We increase the value of gold, or the reverse.

Mr. WOLCOTT. But this bill advocates the purchase of silver up to 1,000,000,000 ounces, and, of course, we know that there are not a billion ounces of silver. The most that is available is possibly 200,000,000 ounces.

Mr. CROSS. I think that there is a little more than that, but nobody knows how much there is to be had.

Mr. WOLCOTT. That puts us on sort of a bimetallic base, and if what I have read is correct, no country in the world has been on a bimetallic base for nearly 70 years, and the reason that I bring that up is this: What opportunity is there for this country, if it should be on a bimetallic base, to sit down around the table at The Hague or anywhere else at an economic conference and work out an international exchange on any base unless we first adopt an international base or some base which the major countries have adopted? If we stand as a bimetallic country, in what position would we be with England or Germany, or with France or any of those nations that are on a gold standard?

On the other hand, if we continue our gold-purchase program, and acquire 80 or 90 percent of the world's gold, and, of course, the same thing is true with respect to silver, if we should acquire or have 89 percent of the world's silver, then the other countries will be forced to abandon any sort of an international agreement with us, and all that we will have in our Treasury is a commodity. We might as well have so many bushels of wheat as to have gold, because there will be no market for the gold that we have. They will be off of the gold standard, or off of the silver standard, by reason of the fact that we have acquired all of the gold or all of the silver, and they will say, "We do not care about your gold or silver standard; we are on some other kind of a standard."

So I cannot get the consistency of this program, if you still keep it tied to gold.

Mr. FOSTER. Gold seems to be one commodity that practically all of the world wants, and it is one that is accepted very readily in foreign exchange.

Mr. WOLCOTT. I understand that.

Mr. FOSTER. It seems to be one of the best single commodities from that point of view that has ever been developed.

Mr. WOLCOTT. I understand that that applies to the gold standard, but I cannot subscribe whole-heartedly to the idea that the United States should abandon for all time or for all purposes the gold standard.

Mr. FOSTER. I think that we agree with you perfectly on that. What we want is a dollar based on gold, but with the grains of gold or the price of gold flexible. In other words, what we want is the type of gold dollar——

Mr. WOLCOTT. You want a gold dollar, but you want the standard to be fixed in such a manner that it can fluctuate and keep the price of commodities stable.

Mr. FOSTER. That is what we want.

Mr. CROSS. In other words, you want the number of grains in the dollar to fluctuate in response to the whole commodity price level.

Mr. FOSTER. Correct.

Mr. WOLCOTT. So that a bushel of wheat costing $1 today will cost $1 20 years from now.

Mr. CROSS. No; that means taking the whole 30 basic commodities.

Mr. WOLCOTT. I am taking the one commodity as an example. Let us take a bushel of wheat worth a dollar today. You want to create a situation with reference to the dollar 20 years from now, by fluctuating the value of the gold instead of maintaining the constant value of gold and causing the value of the wheat to fluctuate.

Mr. FOSTER. That is correct.

Mr. WOLCOTT. That is perfectly simple; we are all agreed that that is simple up to the point where the consumption and the production of those commodities are more or less stable, but the condition such as we have had during the last year, and which confronts us this year, with the drought, and so forth, seems to knock that whole theory into a cocked hat.

Mr. FOSTER. It would knock it in this sense, that what we want is a dollar with a purchasing power that is constant over a period of years for a good sized group of basic commodities, but in any one year, the price would be arrived at by a formulai, which is supply of and demand for a specific commodity in its relationship to the supply of and demand for gold, so that in any one year, even under a commodity dollar, we might find wheat way up in price because of a drought or extreme shortage in production.

Mr. WOLCOTT. Wheat is a basic commodity.

Mr. FOSTER. Yes.

Mr. WOLCOTT. What would happen if we adopted this dollar and created a Federal monetary authority which had as its objective the maintenance of a stable commodity price, and then because of some peculiar condition in wheat, due to drought or something of that nature, the price of wheat dropped down to 20 cents? Every wheat farmer would be here on our necks to do something for wheat. If the growers of some other commodity had their price drop way down, they, too, would be on our necks to do something for them, and what could we do? We would just simply tell them that we could not adjust that, excepting as the fall in the price of that commodity affected the index, taking into consideration the average of 784 commodities.

Mr. GOLDSBOROUGH. As I understand it, your proposition is not to interfere in any way with the law of supply and demand.

Mr. FOSTER. That is right.

Mr. GOLDSBOROUGH. Your proposition is to maintain a stable average price for basic commodities, and there is no price fixing in your program whatever?

Mr. FOSTER. Not at all.

The CHAIRMAN. That does not get away from what Mr. Wolcott says.

Mr. CROSS. I can get away from that. When any commodity like cotton goes too low, then I go in and plant oats, or put it in pasture and raise sheep, and I shift things to meet that situation.

Mr. WOLCOTT. You know, in order to meet that situation, the A. A. A. was created to curtail the production of wheat and to curtail the production of cotton and everything, including sugar beets, but the people did not respond as it was expected they would. The wheat farmers insisted upon growing wheat, and the cotton growers insisted upon growing cotton, whether they were justified in that or not, nevertheless they sought relief. If what Mr. CROSS says is true, all that they needed to do in the cotton belt was to start growing carrots, but when the production of wheat reached, as it did in 1921, if I remember the figures correctly, when we consumed 20 percent per capita less wheat in 1921 than in 1913, and we were producing 20 percent per capita more wheat in 1921 than in 1913, it resulted in a total disparity of nearly a 40 percent surplus of wheat.

Now, what I do not understand is this: I am heartily in agreement with some plan that might accomplish what I understand to be your purpose, but I am trying to get the practical side of it. Of course, we are all theorists on this thing, but, to get the practical end of it, how can we manipulate this to prevent a situation where the wheat farmers in our great wheat belt, and where the cotton farmers in our great cotton-growing South, will be up against it because of a drought or because of over-production, and who will be urging us to manipulate this currency to meet their own situation?

Mr. FOSTER. It seems to me that the answer would be this, that when you bring basic commodities in line, so far as price is concerned, with the existing debt level, it will erase a lot of difficulties that you have cited here now.

Another thing that occurs to me is this, that you have raised the question, suppose that we had 40 basic commodities governing the purchasing power of the dollar, and something went wrong with one of those commodities, such as would be caused by a drought, an extreme short crop, or extreme overproduction because of too much rain or something, and the point that you raise is, what would the producers of that particular commodity be seeking from Congress to correct their problem?

Mr. WOLCOTT. Yes.

Mr. FOSTER. It does not seem to me that when you use a base as broad as 40 commodities, very much is going to get wrong with many of those commodities for any specific year. In other words, as far as the base is concerned, one commodity going out of line for 1 year will not affect the total, because it may be but one-fortieth of the whole group, and I think that if one of those groups of producers finds that something is terribly out of joint in any one particular industry, that group as a unit has got to do some adjusting of its own supply and demand.

Mr. WOLCOTT. Now, if India, Chile, and other cotton-producing countries continue to increase their production as they have during this last year or so, to the prejudice of our exports of cotton, there will be a constant and continual decline in the world demand for our cotton. We have to meet that situation, because I think it is here, and I do not mind saying frankly that I think it is here because the administration has so forced up the price of cotton that the foreign countries cannot afford to purchase it. That is my own personal opinion; I do not expect anybody to agree with me. But I think that we are losing our possibilities of marketing rural products because of this program of artificially forcing up prices, so that foreign markets cannot afford to buy from us, and if that continues for 3 or 4 years, we cannot expect any other result than that the cotton growers are going to considerably restrict their market.

The same is true of wheat, and we have to reconcile ourselves to the fact that we cannot continue to compete with the acceleration in the production of wheat in foreign countries, to the extent that we are ever going to get back the wheat markets that we had years ago.

It is very well to say that the wheatgrowers should go into the business of growing something else, or that the cotton growers should go into the business of growing something else; that diversified farming is what we have been trying to sell the farmers for a good many years, but if wheat happens to be ordinarily 50 percent of the value of the farm crop, a change such as has been referred to in any one year in the situation with respect to wheat would throw the whole thing out of balance.

So, after all, we cannot rely upon these 40 basic commodities, or even upon the 784 basic commodities which the Department of Labor takes in establishing their price index. We have to get more or less specific instances. This Congress is always dealing with specific crops or with specific individuals, and so if we could adopt any plan which would meet this whole situation, it would be very simple, but I know that our subcommittee last year—and I think that Mr. Goldsborough will agree with me—for 7 steady weeks lived, slept, and ate with this problem, and that was constantly confronting us, what we could do to stabilize the individual crops when they became divorced from the basic commodities.

Mr. FORD. You say that we cannot sell cotton because it is too high. We exported less cotton at 5½ cents than we are exporting today.

Mr. WOLCOTT. You will recognize, will you not, that something has happened to the cotton market?

Mr. FISH. In the first place, I question the gentleman's figures very seriously. We have lost 60 percent of our cotton exports.

Mr. FORD. Since when?

Mr. FISH. In the last year and a half, and you might want to know, because I have the figures here, what our wheat export situation is.

We have exported, from July until March 16, 3,000,000 bushels, and we imported 16,000,000 bushels.

I do not think that the Congress or anyone else has the slightest idea of what is going on in the cotton market.

Mr. FORD. You will find that there was less cotton shipped when the price was down to 4½ and 5 cents than since it went up.

Mr. FISH. In the last year and a half we lost 60 percent of our export trade.

Mr. GOLDSBOROUGH. As I understand Mr. Foster, he is not here making an argument on behalf of any of these various "initialed" organizations downtown. His argument is that if we had adopted a commodity dollar in 1920, for instance, we would not have had this terrible catastrophe that we have had, and it would not have been necessary to create these various "initialed" organizations.

Is that right?

Mr. FOSTER. Correct.

Mr. DIRKSEN. He does not mean that.

Mr. GOLDSBOROUGH. That is what he says he means, and that is what I think is true, also.

What I think is this: I think that if we could have had a compensated dollar in 1920 up to the present time, the price of all basic commodities would have been stabilized, and our whole industrial and credit system would have been stabilized and placed on the same level, and overproduction would have been very greatly minimized in any given commodity, and, furthermore, this depression never would have taken place.

Mr. GIFFORD. Do you think that it has any relation whatever to overproduction?

Mr. GOLDSBOROUGH. Of course I do.

Mr. WOLCOTT. I think that it is generally agreed that our problem of overproduction is more one of distribution than it is of production.

Mr. GOLDSBOROUGH. And underconsumption.

Mr. WOLCOTT. Underconsumption is directly affiliated with distribution, because if you can distribute your crops in the United States, they will be consumed.

I do not know, and I hope that what Mr. Goldsborough says is correct, but I cannot see where the establishment of a commodity dollar would help the farmers on 5,000 acres of sugar beet ground in the State of Michigan which have gone out of production, because of the sugar allotment policies of the A. A. A. I cannot for the life of me see where the commodity dollar would affect materially the fact that in Portland, Maine, today, in the midst of the largest potato area in the world, they are selling fewer potatoes and the farmers are getting less than 40 percent of the cost of the production because they are selling these Cuban potatoes in Boston by reason of the fact that this reciprocal treaty allows them to do it.

I think it may be called demagogic, but the statement "America for Americans" nevertheless has its appeal.

But there are so many things entering into this question that I wonder if we do not have to take them all into consideration before we say that the commodity dollar is a panacea for all of our industrial ills.

Mr. Fish. I would like to put into the record here, because that matter was brought up, that the cotton export business has diminished from 8,000,000 bales down to less than 4,000,000 bales in the last 2 years.

Mr. Cross. Would it not be appropriate for you to observe here as to whether or not the same amount of cotton has been exported from other countries?

Mr. Fish. Yes; 3,000,000 bales more have been exported from other countries.

Mr. Cross. Where?

Mr. Fish. Brazil, India, Egypt, China, and parts of Africa.

Mr. Cross. Brazil produces very little cotton.

Mr. Fish. I have given you the last figure; 3,000,000 bales more this year from those countries, and I do not want to make a prediction, but it will be a great deal more than that next year, too.

Mr. Foster. Getting back to our commodity dollar now, and I will attempt to close as soon as I can, for I do not want to hold you here too long, I have already referred to the fact that gold goes through a wide fluctuation of value, that we did have a single-commodity dollar, and that if we have our dollar tied to that commodity, with a definite number of grains, we are bound to have wide fluctuations in purchasing power over a period of years.

In the charts that I just recently passed out, you will note that although the value of corn has been rising, it has been more stable than the value of gold, that is, from 1873 on.

You will notice that the value of hides has been about as variable as the value of gold over a long period of time, and that the value of lard has been much more stable than the value of gold.

Pig iron has been declining about four-tenths of 1 percent per year, but it has been considerably more stable in value than gold. The value of copper has been about as variable as gold. The value of cotton has been more stable than the value of gold during that same period.

Over a long period of time, the value of wheat has been more stable than the value of gold, and when you average out the 8, as you will see in the last chart, the 8 commodities are far more stable than any one of the 8 taken individually, which would lead to the conclusion that if we could have our dollar based on gold, with the quantity of gold in the dollar or the price of gold fluctuating to keep the purchasing power of the dollar in line with a good-sized group of basic commodities, we could iron out a lot of troubles and a lot of our ups and downs, that get people into debt when prices rise and get them to the sheriff's door when prices fall.

I thing that anything that we can accomplish along the line of stability is exceptionally good and should be accomplished.

I appreciate the opportunity of making these remarks here this afternoon, and we shall——

Mr. WOLCOTT. In respect to this last chart, it seems to me that gold has gone up. I assume that that line means that it has gone to $35 an ounce?

Mr. FOSTER. In your last 8 years.

Mr. WOLCOTT. It seems to me that there is more disparity now between the price level of your eight commodities and the price of gold than there ever has been. If your theory is right, that the price of commodities follows the price of gold, why didn't these basic commodities try to keep up with the price of gold?

Mr. FOSTER. They did. You will notice that the average of the 8 commodities has turned up almost parallel, but has not gone as high.

Mr. WOLCOTT. The disparity was about 50 points, and now it is about 60 points.

Mr. FOSTER. Will you state that again?

Mr. WOLCOTT. The widest variation here, between 1890 and 1900, seems to be 50 points.

Mr. FOSTER. Yes.

Mr. WOLCOTT. And the disparity at the present time is about 60 points.

Mr. FOSTER. The reason for that is that the value of gold has gone up tremendously since about 1896, and the value has gone way out of line with the value of commodities.

Mr. WOLCOTT. You do not mean 1896, do you?

Mr. FOSTER. The value of gold has been increasing ever since about 1896.

Mr. WOLCOTT. According to your chart, the value of gold has been steadily going down since 1896, and reached a low in 1920, and now it is way up to an index of about 160.

Mr. FOSTER. You are correct as to from 1920 on, but we had a fall from 1896 on.

Mr. WOLCOTT. In 1933 there was a rise in the price of commodities, but still there was the widest disparity between the price of gold and the price of commodities.

Mr. FOSTER. That line represents the value of gold to the value of commodities. The value of gold has gone up at a tremendous rate, much faster than prices have gone up.

Then, the price of gold and the value of gold are two different things. Value is its exchange for commodities, and price is the exchange of currency for gold.

Mr. WOLCOTT. What is it you claim, that the price of commodities follows the price of gold?

Mr. FOSTER. The price of commodities follows the price of gold very closely.

Mr. WOLCOTT. But it does not necessarily follow that the value of gold does?

Mr. FOSTER. No. When gold becomes more valuable, the price of commodities goes down.

Mr. WOLCOTT. That is value in terms of purchasing power.

Mr. FOSTER. Purchasing power for commodities.

Mr. WOLCOTT. And we should not be too technical in reducing the purchasing power in terms of dollars, because when we reduce it in terms of dollars, we get this wide disparity which we do not get in terms of purchasing power.

Mr. FOSTER. Yes.

Mr. GOLDSBOROUGH. You had a statement that you also desired to include?

Mr. FOSTER. Yes; I have it here.

Mr. GOLDSBOROUGH. Without objection it is so ordered.

The CHAIRMAN. The committee will adjourn until 10:30 o'clock tomorrow morning.

(Thereupon, at 5 p. m., an adjournment was taken until Tuesday, Mar. 26, 1935, at 10:30 a. m.)

(The statement referred to was previously incorporated in this record; but the charts referred to by the witness follow.)

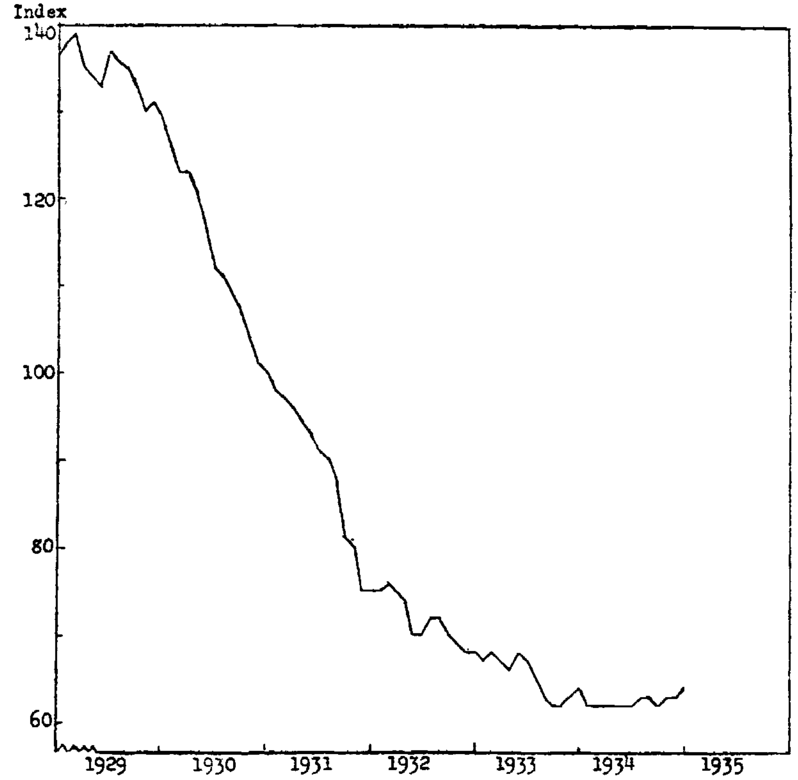


FIGURE 1.—Prices of raw materials in six countries expressed in pre-war gold currencies. 1913=100

Prices declined with great rapidity for three years, less rapidly for one year, and have been nearly stationary for about a year and a half.
Apparently the rapid increase in the value of gold has been checked.
Prices in gold are lower than at any previous time for a century and a half.

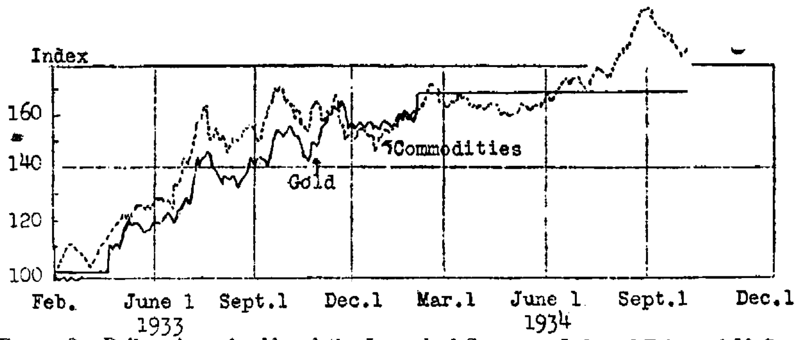


FIGURE 2.—Daily prices of gold and the Journal of Commerce Index of Prices of 30 Commodities. February 1933 to October 1934.

February 1933=100

Since prices in gold-standard countries have declined only a little during the year, prices in the United States moved approximately in proportion to the dollar price of gold.

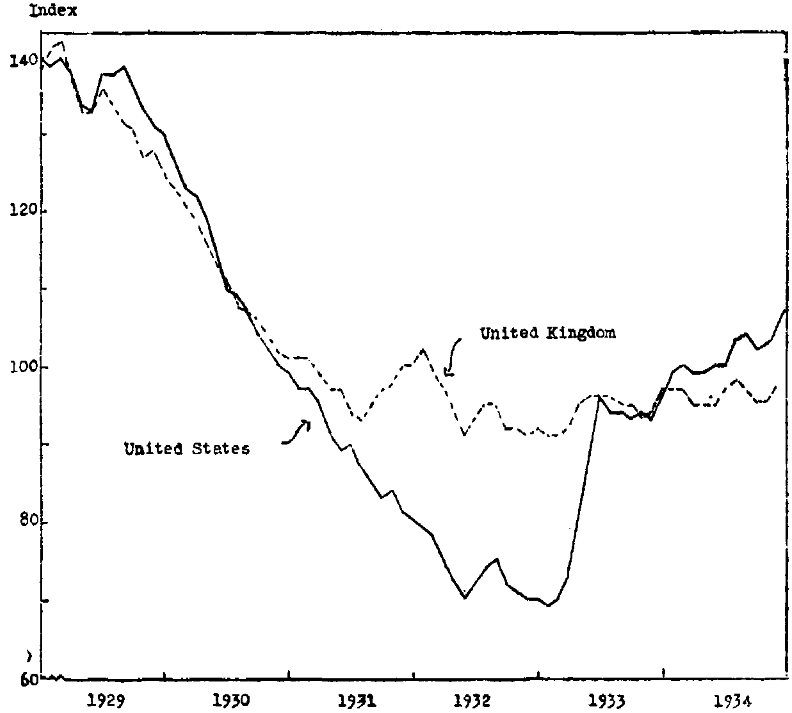


FIGURE 3.—The Sauerbeck-Statist index number for England and a comparable index number for the United States.

1913=100

PRICES IN CURRENCY

By suspending the gold standard and raising the price of gold in September 1931, at a time when gold was rapidly rising in value, England stopped the decline in prices. By raising the price of gold in 1933, prices in the United States were brought to the English level.

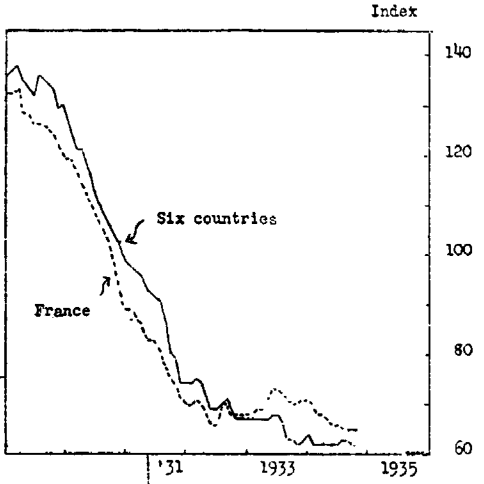


FIGURE 13.—France has maintained the gold standard and her prices have followed the world level of commodity prices in gold.

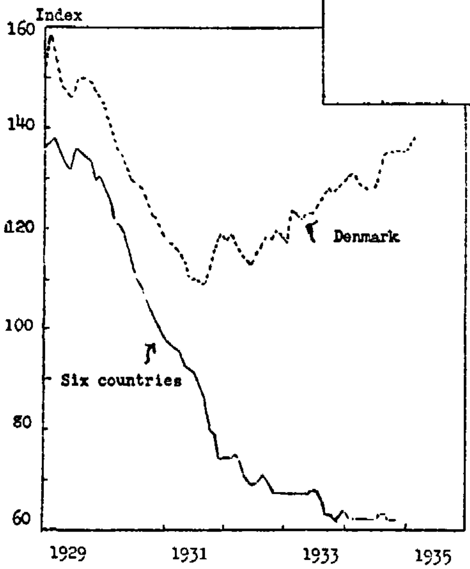


FIGURE 14.—Currency prices of commodities in Denmark followed the world level of commodity prices until she left the gold standard in 1931. Denmark has doubled the price of gold and prices have risen.*

* Denmark — 118 commodities.

FIGURES 13–14.—Prices of basic commodities in six countries in gold and prices in France in pre-war gold and in Denmark in currency.

1913 = 100

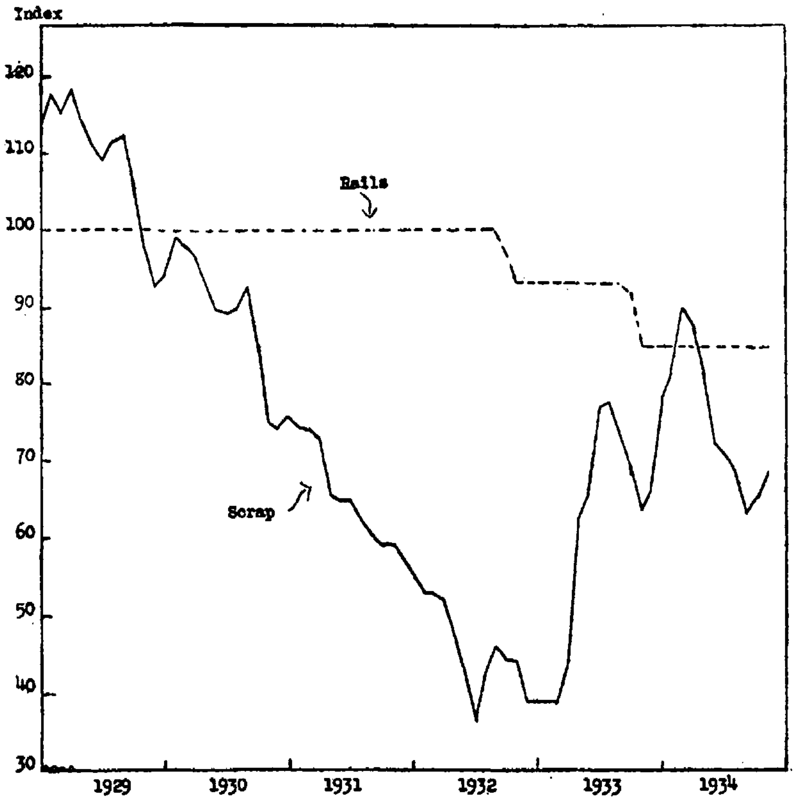


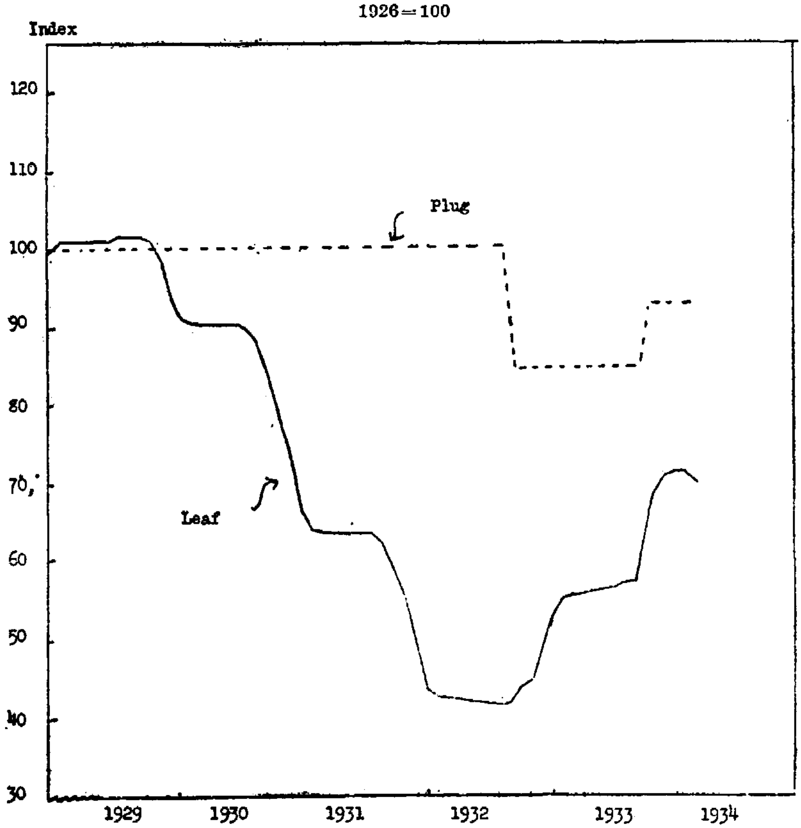
FIGURE 17.—Wholesale prices of scrap steel (Chicago) and steel rails (mill) (United States Bureau of Labor).

1926=100

In February 1933, scrap steel was selling for approximately one-third the September 1929 price. This is a 65 percent decline in the price of scrap steel. During the same period, steel rails declined 7 percent. With the advancing premium for gold, scrap steel rose 76 percent in November, or more than the advance in the price of gold, which was 69 percent. Steel rails fell somewhat.

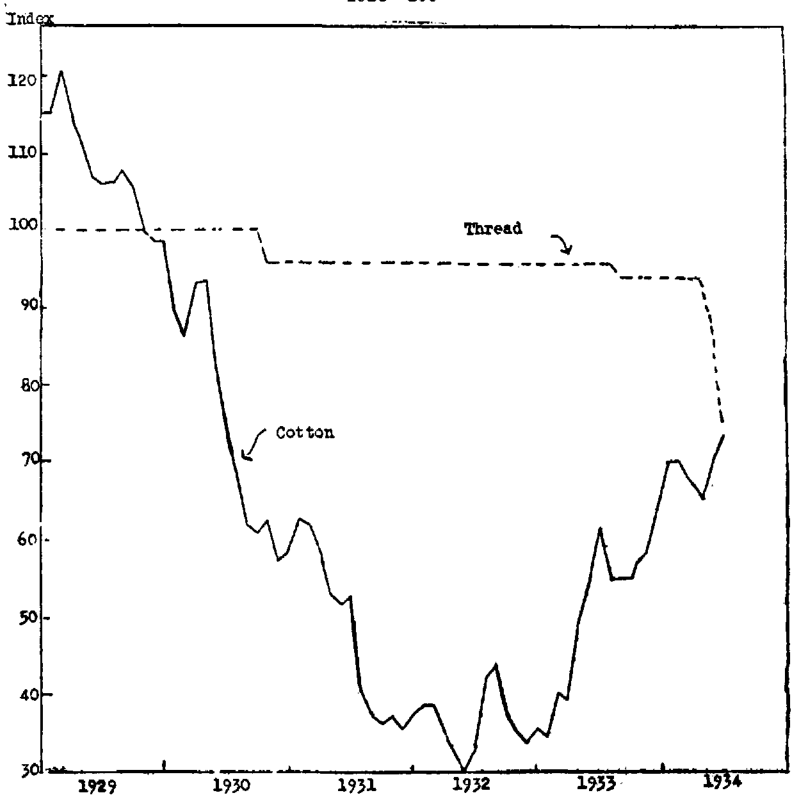
WHOLESALE PRICES OF TOBACCO LEAF AND PLUG TOBACCO (UNITED STATES BUREAU OF LABOR STATISTICS)

1926=100



From September 1929 to February 1933, wholesale prices of leaf tobacco fell 46 percent, and plug tobacco 16 percent. This resulted in a striking disequilibrium in the price structure. Reflation was accompanied by an advance of 27 percent in the price of leaf tobacco and a 9-percent advance in plug tobacco. Remarkable progress has been made in establishing an equilibrium in the price structure.

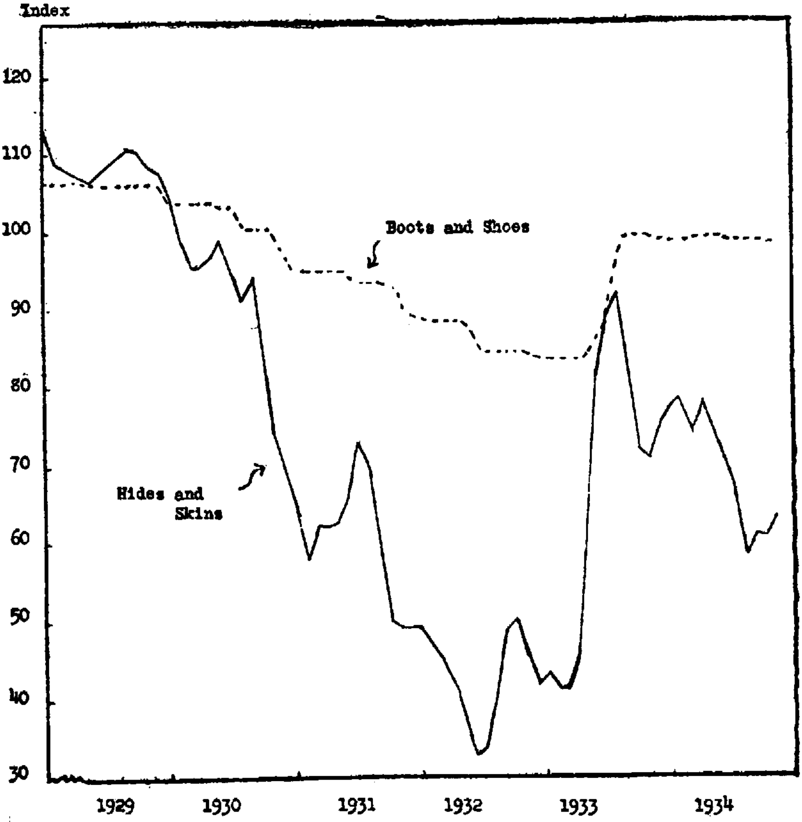
WHOLESALE PRICES OF COTTON AND THREAD
(United States Bureau of Labor Statistics)
1926=100



From September 1929 to February 1933, cotton declined 68 percent in price, while thread declined only 4 percent. From February 1933 to April 1934, cotton advanced 97 percent, but thread declined 2 percent.

FIGURE 18.—Wholesale prices of hides and skins and boots and shoes (United States Bureau of Labor)

1926=100



From September 1929 to February 1932, hides and skins fell 63 percent, and boots and shoes 21 percent. With the 69-percent advance in the price of gold, hides and skins rose 54 percent; boots and shoes rose 17 percent. After a period of incomplete deflation a rise in the price of gold causes a rapid increase in the prices of those commodities which declined sharply and little change in those inflexible prices which lagged in the price collapse. A rise in the price of gold relieves inflexible prices from falling.

TABLE 1.—*Index numbers of the price of gold in various countries*

	England	South Africa	India	Canada	United States	Sweden
December 1929	100	100	100	100	100	100
December 1930	100	100	102	100	100	100
July 1931	100	100	101	100	100	100
October 1931	125	100	127	112	100	116
December 1931	144	100	144	121	100	143
July 1932	137	102	137	115	100	147
October 1932	143	102	142	110	100	153
February 1933	142	144	141	120	100	147
July 1933	146	148	146	148	140	156
October 1933	155	157	155	152	149	165
Oct. 5, 1934	167	167	166	165	169	178
Dec. 3, 1934	166	166	165	166	169	177
Mar. 6, 1935	173	173	172	172	169	185

	Norway	Finland	Denmark	Australia	New Zealand	Argentina	Japan
December 1929	100	100	100	102	100	104	100
December 1930	100	100	100	109	100	128	100
July 1931	100	100	100	131		138	100
October 1931	121	109	122	163	138	186	101
December 1931	145	149	144	181		165	115
July 1932	152	164	140	172	150	165	182
October 1932	156	170	152	179	157	165	216
February 1933	153	169	176	179	178	165	240
July 1933	160	171	180	184	183	167	242
October 1933	170	181	191	195	194	166	267
Oct. 5, 1934	183	194	206	209	207	217	292
Dec. 3, 1934	182	193	204	207	206	217	291
Mar. 6, 1935	190	201	213	217	215	226	302

Switzerland and Holland still maintain their pre-war currencies. Their price of gold has continued at 100.

France, Italy, and Belgium raised the price of gold previous to the depression so that their prices are higher than before the war, but have not been changed since 1929.

TABLE 2.—*Commodity prices in currency and in pre-war gold currency*

[Pre-war=100]

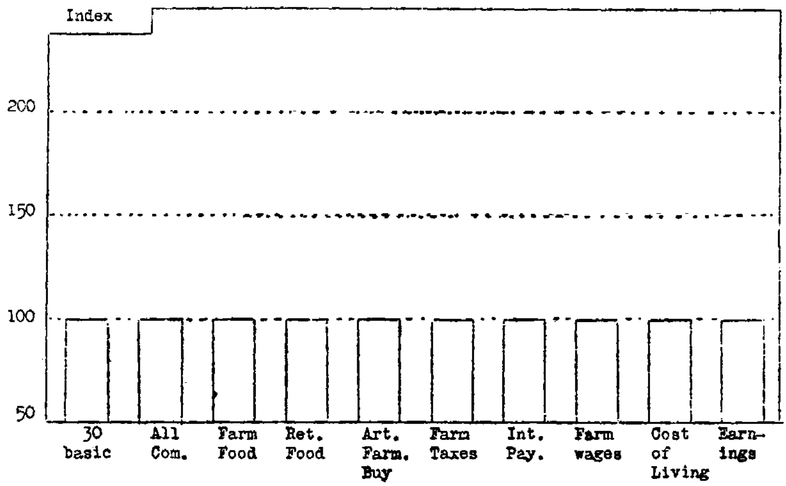
General index numbers	Month	Prices in currency	Price of gold	Prices in gold
Australia, Commonwealth Statistician, Melbourne	November	136	2.08	65
Belgium, Ministry of Industry and Labor	December	458	6.94	66
Canada, Dominion Bureau of Statistics	January	112	1.69	66
Denmark, Statistical Department	do	135	2.07	65
England, Board of Trade	December	104	1.66	63
France, General Statistical Bureau	January	349	4.92	71
Holland, Central Bureau of Statistics	do	78	1.00	78
Italy, Riccardo Bachi	December	276	3.67	75
New Zealand, Government Statistician	do	134	2.08	64
Norway, Central Bureau of Statistics	do	125	1.82	69
Sweden, general index	January	116	1.80	64
Average, 11 countries				68
United States (Bureau of Labor Statistics "All-commodity")	January	115	1.69	68

No country can keep its prices in gold far out of line with world prices.

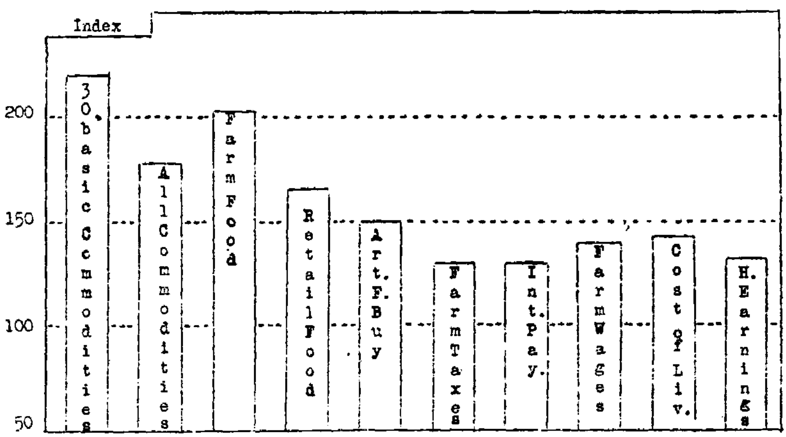
Prices in the United States are about as much above the world level as we have raised the price of gold.

No further important advance is to be expected unless there is (1) a world-wide rise in prices in gold, i. e., a fall in the value of gold; or (2) an increase in the price of gold.

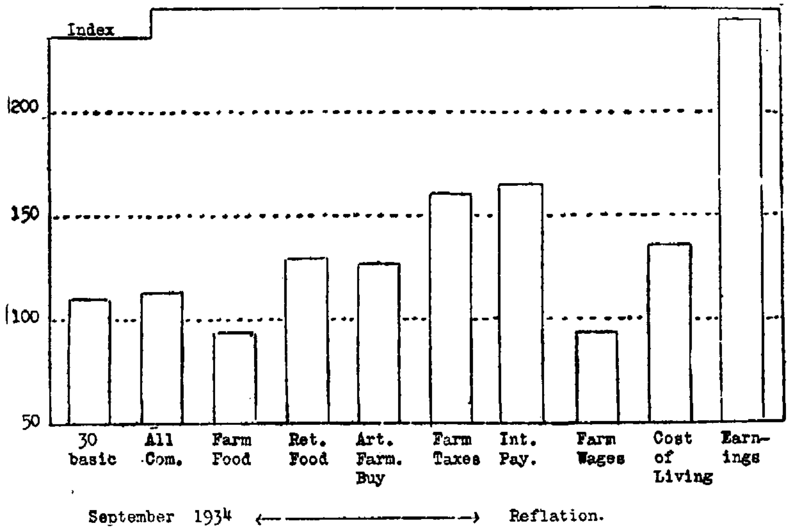
Since February 1933 the general index for Italy has fallen 3 percent, for Belgium 11, and for France 14 percent. Conditions in these countries have grown steadily worse.



1910 - 14 ←——————→ Equilibrium



June 1917 ←——————→ Rising Prices

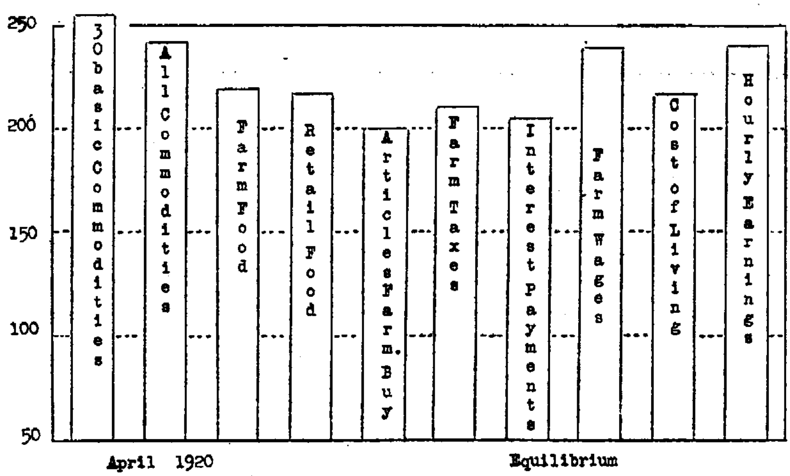


The United States Bureau of Labor all-commodity index, which includes many prices that had not declined much, has risen 32 percent. Raw materials rose 59 percent. The Journal of Commerce index for 30 basic commodities has risen 98 and prices paid to farmers 95 percent. Those things which fell most have, in general, risen most, but are still low compared with things that fell little.

TABLE 3.—*Comparison of business activity and currency prices of gold*

	Industrial production [1] July or August 1934 (1928=100)	Index of price of gold, July 1934 (par=100)
Japan	149	282
Chile	128	200
Denmark	125	201
Norway	110	179
Sweden	108	174
Great Britain	105	163
Italy	87	100
Canada	85	167
France	76	100
Austria	74	126
Czechoslovakia	70	120
Belgium	70	100
United States	69	169
Netherlands	67	100
Poland	62	100

[1] Comparative Recovery, New York Times, p. 14, Nov. 3, 1934.


250
200
150
100
50
30 basic Commodities
All Commodities
Farm Food
Retail Food
Articles Farm. Buy
Farm Taxes
Interest payments
Farm Wages
Cost of Living
Hourly Earnings
April 1920
Equilibrium

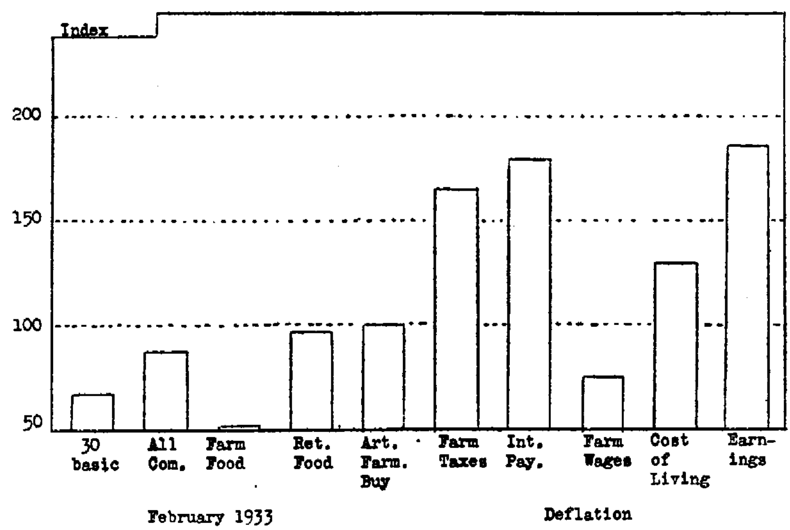

Index
200
150
100
50
30 basic
All Com.
Farm Food
Ret. Food
Art. Farm. Buy
Farm Taxes
Int. Pay.
Farm Wages
Cost of Living
Earn-ings
February 1933
Deflation

TABLE 4.—*Economic conditions in the United Kingdom* [1]

	Percent change from August 1933 to August 1934	Percent change from 1929 to August 1934
Electricity generated	+11	−4
Orders received by heavy electrical manufacturing industry:		
Home	+37	−19
Export	+38	−12
Total	+43	−15
Coal consumption	+11	−8
Motor-vehicle registration (July)	+12	+14
Building activity	+11	+57
Iron and steel consumption	+47	−18
Cotton consumption	−10	−6
Movement of shipping	+3	−3
Employment in all trades	+4	0
Bank clearings:		
Provincial	−3	−5
London	+4	−5
Complete index of activity	+6	0

[1] Data taken from The Economist, pp. 18 and 19, Sept. 29, 1934.

Year	United States Bureau of Labor wholesale prices all commodities (1910–14 = 100)	United States Bureau of Labor raw materials (1913 = 100)	United States Department of Agriculture prices paid to farmers (1910–14 = 100)	Farm wages (1910–14 = 100)	National Industrial Conference Board hourly earnings males (July 1914 = 100)	Cost of living (1913 = 100)
1928	141	144	149	169	228	171
February 1933	87	70	55	[1] 74	183	[2] 132
January 1935	115	111	107	86	[3] 230	[3] 139

[1] January 1933. [2] December 1932. [3] November 1934.

TABLE 2—*Wholesale prices of cotton in the United States and in France*

	Prices in currency	Prices in gold
New York: Middling upland, cents per pound:		
February 1933	6.1	6.1
March 18, 1935	10.65	6.3
Percent advance	75	3
Havre, France: American cotton, francs per 50 kilograms:		
February 1933	209	209
March 18, 1935	222	222
Percent advance	6	6

TABLE 1.—*Index numbers of the value of gold in six countries*

[In pre-war gold currencies, 1913=100]

	England	Sweden	Canada	France	Italy	United States	Average six countries
1928	68	----------	64	----------	----------	65	----------
1929	74	77	65	79	81	74	75
1930	88	84	78	93	101	88	88
1931	110	103	108	123	125	111	112
1932	147	152	132	145	141	135	141
1933	156	169	156	141	145	152	152
1932:							
January	141	145	128	143	135	125	135
February	139	145	125	143	135	127	135
March	135	141	125	141	133	128	133
April	133	147	125	143	137	133	135
May	141	147	130	147	143	139	141
June	147	147	137	152	145	143	145
July	147	152	135	152	147	139	145
August	147	154	133	145	141	135	143
September	147	154	132	143	139	133	141
October	156	161	133	147	143	139	145
November	161	164	139	147	145	141	149
December	164	161	145	147	145	143	149
1933:							
January	156	161	143	147	143	143	149
February	156	164	149	147	143	145	149
March	156	161	147	145	143	143	149
April	154	164	147	145	145	143	149
May	154	167	152	141	147	145	149
June	149	164	149	137	143	139	147
July	152	167	149	137	143	145	147
August	154	175	154	139	145	145	152
September	164	182	164	141	145	159	159
October	169	179	169	143	149	159	159
November	164	179	172	143	147	169	161
December	159	172	169	141	147	169	159
1934:							
January	159	167	167	141	145	167	156
February	169	172	172	143	143	169	161
March	167	172	175	147	141	169	161
April	167	169	175	147	143	169	161
May	169	169	172	149	143	169	161
June	172	169	167	152	145	169	161
July	169	169	167	152	143	169	161
August	167	169	161	154	145	164	159
September	169	172	161	154	145	161	159
October	175	175	164	154	145	167	161
November	172	169	164	154	143	164	161
December	172	169	167	------	141	161	----------

TABLE 2.—*Index numbers of the currency prices of gold in various countries, December 1934*

	Index		Index
Belgium	100	United States	169
France	100	Straits Settlements	174
Germany	100	Sweden	178
Holland	100	Norway	182
Italy	100	Finland	195
Poland	100	Denmark	205
Switzerland	100	New Zealand	208
Czechoslovakia	120	Australia	210
Austria	127	Argentina	218
Yugoslavia	131	Uruguay	218
Egypt	[1] 163	Greece	234
India	166	Spain	239
England	166	Colombia	255
Portugal	166	Japan	292
Canada	167	Mexico	303
South Africa	168		

[1] November.

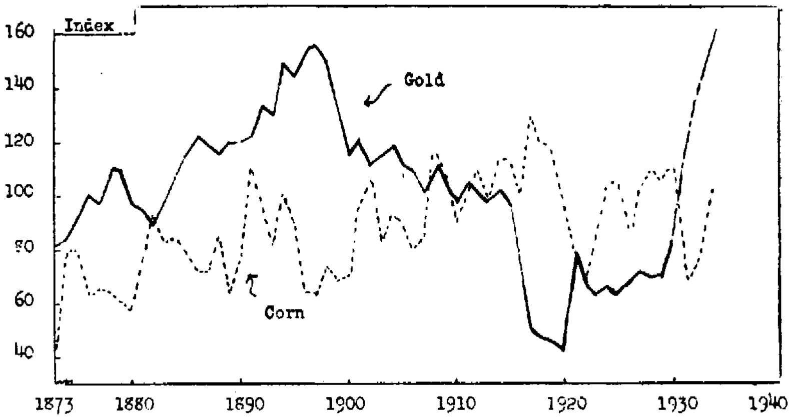


Figure 24.—Index numbers of the value of gold and value of corn in terms of 30 basic commodities, 1873–1934

Although the value of corn has been rising, it has been more stable than the value of gold.

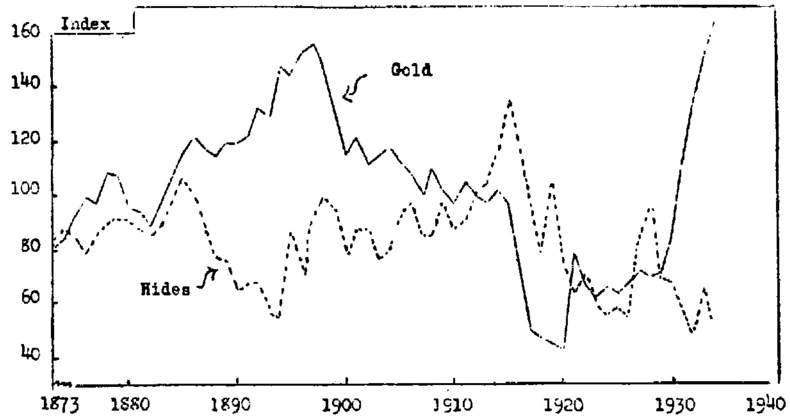


Figure 25.—Index numbers of the value of gold and value of hides in terms of 30 basic commodities, 1873–1934

The value of hides has been about as variable as the value of gold.

127297—35——42

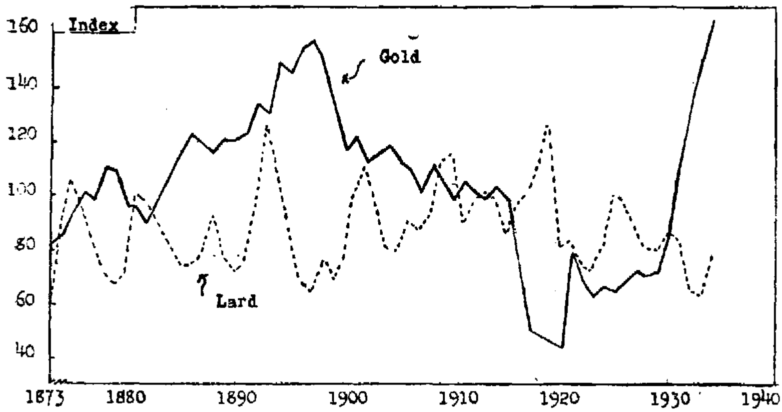


FIGURE 26.—Index numbers of the value of gold and value of lard in terms of 30 basic commodities, 1873–1934

Over long periods of time the value of lard has been much more stable than the value of gold.

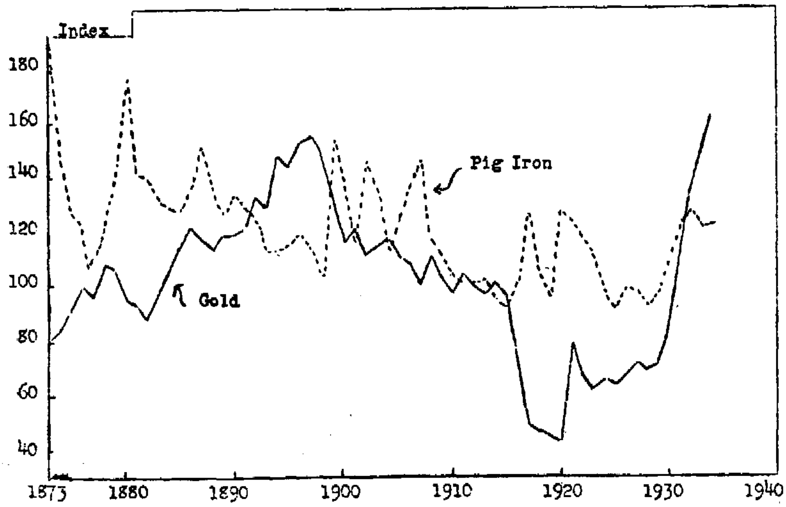


FIGURE 27.—Index numbers of the value of gold and value of pig iron in terms of 30 basic commodities, 1873–1934

Although the value of pig iron has declined about 0.4 percent per year, it has been more stable than the value of gold.

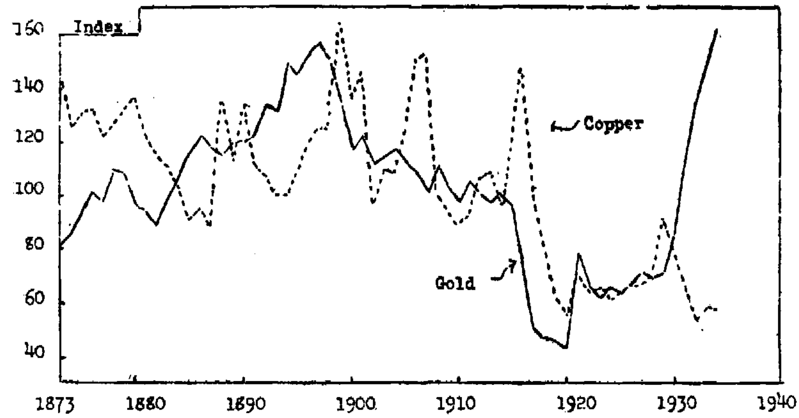


FIGURE 28.—Index numbers of the value of gold and value of copper in terms of 30 basic commodities, 1873–1934

The value of copper is about as variable as the value of gold.

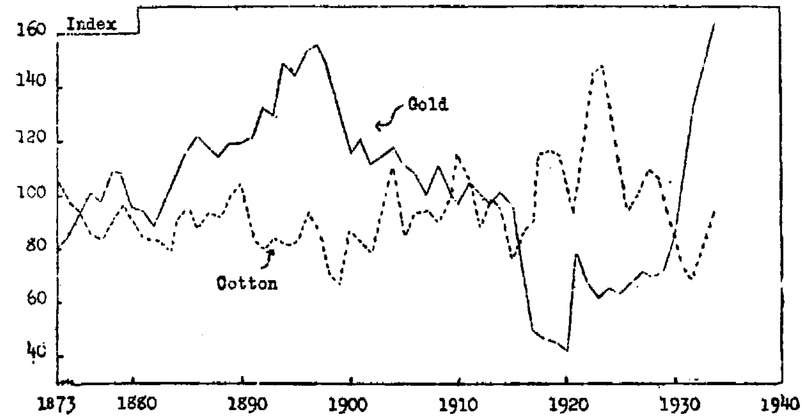


FIGURE 29.—Index numbers of the value of gold and value of cotton in terms of 30 basic commodities, 1873–1934

The value of cotton has been more stable than the value of gold.

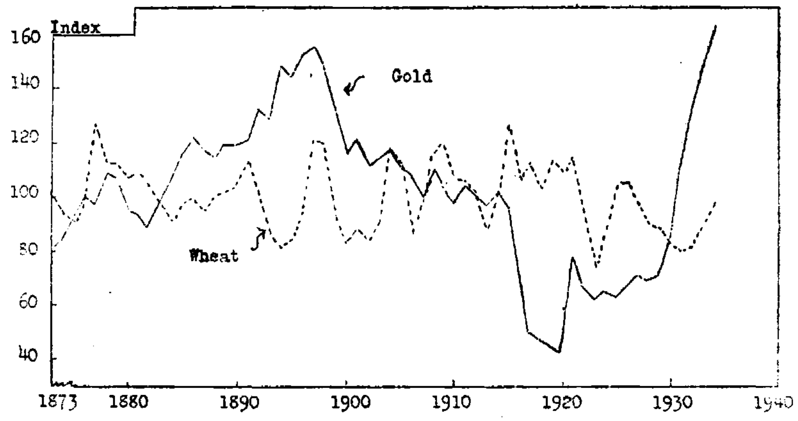


FIGURE 30.—Index numbers of the value of gold and value of wheat in terms of 30 basic commodities, 1873–1934

Over long periods of time, the value of wheat has been more stable than the value of gold.

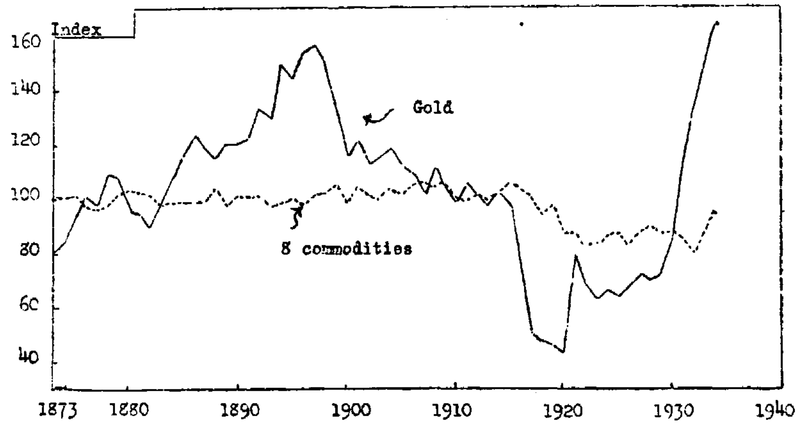


FIGURE 31.—Index numbers of the value of gold and the average value of 8 commodities. 1873–1934

The average of 8 commodities—corn, wheat, cotton, pig iron, copper, lard, hides, and gold, is much more stable than the value of gold. Our one-commodity gold dollar has been much more variable than an eight-commodity dollar would have been.

FURTHER STATEMENT OF E. A. O'NEAL

Mr. GOLDSBOROUGH. Mr. O'Neal, have you any other witness that you would like to have heard?

Mr. O'NEAL. That is all that we had arranged for today. I asked Chairman Steagall if he would allow Mr. Taber to file his statement, because he could not be here.

Mr. GOLDSBOROUGH. You have arranged that with Mr. Steagall?

Mr. O'NEAL. Yes; and he said that it would be all right, and we will put Mr. Taber's statement in.

In closing, I want to thank you for the courtesy and for the splendid attention that your committee has given to us, and we hope for proper action on our definite recommendations.

Mr. Chairman, I just want to say this to the committee, in answer to one of the questions asked a while ago by the distinguished gentleman from Michigan.

Mr. WOLCOTT. Do not get me into an argument. [Laughter.]

Mr. O'NEAL. No country in the world can go but a certain distance. Today Japan may have what they call a stabilization fund, whereby they arrange the costs of exporters and importers—in other words, they are getting our markets because of their great deflation. They are getting world markets. There is no question about that. They stand first, and Great Britain stands second in world commerce today. When they buy their raw materials, necessarily, with the great deflation, they have to pay in their currency and it reaches into a very high price.

Now, they check back so as to keep an equilibrium.

Mr. BROWN of Georgia. Has the export of cotton fallen any more than any other commodity?

Mr. O'NEAL. No; it has decreased less.

The distinguished gentleman from New York has made a statement with respect to that, and I have right before me the March 1 report of the Department of Agriculture, with respect to the exports of cotton from this country, and I want to say this, as a cotton grower, that I am 60 years old, and I have heard for many years that we were losing our market for cotton. But I am not greatly disturbed. I am disturbed in this regard, Mr. Fish, that if you lower the tariff, so that we can trade, commodity for commodity——

Mr. FISH. You started to make a statement there, but you have not made it.

Mr. O'NEAL. In other words, the statement is this——

Mr. FISH. You are talking about the tariff and not about the loss of the cotton market.

Mr. O'NEAL. The tariff has a great deal to do with it. In other words, I have heard for many years——

Mr. FISH. We are talking about facts, and not about what you heard 40 years ago.

Mr. O'NEAL. I knew facts 40 years ago as well as you do now, I believe.

Mr. FISH. I sort of doubt it.

Mr. O'NEAL. In those years, I heard that we were going to lose our foreign market of cotton, and we have not yet.

Mr. Fish. Mr. Chairman, he questioned my statement, and I want to know whether he questioned my statement that we have lost 50 percent of the markets in the last 2 years.

Mr. O'Neal. We have lost, Mr. Fish, our market to a considerable degree, but the main reason for losing that market was because they have not the buying power in Europe to buy cotton.

Mr. Fish. I did not ask the reason. I made a definite statement, and if you are contradicting that statement, I want to know what the facts are.

Mr. O'Neal. I am not contradicting your statement, but I heard such things long ago.

Mr. Fish. You are denying it.

Mr. O'Neal. I heard such things long years ago, that we were losing our market, but yet cotton has lost a smaller percentage than any of our exports, and this record shows that in 1934 we exported 5,753,000 bales of cotton.

The present situation is, as I said, because Europe cannot buy, but if we will do a little trading with Europe, and if we follow Great Britain's policy, of a managed currency, or a commodity dollar——

Mr. Fish. May I ask the gentlemen a question?

The Chairman. Let him finish.

Mr. Fish. He has made his statement, that he thinks the tariff should be reduced. He made the statement that the tariff should be reduced in order to provide buying power abroad, but I would like to call attention to the fact that this processing tax is nothing but a tariff in our country. How can we consistently advocate a processing tax, which is a tariff within our own country, in the 48 States, and then suggest that we should reduce the tariff for somebody else?

Mr. O'Neal. Might I answer that I have been a free trader on cotton up until the time we had the Agricultural Adjustment Act, and I myself helped to try to persuade some of our associates in Congress to put a tariff on cotton textiles, to help the cotton manufacturer.

We paid the bill, believe me; the cotton producers paid it. The 50 or 45 percent of our cotton farmers in the South have a standard of living no higher than a Chinese. We paid the bill with the tariff system.

Now, when we had the opportunity, we came to Congress and the President and asked if we might have a little tariff or a little butter on bread in the way of a processing tax, and if you will compare the processing tax on cotton to the tariff on textile mills today dollar for dollar with yards of thread, you will see that we are getting a very small tariff as compared to the textile industry in this country—very small.

Mr. Fish. One is against farmed goods, and the other is on goods produced in our own country.

Mr. O'Neal. We produce cotton ourselves. In other words, you have a shirt on that I grow the cotton for. Your shirt has about a pound of cotton in it; that is all. The processing tax is 4.2 cents a pound on the raw cotton, and when a mill in the State of New

York, or in Connecticut, gets a pound of cotton from Alabama, they have about 0.71 of a pound of material that goes into cloth; the other is waste. So you are paying me a nice little tariff of about 3 or 4 cents, and your manufacturers in New York are getting an ad valorem tariff there of about, I think it amounts to, 37½ cents on each shirt.

Mr. FISH. It is not enough; that is all I tell you.

Mr. O'NEAL. You fixed it, all right.

In some instances you get over 100 percent ad valorem.

Mr. FISH. They only brought in 20,000 square yards of Japanese cotton goods last month.

Mr. O'NEAL. In other words, what is butter for your bread is not good for my bread; that is your conclusion. Why should you hold an argument that you would penalize the very poor agricultural population of the United States, where in the South especially the standard of living is lower than that of a Chinese? You let them sweat their lives, blood, and flesh for generations producing cheap raw material, in order that you could have a 100-percent ad valorem tariff. That is very consistent!

Mr. FISH. What you have done by this processing tax is that you have put a tariff on commodities raised in this country which we never had before, and that is nothing but a processing tax against your consumers. And I want you to remember this, that I am an American before I am a northerner, and I think that the future of the South is just as important as the future of the North, and I am positive that if this thing continues another 2 years, you will not have any exports at all, regardless of what happened 40 or 50 years ago.

Mr. O'NEAL. We come before your committee recommending very definite steps to improve the situation, and, as I see it, I think that with a managed currency we will take a long step toward the solution of this problem, and I know this, that the Congress of the United States in 1933 voted on this Adjustment Act, and we had to take it because we were in that situation, and Congress was wise when it wrote the law. It took the three great fundamental things that the farmers had been fighting for and put them in one bill, parity of prices to the farmers, rural credits for farmers, and the Thomas amendment.

Now, we are making progress, and we come to you, and we ask you in your judgment to come along with another angle of it, and let us be sure to use the wit and judgment that Yankees had the reputation of using, meaning Americans, over the years. We have that opportunity, or we will move the ball, and I think that we would do well to look at and study Great Britain's policy. They are pretty wise.

May I just stop with this, that if you were to ask me what are the important things in producing a crop, I might be so cranky as to tell you that the only thing you ever use is water, and another man over here might say that the only thing you have got to have is land, and another fellow over here would say good seed and cultivation, and yet I see men charged with responsibility in this country that advocate all water, all land and all cultivation to raise a crop, and I say that we have a policy that we are engaged in that is as involved as producing the crop. Fundamentally, with us, we simply have got to have an honest medium of exchange, and what we are recommending to you will help to solve the cotton problem and all of these other problems.

Thanks; I did not mean to make a speech to the committee.

The CHAIRMAN. We are certainly glad to have heard you again.

The committee will adjourn until 10:30 o'clock tomorrow morning.

(Thereupon, at 5 p. m., an adjournment was taken until Tuesday, Mar. 26, 1935, at 10:30 a. m.)

BANKING ACT OF 1935

TUESDAY, MARCH 26, 1935

HOUSE OF REPRESENTATIVES,
COMMITTEE ON BANKING AND CURRENCY,
Washington, D. C.

The committee met at 10.30 a. m., Hon. Henry B. Steagall (chairman) presiding.

The CHAIRMAN. Gentlemen, we have with us this morning Mr. J. F. T. O'Connor, the Comptroller of the Currency. who will discuss title III of the bill.

I assume, Mr. O'Connor, you desire to make a preliminary statement, and if so, we will be glad to have you do that without interruption. When you conclude members of the committee will interrogate you.

STATEMENT OF J. F. T. O'CONNOR, COMPTROLLER OF THE CURRENCY; ACCOMPANIED BY F. G. AWALT, DEPUTY COMPTROLLER OF THE CURRENCY

Mr. O'CONNOR. Mr. Chairman and gentlemen of the committee, practically all of the amendments we suggest were before this committee a year ago, and the bill was approved by this committee unanimously and sent to the House. It was also approved by the Senate committee and reported to the Senate, but it was lost on the last day of the legislative session in June of last year.

Practically all of the things I am going to talk about are technical matters, largely corrections in language, with just a very few new sections suggested.

The majority of the amendments in question are based upon H. R. 9876 and S. 3748, submitted at the last session of Congress, which bills were mutually acceptable to the Federal Reserve Board and to the Comptroller's office and were favorably reported by the Banking Committees of both Houses.

A general statement of the object of the various amendments suggested in last year's bill and now resubmitted, and those added thereto in title III of this bill, are as follows. Where these amendments were not emplaced in last year's approved bills or are substantially different from those presented, the notation that they are new will appear in connection with this explanation.

Section 301, which is new gives the Federal Reserve Board discretion to exempt so-called "accidental" holding-company affiliates from the burdensome and expensive elements involved in obtaining a voting permit where such affiliate is not engaged as a business in holding bank stock.

Section 302 amends section 20 of the Banking Act of 1933, which requires the divorcement of member banks from affiliated securities companies so as to make it clear that its requirements do not extend to a securities company which has been placed in formal liquidation and transact no business except such as may be incidental to the liquidation of its affairs. This is in accord with rulings by the Federal Reserve Board and the Comptroller's office as to a proper interpretation of the law.

Section 303 (a) makes it clear that the provisions of section 21 (a) (1) of the Banking Act of 1933, prohibiting dealers in securities from engaging in the business of taking deposits, does not prevent banking institutions from dealing in, underwriting, purchasing, and selling investment securities to the extent expressly permitted to national banks under the National Banking Act and does not prevent banking institutions from selling mortgages without recourse. It will be observed that national banks are limited in dealing in and underwriting securities to doing so as to Government obligations, general obligations of States or political subdivisions, obligations issued under authority of the Federal Farm Loan Act, by the Federal Home Loan Board, or the Home Owners' Loan Corporation.

Section 303 (b) makes it clear that section 21 (a) (2) of the Banking Act of 1933 does not require that business institutions which accept deposits only from their own officers, agents, or employees need submit to examination and publication of reports of condition. Hundreds of corporations, such as the B. & O. Railroad, Chrysler Motors, Deere & Co. permit employees to leave part of their wages on deposit and in turn loan these funds to other employees so as to encourage thrift and be of assistance thereto.

This section also makes it clear that the expense of examining private banks by this office or by the Federal Reserve Board shall be paid by the institution examined, as there are otherwise no funds available to bear the expense of such examination.

Section 304, which is new, eliminates the double liability of shareholders of national banks on July 1, 1937. This provision is considered desirable because of the fact that such liability has already been eliminated as to banks organized since July 16, 1933, and as to new capital issued since that date, with the result that at the present time many banks are in the awkward position of having outstanding some common stock with liability and other common stock without liability, resulting in needless confusion. Provision is being made in section 314 of this bill for banks gradually increasing their surplus out of earnings until the same equals the bank's capital, thereby giving the creditors of the bank substantially the same additional protection which is now afforded by the assessment liability.

Section 305, which is also new, corrects the accidental omission of national banks in Alaska and Hawaii from the benefits of an act passed at the last session repealing the requirement of section 31 of the Banking Act of 1933 that directors of national banks and member banks increase the amount of their share holdings therein. This law was repealed incidentally because it was found physically impossible to enforce its requirement, with the result that many banks would have been forced to cease operations for lack of a qualified board of directors.

Section 306, which is also new, gives the Federal Reserve Board power to control relationships of officers, directors, and employees of banks with securities companies through regulation, thereby saving the great burden involved in present procedure of issuing individual permits.

Section 307 (a), which is also new, in part, makes it clear that section 16 of the Banking Act of 1933 was not intended to prohibit national banks or member banks from buying or selling stocks solely for the account of their customers and as an accommodation thereto and not for their own account.

This is extremely important, particularly in communities remote from financial centers, and since there is involved no investment by the bank of its own funds, no objection can be seen thereto. The amendment further limits national banks in purchasing investment securities for their own account to the purchase of the same in an amount as to any one issue limited to 10 percent of the bank's unimpaired capital and surplus. The present law permits such investment in any one issue to an equal amount to 15 percent of the unimpaired capital and 25 percent of surplus, except where the total issue does not exceed $100,000 and does not exceed 50 percent of the capital of the institution.

Section 307 (b) merely restates in a clearer form the existing prohibition against national banks purchasing stock for their own account.

Section 308, which is new, enacts into law present requirements of the Comptroller's office as a matter of policy that newly organized national banks have a paid-in surplus equal to 20 percent of capital before being authorized to do business, which requirements may be waived where necessary in connection with a State bank converting into a national bank.

Section 309, which is also new, eliminates any possibility of section 18 of the Banking Act of 1933 being construed as preventing corporations other than a bank from conditioning transfer of their shares on the simultaneous transfer of shares of bank stocks, but preserving the unimpeded free and unconditional transfer of bank stocks.

Section 310 (a) permits a holding company to vote on the question of placing a bank in voluntary liquidation without having to go through the expensive routine incidental to obtaining a voting permit.

As to section 310 (b), under present law, shares held by a bank as sole trustee cannot be voted. It consequently sometimes results, where a large number of shares are so held in trust, that it is impossible to obtain the requisite number of votes required by law to accomplish certain steps such as reduction in capital, amendments to articles, et cetera, or to vote to go into voluntary liquidation where such is necessary.

Provision is accordingly made that the shares so held in trust shall be excluded in determining whether the resolution in question has been adopted by the requisite number of shares. For example, a bank has 1,000 shares outstanding. Four hundred of the shares, however, cannot be voted because held in trust by the bank as sole trustee. Consequently, in determining whether or not a resolution has been adopted by the required two-thirds vote, the 400 shares held in trust will be excluded, leaving a balance of 600 shares as the basis for determining whether a two-thirds vote has been obtained, in which case a vote of 400 shares in favor of the matter would be the requisite two-thirds majority of the shares entitled to vote.

Section 310 (c), which new, eliminates any doubt that a holding company, which has met the requirements for obtaining a voting permit, may cumulate its shares in the same manner as other shareholders are permitted to do. This is in conformity with the construction placed under the present law by the Federal Reserve Board and by the Comptroller's office.

Section 311 gives discretion to the Comptroller to permit a State bank converting into a national bank to carry over and retain, subject to certain conditions, such sound assets as a State bank may have which do not conform to the requirements as to assets held by national banks.

SECTION 312 permits the Comptroller to delegate the manual labor of countersigning bond trasfers in connection with substitution of securities held to secure circulation issued by national banks.

Section 313 permits branches of national banks, which branches are located outside of the United States, to charge the same interest rate permitted by local law to competing institutions.

Section 314, which is new, provides that before the declaration of dividends, national banks shall carry not less than one-tenth part of their net profits of the preceding half year to surplus until the same is built up to an amount equal to the capital, instead of the present requirement that the same need only equal 20 percent of the capital. This change is deemed desirable in connection with the recommendation that asesessment liability be eliminated from bank stock and is further desirable from the standpoint of building up a proper capital structure.

Section 315, which is new, extends the terminal provisions of existing law relative to embezzlement, false entry, et cetera, by officers and employees of member banks to include any insured banks.

Section 316 gives the Comptroller closer supervision over national banks in voluntary liquidation as distinguished from those in receivership by requiring reports to him and to the shareholders and subjecting the banks to examination. It also enables the shareholders to remove an incompetent liquidating agent.

Section 317, which is new, extends the present prohibition on the use of the word "national" by banks other than national banks, to include any combinations of such word.

Section 318, which is also new, corrects an oversight in the present law to require member banks of the Federal Reserve System to reduce the amount of their shareholding in a Federal Reserve bank to correspond with the reduction of the bank's surplus.

Section 319 authorizes the Federal Reserve Board to prescribe the form and contents of reports of condition to be made by State member banks and prescribes the manner in which such reports must be published.

Section 320 extends to State member banks the same privileges now enjoyed by national banks with respect to the amount of loans which may be made where secured by Government obligations. This is considered desirable, because paragraph M of section 11 of the Federal Reserve Act is susceptible to a contrary consideration. As to section 321, which is new, the present law permits a Federal Reserve bank to make direct loans to private business on adequate endorsement and security. The amendment permits such loans on adequate endorsement or security.

Section 322, which is also new, has reference to par value of Federal Deposit Insurance Corporation stock in the loans to industry act, changed to "the amount paid for said stock."

Section 323 (a), which is partly new, authorizes the Federal Reserve Board to define "deposit" and related terms for reserve and interest requirements respecting deposits.

Section 323 (b), which is also new, permits amounts due from other banks to be deducted from gross deposits instead of amounts due to banks, in determining reserve requirements.

Section 323 (c) extends the power to regulate the rate of interest payment by member banks to include the rate paid by all insured banks except mutual savings banks, and Morris Plan banks which are not members of the Federal Reserve System.

Section 323 (d), which is new, requires member banks to maintain the same reserves against Government deposits as against other deposits.

Section 324 permits the Federal Reserve Board or the Comptroller of the Currency, as the case may be, to permit a waiver of report and examination of affiliates of a bank where such report and examination is not necessary in a particular case to disclose the relationship existing between the bank and the affiliate. This eliminates the burden and expense now involved in hundreds of cases where there is no beneficial object to be gained in requiring submission and publication of such report, due to the fact that the affiliate is merely a technical accidental affiliate having no relationships whatsoever with the bank, such, as for example, newspaper, clothing stores, lumber yards, et cetera, which become technical affiliates because of the accident that a majority of their directors happen to be directors of the bank.

Section 325 (a), which is also new, extends the present provisions of the law prohibiting loans and gratuities to examiners of member banks to include examiners of all insured banks.

Section 325 (b), which is also new, extends to Federal Deposit Insurance Corporation examiners the present prohibitions of law against disclosure of confidential information by examiners.

Section 325 (c), which is partly new, corrects impractical features of the present law relative to loans to executive officers of banks by vesting certain discretions with the Federal Reserve Board to issue regulations governing the same and substituting removal from office for the present criminal provisions of the law. There is also a 3-year extension of time within which present loans must be retired, such extension, however, being operative only if the board of directors adopts a resolution determining that it is to the best interest of the bank to make the extension and that the officer has made every proper effort to reduce his obligation.

Section 326 is partly new. Under the present law there are certain rigid requirements and limitations on loans to affiliates. Exception to these requirements is provided for where the affiliation arose out of foreclosure by the bank on collateral. It is often necessary to advance funds to an affiliate, control of which has been obtained through foreclosure in order to enable the bank to salvage the real value out of its assets and reduce the bank's loss.

Under the circumstances, such affiliate manifestly cannot borrow elsewhere. There is also excluded the accidental type of affiliate, control of which is obtained by the bank in a fiduciary capacity, as, for example, where the bank becomes executor and/or trustee of the deceased's estate, among the assets of which is a going business which must be operated by the bank as such trustee. There is also excluded an affiliate engaged solely in operating property acquired for bank purposes.

Section 327, which is new, exempts loans for industrial purposes made in cooperation with a Federal Reserve bank or the Reconstruction Finance Corporation from existing restrictions on real-estate loans by national banks, due to the protection received by the banks from either the Federal Reserve bank or the Reconstruction Finance Corporation, where such loans are jointly made. As to such loans there is no need for such restrictions as are desirable for a real-estate loan made by the bank in its sole capacity.

Furthermore, such existing restrictions have been found to seriously interfere with the scope and object of the Industrial Loan Act as they operate to prevent two or more banks cooperating with the Federal Reserve bank or the Reconstruction Finance Corporation in making a single industrial loan, prevents such loan where a substantial part of the security is real estate located outside of the restricted area in which national banks are limited in making real-estate loans, and for other reasons.

Section 329, which is also new, amends the Clayton Act to permit the Federal Reserve Board to supervise by regulation instead of by permit the matter of interlocking directorates.

Sections 329 and 330 bring the law governing consolidation of national banks into conformity with that governing consolidations of a State and national bank and offers additional protection to dissenting stockholders in the matter of obtaining the appraised value of their stock. Requirement is made that notice of dissent be given by such shareholders when the vote to consolidate is had.

Sections 331 and 332, which are also new, extend to the Federal Insurance Deposit Corporation the protection now given by law to other Federal institutions against the misleading use of their name and extends to all insured banks the present requirements of the law making robbery of members banks a Federal offense.

Now, in reference to the amendments we are suggesting to the committee, first, a new section to be numbered 333. It provides:

> Section 5143 of the Revised Statutes, as amended, is hereby amended by striking out everything following the words "Comptroller of the Currency", where such words last appear in such section, and substituting the following: "And no share holder shall be entitled to any distribution of cash or other assets by reason of any reduction of the common capital of any association unless such distribution shall have been approved by the Comptroller of the Currency and by the affirmative vote of at least two-thirds of the shares of each class of stock outstanding, voting as classes."

We suggest a new section 334, to read:

Section 5139 of the Revised Statutes, as amended, is amended by providing at the end of the first paragraph the following new paragraph:

"Certificates hereafter issued representing shares of stock of the association shall state (1) the name and location of the association, (2) the name of the holder of record of the stock represented thereby, (3) the number and class of shares which the certificate represents, (4) and, if the association shall issue stock of more than one class, the respective rights, preferences, privileges, voting rights, powers, restrictions, limitations, and qualifications of each class of stock issued shall be stated in full or in summary upon the front or the back of the certificates, or shall be incorporated by a reference to the articles of association set forth on the front of the certificates. Every certificate shall be signed by the president and the cashier of the association, or by such other officers as the bylaws of the association shall provide, and shall be sealed with the seal of the association."

We suggest a new section 335, to read as follows:

The last sentence of section 301 of the emergency banking act of March 9, 1933, as amended, is amended to read as follows:

"No issue of preferred stock shall be valid until the par value of all stock so issued shall be paid in and notice thereof, duly acknowledged before a notary public by the president, vice-president, or cashier of said association, has been transmitted to the Comptroller of the Currency and his certificate obtained specifying the amount of such issue of preferred stock and his approval thereof and that the amount has been duly paid in as a part of the capital of said association; which certificate shall be deemed to be conclusive evidence that such preferred stock has been duly and validly issued."

The last amendment we suggest is a new section numbered 336, as follows:

The additional liability imposed by District of Columbia Code, Supplement I, title 5, section 300 A (b) upon the shareholders of savings banks, savings companies, and banking institutions and the additional liability imposed by District of Columbia Code, title 5, section 361, upon the shareholders of trust companies, shall cease to apply on July 1, 1937, with respect to such savings banks, savings companies, banking institutions, and trust companies, which shall be transacting business on that date. Each such savings bank, savings company, banking institution, and trust company, shall before the declaration of a dividend on its shares of common stock carry not less than one-tenth part of its net profits of the preceding half year to its surplus fund until same shall equal the amount of its common stock.

May I take up these four amendments and explain them?—and then I will be ready to answer any questions you may desire to ask.

The first amendment we are suggesting to the committee, gentlemen, is briefly this: Where we permit a reduction of common capital stock in a bank we want it clear that we have the right to require the bank to retain the assets. We tell a bank, for instance, that there are so many assets that are questionable or bad, and then we ask them to reduce their capital stock.

Then the question arises, are the stockholders entitled—and in some instances they claim they are—to assets eliminated because of the reduction of the stock?

We should have the privilege, beyond any doubt, of retaining those assets as a recovery value of the bank to the stockholders, and not distribute them to the shareholders, if that is the proper position to take.

On the other hand, that is not always the case, because you might find a bank overcapitalized for a particular community because the business has gone to an adjoining community. Then we reduce our common capital, say, to $50,000, which is ample for the needs of the community. They may have cash assets that correspond to the reduction, and we do not see any injustice in having them distributed to the stockholders. But we ask that we be given the right to approve the distribution after the required vote of two-thirds of the shares.

That is the first amendment.

The CHAIRMAN. Your power under that amendment would not be any greater than the power which the Comptroller now has, in the case of the original organization of a banking association.

Mr. O'CONNOR. Not at all; it would be exactly the same.

The CHAIRMAN. Except where you require a two-thirds vote to permit the distribution of stock in the case of a reduction of capital.

Should not that be a majority, instead of two-thirds? If a majority of the stockholders think they are justified in having a distribution of their assets, and the Comptroller approves it, would not that be a fair way to handle it?

Mr. O'CONNOR. I think the only reaction there, Mr. Chairman, is the fact that the shareholders are very anxious to get some assets that we think ought to remain in the bank.

The CHAIRMAN. That is true, but you would still have to approve it.

Mr. O'CONNOR. Frankly, I think a majority vote would be all right.

The CHAIRMAN. Either way would be all right?

Mr. O'CONNOR. Either way; it does not make any difference.

Mr. GOLDSBOROUGH. Under the present law, has the Comptroller's office, or any other branch of the Federal Government, the right, upon the reduction of the capital stock, to permit the disbursement of any amount of the assets to the bank stockholders?

Mr. O'CONNOR. Oh, yes; we can permit that under the present law.

The CHAIRMAN. I do not know whether you understood what Mr. Goldsborough had in mind. I think Mr. Goldsborough meant to inquire whether or not under the present law you are given authority to approve or disapprove.

Mr. GOLDSBOROUGH. Yes.

Mr. O'CONNOR. The answer is we can, but the point is that in connectiton with this section a serious question arises as to whether or not they are always entitled to it. That is what we want to get away from.

The CHAIRMAN. There might be cases where there would be no need for that.

Mr. O'CONNOR. Yes.

Mr. HANCOCK. The law requiring a two-thirds vote instead of a majority would make it easier on you at times.

Mr. O'CONNOR. Yes.

Mr. FORD. Could not a majority of the stock be held by three or four stockholders, and a bare minority by a great number, and thus due to the control of the situation by those few stockholders, possibly the great number, if they knew the circumstances, would not want it done.

I am inclined to think that two-thirds would be better myself.

Mr. GOLDSBOROUGH. That is my opinion. You want to afford protection to the minority.

Mr. WILLIAMS. It places the full power in the hands of the Comptroller?

Mr. O'CONNOR. To reduce the common capital, but it takes a two-thirds vote to distribute it. We have two problems, the reduction and the distribution.

Section 334, which I have read to you, gentlemen, is the form of certificate to be issued when a national bank issues stock.

Practically all States now have "blue-sky" laws, but there is always a question as to whether such laws apply to national bank stock.

If the Congress speaks on questions within its jurisdiction, in connection with national banks, that excludes the States from acting, and if you fix a form of certificate for the national banks, that settles the question.

I have read the provisions that I believe ought to be in the certificate of a national bank. Every purchaser of stock should know what other stock is outstanding, and what its liabilities are, and we have asked you to incorporate that so we can compel them to do that in connection with bank shares.

Section 335 is the one we are asking you to adopt in connection with preferred stock providing that no preferred stock shall be valid until there is a certificate issued by the Comptroller of the Currency, in connection with national banks.

You have provided that already with reference to the common capital of national banks. No stock is valid until the Comptroller issues his certificate that the stock has been regularly and properly issued, and then that stops anybody from going back of the certificate to find out whether all of the technical steps have been taken leading up to the issue of the common capital stock. When that certificate is issued that settles it. We feel that the same rule ought to apply to preferred stock.

The last amendment is in reference to double liability. As I have said, we have recommended in the bill, if you shall accept it, the elimination of double liability on stock after July 1, 1937. This last amendment is merely included to apply not only to national banks, but to State banks and trust companies and savings banks located in the District of Columbia, because they also come under the jurisdiction of the Comptroller's office, although they are State institutions.

Mr. HANCOCK. What is the significance in fixing the date as of July 1, 1937?

Mr. O'CONNOR. I think probably two considerations enter into that, Mr. Congressman.

First, there is a rather serious constitutional question as to whether we could eliminate as of today the double liability on stock that has been issued, because of the contractual relation existing between the depositors and the bank, and my opinion is we could not do that.

The second consideration is that the Government has got a great deal of money invested in these banks, and we are just getting these banks in very fine condition, and it enables us, in many instances, to work out a much better situation with the bank officials than if the double liability was off at this time.

When we go into a bank and insist that it has to be strengthened to protect the depositors, and that more capital has to come into the bank, and the Government is willing to assist in it, then if they decline to do it, and decline to strengthen their bank and to get it in better condition, and we close the bank, we can impose a double liability, and the officers knowing that, those owning the bank will go much further to save the bank and make it an active, going bank than if you did not have a double liability. Those are the two reasons, as I see it.

Mr. HANCOCK. How will conditions have changed by July 1, 1937?

Mr. O'CONNOR. That is an arbitrary date. But we feel the capital structures of the banks should be in good shape by that date.

We have just set a figure along there, or a date, and we feel that by 1937 the questions that I have now presented to you probably will be minimized or eliminated. That is the only reason.

Mr. HANCOCK. What has the additional liability been worth, since the bank holiday?

Mr. O'CONNOR. It is practically 50 percent.

Mr. BROWN of Michigan. By taking the time between now and July 1, 1937, you will also give ample opportunity for working out some plan of advising the depositors in the bank of the change in liability, because as you have indicated before, there is a semblance of contractual liability there, and it does seem to me some regulations will have to be worked out to give depositors an opportunity to withdraw their accounts, or something of that kind; that is, if they do not care to leave their accounts in the banks subject to the double liability. It seems to me that time is a very valuable element.

Mr. O'CONNOR. Another thing that I think is important is that there is a gradual tendency in the small communities throughout the country to strengthen their banking system by merging the two, State banks and national banks, and that also is quite an important element in connection with this date in 1937.

Mr. CROSS. Take the proposal you referred to a while ago, that they should build up reserves equal to the capital stock. Time would be an element there also.

Mr. O'CONNOR. Yes.

Mr. HANCOCK. That is one of the fine things your office has been able to do in respect to the banking structure, in cooperation with the R. F. C.; is it not?

Mr. O'CONNOR. Yes; it is one of the best things that has been done in the way of strengthening the whole banking structure of the United States.

Mr. WILLIAMS. I understood you to say that you hoped at that time to retire a substantial part of the preferred stock that the R. F. C. has taken from the banks in order to build them up since the bank holiday.

Who determines when that stock shall be retired?

Mr. O'CONNOR. The bank makes an application, if it is a national bank, and it cannot be retired without the approval of the Comptroller's office, and, I believe, the Federal Reserve Board. I believe we are asking to have that lodged entirely in the Comptroller's office.

In other words, an application comes in for the retirement of stock, and that has to be passed upon by the Federal Reserve Board, and it is our opinion that this is the way it works out.

A bank desires to retire stock, so it makes an application and sets forth all its facts justifying it, and submits that to the Comptroller's office. We send it back to the national bank examiner in that district, and he makes a thorough investigation of it, and what information is available he submits to the Comptroller's office, and the Comptroller's office has all of the reports of the bank, and also the one that the examiner has just submitted, and he makes his recommendation, and upon that we act.

I believe under the present law after that has been done we must submit that to the Federal Reserve Board, and the Federal Reserve Board have to go through the same performance and certify that back to us, and I think that is a needless step.

Is not that the procedure, Mr. Awalt?

Mr. AWALT. That is correct as to common capital, but in reference to the preferred it is not necessary to certify it to the Federal Reserve Board.

Mr. WILLIAMS. I know of some fine banks that are in the Federal Deposit Insurance Corporation, and under the State laws they are not permitted to issue preferred stock, but they issue capital notes instead. How is that to be retired?

Mr. O'CONNOR. That is entirely between the R. F. C. and the State bank, my office having no jurisdiction over a State bank.

Mr. WILLIAMS. I understand that, but what about the F. D. I. C.?

Mr. O'CONNOR. We have no power over in the Federal Deposit Insurance Corporation to enforce anything. So that whether that preferred stock or capital notes or debentures that State banks have are retired is entirely between the R. F. C. and the State banks.

Mr. WILLIAMS. Do you know what procedure is followed?

Mr. O'CONNOR. Yes, sir. The State bank applies to the R. F. C. for the payment of its debentures or notes, or the preferred stock, and the R. F. C. usually refers that offer to the Federal Deposit Insurance Corporation, and then we make an examination of it, and if the bank should not retire those notes or debentures or stock, we so advise the R. F. C., that in our opinion they should not be retired. But they can ignore that; we have no authority to enforce it.

Mr. WILLIAMS. You have the same relation there that you do with reference to its issuance, practically, in the first place.

Mr. O'CONNOR. With reference to its issuance. Of course, but as to the Federal Deposit Insurance Corporation we have no authority.

Mr. WILLIAMS. But you do make an investigation and pass on the question as to whether or not they should come into the corporation.

Mr. O'CONNOR. Yes; that is true.

Mr. WILLIAMS. And you also make an investigation to see whether they ought to be retired, in order to keep them in the corporation, to determine whether or not it is advisable to retire the capital notes and still retain their soundness?

Mr. O'CONNOR. Yes.

Mr. WILLIAMS. You still make that investigation?

Mr. O'CONNOR. Yes.

Mr. WILLIAMS. You still really have the same relation that you did in the first place?

Mr. O'CONNOR. Yes; I would say that is correct, Congressman.

Mr. BROWN of Michigan. As to the provision for the examination of banks, in section 302 of the proposed law, I think it is, I favor that, I will say. I wonder upon what authority we have a right to prohibit people from engaging in the private banking business.

There has been some controversy between your office and the small private banks, particularly over the question of whom should pay the expense of the examination by the Comptroller's office.

Some of the smaller banks in my district have raised this question, and they think that Congress has no right to prevent them from engaging in the banking business. I would like to know what your view about that is.

Mr. O'CONNOR. Well, Mr. Congressman, you have opened up a very important and a very wide field by your question.

My own personal opinion as a lawyer is that we have no jurisdiction at all over a State institution, such as a private banking institution.

Mr. BROWN, of Michigan. Generally, I may say in Michigan—and I think it is quite common—private banks are not allowed to engage in the business, if they were not in business 2 or 3 years back, and the States are cooperating in an effort to stop that kind of banking business.

It just occurs to me that they are willing in my State now to submit to the examination, but they are not willing to pay for it. It seems to me, if we are endeavoring here to bring them under some reasonable regulation and force them to publish statements, it would be wiser to leave this addition you propose out and let the Federal Government bear the small expense that it would have to examine those banks.

Mr. O'CONNOR. I suggest this, Mr. Congressman, that in view of the policy of the office, which is that the Federal Government does not bear the expense of any examination, it would be unfair to have the Federal Government pay the expense of the examination of the private banks when the Federal Government does not bear the expense of the examination of any other bank.

Mr. BROWN of Michigan. If we do not I have the feeling they will tell us where to go.

The CHAIRMAN. There can be no fixed charge on the Government except by legislation authorizing an appropriation.

Mr. WILLIAMS. What do you mean by a private bank, Mr. Brown?

Mr. BROWN of Michigan. There are a lot of small banks in the smaller towns that simply consist of an individual who accepts deposits and makes loans, without a charter from the State. I know it has been felt by the Comptroller's office and by this committee that we ought to endeavor to at least regulate that business, and I think it should be regulated.

But I am fearful that the way we have it set up in this bill it will amount to nothing.

Mr. WILLIAMS. To what extent does that prevail throughout the country? I was under the impression that private banking, as described and as carried on in that manner, had been generally outlawed.

Mr. O'CONNOR. I would say generally; yes. But there is a great deal of it yet being done in the country. Texas has some of it, your State has some of it. Some of them have been in existence for a great many years.

My attention is called to the fact that 10 or 15 States have this problem.

The CHAIRMAN. They are all small, are they not?

Mr. O'CONNOR. No; there are some that are quite large.

Mr. FORD. Under that head, a private bank makes money, that is, it creates money the same as a State or a Federal Reserve bank, does it not?

Mr. O'CONNOR. Yes.

Mr. FORD. Then why has not Congress got some authority over them?

Mr. BROWN of Michigan. They do not create currency.

Mr. FORD. They create check money.

Mr. O'CONNOR. Congress has no jurisdiction over a strictly State bank. That is the answer to it.

Mr. FORD. I know it, and it has been so recognized. But a State bank which creates money, whether it is check money or currency, is actually usurping that power granted in the Constitution to Congress to coin money and regulate the value thereof, and I believe if the matter were put to a constitutional test it would be found that they were making money and would have to stop.

Mr. GIFFORD. I want to inquire particularly as to the liberalization of the act relating to loans made to executive officers.

The CHAIRMAN. Before you get to that, let me ask one question.

What would you say about a private bank, if you were authorized by law to conduct an examination, the same as with any other bank, except in the publication of the facts, which would be all you could do?

Mr. O'CONNOR. Mr. Chairman, that is our difficulty, and that is an administrative difficulty.

I believe that ought to receive serious consideration by this committee, and frankly, I would like to get the reactions of the committee on that problem from another angle.

At the present time, all we do under the law is to examine these private banks, and then the report on the examination is filed away.

Mr. WILLIAMS. Just why do you make the examination? What is the purpose of it?

Mr. O'CONNOR. You required us to do it.

Mr. WILLIAMS. That is, the private banks?

Mr. O'CONNOR. You required us to do it.

The CHAIRMAN. Mr. Williams and I did not.

Mr. HANCOCK. Strictly speaking, could a private bank confine its operations to intrastate business alone, and if so, how?

Mr. O'CONNOR. I doubt if it could; it would be very difficult.

Mr. HANCOCK. If that is true, it seems to me you could seriously consider the question of the Federal Government being able to regulate it.

Mr. O'CONNOR. Then you also have the question of denying it the mails.

Mr. HANCOCK. I know this question has been seriously considered lately with respect to the jurisdiction of the National Recovery Administration, in connection with the operations of an intrastate establishment.

But it seems to me every bank is engaged in interstate commerce to a certain degree, especially when it comes to the clearance of checks. I may be entirely wrong about that, and I would like to have your opinion.

Mr. O'CONNOR. That is why I am emphasizing the importance of giving this very serious consideration, because you have touched on it.

Mr. HANCOCK. I notice that the Deputy Comptroller, Mr. Awalt, is shaking his head. We might call him in and hear what his opinion is. I think it is a very important question.

Mr. O'CONNOR. I think it is. As to the administrative feature of it, under the present law, I do not know how we can reach it. We examine. They have the right to say, under the law, that they are being examined by a Federal agency, and we have no right to close them; we have no jurisdiction to liquidate them or tell them to put in more capital, or to eliminate assets. We just examine them, which might be construed as somewhat of an approval by the Federal Government, when we have no power to do anything else.

Mr. HANCOCK. Is it not a fact that the general counsel of the Federal Reserve Board has, within the past 2 or 3 years, filed an opinion to the effect that the Federal Government could force upon the country a unified system of banking?

Mr. O'CONNOR. The general counsel is here this morning and perhaps he can tell you about that when I get through.

Mr. BROWN of Michigan. Let us get straight on one thing. I think you have greater authority than merely to examine them. The statute says a bank shall publish its report. It seems to me that the publication is a very effective means of regulating a bank.

Mr. GIFFORD. I want to ask you one or two questions about the liberalization feature of the law in reference to loans made to executive officers of a bank.

As a Congressman, I represent 25 commercial banks in my district, and the men who run them are honest men, many of whom have been evidently penalized by this section, and I am glad to know that that penalty is being removed.

I want to ask you if you find some difficulty in making the actual determination as to who an executive officer might be.

Mr. O'CONNOR. Yes; we do.

Mr. GIFFORD. Is it not possible to define that word, so it will not be subjected to determination by the Federal Reserve Board?

Mr. O'CONNOR. We had in mind presenting an amendment in reference to that very problem, because I asked the Attorney General for a ruling on who was an executive officer, and the ruling was not clear, because he did not know himself.

Mr. GIFFORD. There has been a habit in recent years of adding to the number of directors of a bank; where they formerly had 5 they now, some of them, have 25 in many cases.

While you have liberalized the provision in reference to the amount of stock necessary to be held in order to be a director, some of those men are unable to get any loans from the banks, and that in a country district where there are no other banking facilities. Do you not think it is still a little harsh to say that a director cannot use his own bank? Was that provision made on the assumption that all these men are dishonest until they are proven honest?

I would like to ask you this question. Take, for instance, a corporation, 99 percent of the shares of which are owned by a director in a bank. Could that corporation borrow from that bank?

I am asking you if a corporation, 99 percent of whose stock is owned by a man who is a director in a bank, could borrow from that bank.

Mr. O'CONNOR. Yes.

Mr. GIFFORD. Take the case of a relative of a director of the bank who wants to borrow temporarily from the bank. But the bank says, This is not a very good loan; if the director will sign the note, then it will be all right. The director could sign the note, and after it had once gotten by another bank it would be a proper banking transaction under the law, as I understand it. I do not say these things have happened or would happen, but I know honest men are troubled about them. If they go to another bank they have to report to their own bank if they have been to some other bank. Would it be better to wipe that out? You probably remember the agitation a while ago for a provision to require all honest men to be penalized because the bank found a few business men whom they wanted as directors.

Mr. O'CONNOR. I am rather of the opinion that, generally speaking, officers of a bank should not be permitted to borrow from their bank because of the position that they occupy, really as trustees of the funds they are handling, that they should not be permitted to have those funds loaned to themselves. I think that general principle is sound.

Mr. GIFFORD. In the banks in my district the directors are business men of the community.

Mr. O'CONNOR. The directors are not prohibited from borrowing. They can borrow; because, just as you say, and properly so, they are called in from different avenues of business, down the street, being in other businesses entirely. They just sit on the board of directors once a month at a meeting, and their relationship is not as close to the handling of those funds as that of the executive officers.

Mr. GIFFORD. The directors when they vote on the approval of the granting of the loan, are not the executive officers of the bank.

Mr. O'CONNOR. I do not believe they are; that is my private opinion.

Mr. HANCOCK. Ask him who is an executive officer.

Mr. GIFFORD. I asked him that. They cannot determine it. A poor clerk may be acting as an executive officer one day in the execution of a note when that officer is away.

Mr. HANCOCK. That ought to be clarified.

Mr. GIFFORD. It has been a nuisance, and you know that any banker does not dare to complain. A banker involved in such a transaction may worry himself to death before he would say anything about it these days.

Mr. O'CONNOR. That has not been my experience, and I have met a lot of them. I have encouraged them not only to take up those matters, but also questions as to the examinations, and if there is any objection, I want them to feel that I want to encourage them and feel that they can reach the head of the department any day or any hour they want to.

Mr. GIFFORD. I know; your attitude has been splendid. Since I questioned you before in reference to the examination, I took a report of yours to a friend of mine and I quoted it with reference to that matter and I asked him to read it and report again to me, and he said when the reports come back they read pretty cold.

They are not very reassuring. I tried to comfort him with what you told me. [Laughter.] He was a good banker, in a good bank, and he said that the way you write letters in your Department, it is pretty cold.

Mr. FORD. You would not want him to write poems, would you?

Mr. GIFFORD. But what I am getting at is this, that in our country banks particularly our people are honest, and I think that you ought to make this plainer and far more liberal than you have. The president of the bank may be the only man that is doing much business in that community, and he cannot borrow in his own bank.

The CHAIRMAN. And there have been times when these bank officials would sacrifice every penny that they and their families had in order not to let those banks fail.

Mr. GIFFORD. You are absolutely right.

Mr. CROSS. What has been the experience of your office with respect to those officers breaking banks by borrowing from them? To what degree has that gone on in the past?

Mr. O'CONNOR. I could not give you any offhand opinion.

Mr. CROSS. I do not mean for you to be exact, but has it been extensive or not?

Mr. O'CONNOR. I can put it quite definitely in this way, that at the time this law was passed, prohibiting borrowing by executive officers of a bank, the executive officers of the national banks had borrowed $94,000,000 at that time directly, and about $45,000,000 indirectly.

Now, then, you passed this law and the executive officers have been making quite a strenuous effort to reduce that indebtedness, and I feel in very good faith, because before I suggested to this committee and to Congress that they should extend the time when these loans could be paid for a further period of several years, I did it because I thought that the record showed that the executive officers had been making, in this rather depressed period, a very fine effort to reduce their indebtedness to the banks to carry out the law of Congress, and they have paid about $35,000,000 of that in that period, and they have paid about 30 percent of the $45,000,000 that they were indirectly obligated on.

I think, frankly, that that is a very good showing, considering the times, and we are recommending here that when the loans are to be renewed, even for this period, that the officer asking for the renewal shall present the facts to his board of directors, don't you see, and then if he has done that, he has made reductions, they feel that it is in the interests of the bank that they should give him the additional period that we are asking in this law, which I think is reasonable.

Mr. GIFFORD. I hate always to have to agree, but it is good policy to cut the dog's tail off a little each day, and to make it easier for him to get used to it, and in order to relieve this situation, but you are going to cut him off eventually, and why can we not make a limitation of a small amount, so that in the small country banks, where there are no other facilities, it would not be so great a hardship? I know of one officer who said that he had to pay a loan to his own bank, and he went across the street and borrowed from the other bank; and now they have consolidated, and where is he? He is a perfectly fine character, and it is a good loan, and why force him into such foolish performances?

Mr. O'CONNOR. I think that you have made a very good point. I would be inclined personally to take this view of it, to limit an executive officer; and, secondly, provide that he would have to have the approval of the board of directors, for this reason, that he should not be in a position of having to go elsewhere, as you suggest.

Mr. GIFFORD. Certainly it should have the approval of the board of directors. I agree with that.

Mr. O'CONNOR. I think that those two things could receive the serious consideration of this committee.

Mr. GIFFORD. We should liberalize this this year. I can see the motive back of it, but why punish unnecessarily?

Mr. FORD. Supposing that an executive officer in a bank wants to make a loan, and he cannot get it from his own bank, and he goes to another bank. Does he have to report that loan to the board of directors?

Mr. CROSS. Oh, yes.

Mr. FORD. Would it not be sufficient if he reported it to the chairman of the board?

Mr. HANCOCK. The chairman of the board should not have information with respect to the borrowings of the other directors on that same board.

Mr. SPENCE. Did the opinion of the Attorney General define the duties that would constitute an executive officer?

Mr. O'CONNOR. No, sir.

Mr. SPENCE. What did the opinion say?

Mr. O'CONNOR. That he just did not know; and we did not know, so we asked him.

Mr. SPENCE. And you have not found anybody that knew?

Mr. O'CONNOR. We have not found anybody that knew.

Mr. GIFFORD. He acts as executive officer temporarily?

Mr. O'CONNOR. Yes.

Mr. GIFFORD. And you have to acknowledge that every act practically has to be a measure in itself.

Mr. O'CONNOR. That is the only way that you could judge as to whether or not his capacity was that of an executive officer, and as there is a criminal statute attached, it is a serious thing.

Mr. WILLIAMS. To what extent, in actual practice, are these loans made without the approval of the board? Is it pretty generally a practice that a loan of any size is made by any executive officer of a bank without the approval of the board?

Mr. O'Connor. I think that in the larger banks it is by a lending committee.

Mr. Williams. Ought it not to go finally to the board?

Mr. O'Connor. Oh, yes. I think that all good banks discuss with their boards their loans of any size.

Mr. Williams. After all, there is not much difference between that and a loan to a member of a board.

Mr. O'Connor. Not if they have all the knowledge.

Mr. Williams. I do not see much difference in making a loan to an executive officer of a bank, if it has to be approved by the board, and making a loan to one of the board themselves.

Mr. O'Connor. Well, I think that probably, Congressman, there is this distinction. I believe that the men who are running the bank always own practically most of the stock in the bank. They are the dominating officers in the bank, the officials of the bank. As the chairman has said, they have the greatest stake at interest in the bank, also. We must consider that.

But you cannot get away from the fact that they are more directly in charge of those funds, of the depositors' money, and of the loaning policy of the bank; and usually the directors accept their judgment because of their wider experience in banking, and so forth, and, frankly, I have always felt that that relationship of trust, of truster, and trustee, is such a close relationship that those officers should not be unlimited in borrowing from the bank.

Mr. Williams. Is not that board just as much a trustee as the executive—more so, for that matter, in the final disposition of funds?

Mr. O'Connor. In law, a director is also considered, in many respects, a trustee, when he accepts that position.

Mr. Brown of Michigan. What is the reason for requiring an executive officer of a bank to notify his own bank that he has borrowed money elsewhere? I cannot see any logic back of that rule. I agree thoroughly with your view regarding the other policy; but if he is not indebted to his own bank and cannot become indebted to it, why should he be required to inform his board of directors that he is borrowing somewhere else?

I know that the Comptroller does require it, because that is set forth in every bank report, except as to the borrowings from State banks, but I cannot see the necessity for that particular provision of law.

Mr. O'Connor. I will not take issue with you on that.

Mr. Brown of Michigan. Mr. Awalt?

Mr. Awalt. The following is the explanation, Congressman.

We have had any number of cases where officers have become very heavily involved by borrowing from other banks, and their own boards of directors, or their own chairman of the boards, did not know anything about that condition, and they would suddenly wake up to the fact that this man was heavily involved somewhere else; and there have been cases where he has let loans come into the bank from other places because he was borrowing there, and he will let the officers of another bank borrow in his bank; and the thought was that if he reported those loans to the board of directors of that bank, they would have knowledge all the time of what position he was in and what he was doing.

Mr. O'CONNOR. Mr. Chairman, may I take up some of the technical changes?

Mr. SISSON. Before we leave this question, I want to ask a question about this limitation upon the executive officers of the banks.

What I am thinking of, Mr. Comptroller, is that I have had some letters from three or four small banks, very small national banks, in instances where there is only one bank in a town, and a small town, and I assume that the amount of the loan would be rather small.

Could there not be some safeguard provided which would permit the making of a loan in such an instance, to carry out the purposes that we have in mind and you have in mind, requiring a few securities that would be satifactory?

Mr. O'CONNER. Yes; I do not see any objection. I think that that can be worked out, to be just a little more liberal, as the Congressman has said; to have just a little more liberal interpretation of that principle.

Mr. SISSON. You will remember, Mr. Chairman, that I spoke to you the other day about that. I do not know how many small banks have written to me about that and have even asked to appear before the committee.

I think that a limit could be made reasonably low and a reasonable requirement put in with regard to security that would satisfactorily meet that situation.

Mr. BROWN of Michigan. I am somewhat disturbed by what I hear back in Michigan, particularly in the metropolis, Detroit, about the matter of receiverships, and I would like to discuss that a little while with you.

Under the change which we propose in this law, the Federal Deposit Insurance Corporation will become the receiver of all closed national banks, by appointment from you.

Mr. O'CONNER. Yes; that is the section that I objected to.

Mr. BROWN of Michigan. But, as the bill is now presented, it is there contained?

Mr. O'CONNER. That is right.

Mr. BROWN of Michigan. Do you not think that it would be wise, whether we leave the power entirely with you, or whether we turn it over to the Federal Deposit Insurance Corporation, to provide some means of giving publicity to what is going on in the receiverships? I understand that at the present time it is impossible for a stockholder or a depositor to know what the expense of conducting a receivership under your department is.

Mr. O'CONNER. Of course, that is not correct, because we post up in the bank every quarter a statement showing the expense of that trust, the amount collected, and the exact financial condition of it.

What we try to protect our people against is this, and we have done it fairly well, with the consent of Congress, that whenever a bank fails, there is unfortunately a number of people who get together and if they could get all of the information that they wanted out of that bank, they would go out and try to buy these claims at 10 cents on the dollar, or 15 cents, or 20 cents, and to get those certificates away from those depositors, and that is one way in which we are trying to protect these people.

Out of every dollar that the Comptroller's office has collected. we have returned 93 cents to the depositors, and we have retained 7 cents to pay attorneys' fees, receivers' salaries, overhead, light, rent, and every other item of expense, and there is not a record like that in any receivership in the United States. However, in the two Detroit banks, our record was much better. Our cost up to December 31, 1934, in the First National Bank, Detroit, Mich., is only 1.989 cents for each dollar collected and in the Guardian National Bank of Commerce, Detroit, Mich., only 1.97 cents for each dollar collected, or less than 2 cents for each dollar collected. This means there was available for depositors and creditors 98 cents plus out of every dollar collected.

Mr. Brown of Michigan. That is undoubtedly true, and yet in a large bank, excessive attorneys' fees and excessive receivers' fees could be paid. You are not subject to the Federal courts in any way in fixing those fees.

Mr. O'Connor. No, sir.

Mr. Brown of Michigan. Are you willing to tell this committee now what is being paid, as receivers' fees, to the receivers for the First National and Union Guardian Banks in Detroit?

Mr. O'Connor. Yes. Mr. V. C. Schram was appointed receiver of the Guardian National Bank of Commerce, Detroit, Mich., on May 11, 1933, at a salary of $14,000 per year. The total assets at the date of suspension were $141,000,000.

Mr. C. O. Thomas was appointed receiver of the First National Bank, Detroit, Mich., on May 11, 1933, at a salary of $14,000 per year. The total assets of this bank were $485,000,000. Subsequently, Mr. Thomas of his own volition to take a position with a going bank, and I requested Mr. Schram to become receiver of both banks at a total salary for said banks of $16,000 per year. For the tremendous amount of assets involved and the many involved problems centered in these two banks, the compensation was and is small.

Mr. Brown of Michigan. What is being paid to the attorney in the case of the First National and Guardian National?

Mr. O'Connor. That is fixed by myself under a contract. Every attorney who becames an attorney for the Comptroller's office signs a contract. He cannot fix his own compensation. He cannot render a statement and stand in court upon it. He must submit that to my department, where his charges are gone over carefully by my staff, in connection with the work involved, and we allow what we believe is fair compensation, and if you will come to my office, because the other members of this committee are not interested, and I am not interested in any newspaper headlines, I will give you the amount.

Mr. Brown of Michigan. Do you not think that the depositors and the stockholders in those banks are entitled to know what those fees are?

Mr. O'Connor. They get them in their quarterly reports; they get the expenses of their liquidation.

Mr. Brown of Michigan. No one in Detroit knows what is being paid to the attorney in that case. As a matter of fact, the receivers for the Detroit Bankers Co. do not know.

Mr. O'Connor. I am happy to know that we have been able to keep our records in that condition.

Mr. BROWN of Michigan. I think that the stockholders who may be interested in the Guardian Bank, because the chances of their paying off are pretty good, and certainly the depositors in the First National, ought to know what the expense of this receivership is.

Mr. O'CONNOR. I just told you what I would do.

Mr. BROWN of Michigan. You say that you will tell it to me.

Mr. O'CONNOR. Yes, sir.

Mr. BROWN of Michigan. I do not want to know. I am neither a stockholder nor a depositor, and I have no personal interest in it at all, at least not directly, but I have been requested to raise the question of what is being paid at the present time to the attorneys who are there.

As you know, there is a great deal of criticism, whether justifiable or not, for bringing in an Ohio lawyer to take care of the interests of the banks in Detroit.

Mr. O'CONNOR. He just finished trying, in one month, 94 cases for my Department, and he won every single one of them.

Mr. BROWN of Michigan. I have no criticism of the conduct of his office, but I think that the interested parties are entitled to know what he is getting at the present time in the way of attorney's fees.

Mr. O'CONNOR. The failure of that bank occurred before March 4, 1933, as you know, but Mr. Awalt just tells me that there was not a firm available out there that was not connected in some way with that bank. Either they had to be sued, or they represented big stockholders or different interests.

Mr. BROWN of Michigan. I think a great deal of Mr. Awalt, as he knows.

Mr. O'CONNOR. He just passed that information on to me.

Mr. BROWN of Michigan. And I have highly praised him to the Michigan Bankers' Association. I will send him a copy of the speech. But I think that he is exaggerating a little when he says that there was no available firm of lawyers in Detroit that could have handled that case. I think that a Detroit lawyer could have been secured, at least a Michigan lawyer, who could have handled the situation.

But I do not want to be driven away from the main question. I want to know, as a Representative on this committee from the State of Michigan, what Mr. Marx has gotten.

Mr. O'CONNOR. I told you what I would do.

Mr. BROWN of Michigan. I want to know it in such a manner that it may be presented to the interested parties in the State of Michigan and in the city of Detroit, and I want it, Mr. O'Connor, for the protection of yourself, myself, and the present administration.

Mr. O'CONNOR. I will tell you. I will give it to you——

Mr. BROWN of Michigan. I can say to you that I was informed by a reliable business man in the city of Detroit no less than 2 weeks ago that Mr. Marx had presented, or would present, a bill for a quarter of a million dollars.

Now. I cannot believe that that can be so, and I would like to see it officially denied if it is not so, and if I can understand that this information that I received from you can be made known to the interested parties, that is all that I care about.

Mr. WOLCOTT. May I interrupt?

Mr. BROWN of Michigan. Let me get an answer to my question.

Mr. O'CONNOR. I will give you the information, Mr. Congressman, because as a Congressman I think that you are entitled to it, and you can then do whatever you think is in the interests of this Government.

I have had more trouble with your banks than with any other part of the United States. I have had more trouble with your people than with those in any other part of the United States, and after we paid the depositors in full, I got letters from those same depositors who got 100 cents on the dollar criticizing the administration, the receiver, and the plans that we had to put it into a holding company; and I wrote back and thanked them for their continued interest in an institution in which they did not have a dollar. [Laughter.]

Mr. BROWN of Michigan. Let me just add a word. I might say that I do not represent the city of Detroit. I am the only Michigan Representative of the majority party on this committee. I have continually upheld the administration of the Comptroller's office of the two big Detroit banks that have been closed, and I so stated to the Michigan Bankers' Association in a speech delivered before them last June in the presence of Judge Birdzell of the Federal Deposit Insurance Corporation, but I am not going to see my administration criticized in the manner that it has been back in Michigan in this matter, and that is why I asked the question.

Mr. O'CONNOR. I will give you that information, and it is up to you.

Mr. WOLCOTT. In that same connection, I addressed a letter to you yesterday, or the day before, asking for this same information. I do not want to make use of that information if you do not desire me to. I sent you this letter at the request of some people in my district who were interested in those banks.

Would it be perfectly agreeable to you, if I called on you with respect to this?

Mr. O'CONNOR. Yes; and I would particularly like to have you come over, so that we could go through the files and see what the situation is. One of the biggest jobs in the United States has been done in Detroit. We have saved several million dollars' worth of property.

Mr. BROWN of Michigan. I do not want to take up too much time, but one of my favorite subjects has been this subject of bank examinations, and I would like to discuss that with Mr. O'Connor when we have plenty of time, but I feel that we are needed on the floor.

The CHAIRMAN. I think that the situation is such that we should adjourn until 3 o'clock. Will you come back, then?

Mr. O'CONNOR. Yes.

(Thereupon, at 12:15 p. m., a recess was taken until 3 p. m.)

AFTER RECESS

Upon the expiration of the recess, the hearing was resumed.

The CHAIRMAN. All right, Mr. O'Connor; you may proceed.

STATEMENT OF J. F. T. O'CONNOR—Resumed

Mr. O'Connor. Mr. Chairman, I want to call the committee's attention to quite a large number of very small inaccuracies, or whatever you want to call them, in title 3 of the proposed Banking Act of 1935 and other technical amendments. For instance, just to illustrate what I have here, in section 310 (c), on page 57, line 10, substitute the letter (b) for the letter (c) in the parentheses, and so on down through.

I would like to put that in the record.

The Chairman. Yes, sir; leave it here.

Really, that might be reserved for executive session, but it is all right put it in the record.

(The changes proposed are as follows:)

Technical Amendments Which Should be Made in Title III of Proposed Banking Act of 1935 (H. R. 5357 and S. 1715)

Section 301. On page 51, line 14, after the words "shall not include" insert the following: "(except for the purposes of section 23A of the Federal Reserve Act, as amended) any corporation all of the stock of which is owned by the United States of America or".

(Note.—The words "except for the purposes of section 23A of the Federal Reserve Act, as amended," are added in order that the restrictions of section 23A upon loans by member banks to affiliates and holding company affiliates will continue to be applicable to accidental holding company affiliates. The other words added by the amendment are for the purpose of confirming the present interpretation of the law to the effect that the Reconstruction Finance Corporation and other corporations whose stock is owned by the United States are not included within the term "holding company affiliate.")

Sections 310 (a) and (b). Strike out all of subsections (a) and (b) of section 310 (p. 56, line 20 through p. 57, line 9) and insert in lieu thereof the following:

Sec. 310 (a). The first paragraph of section 5144 of the Revised Statutes, as amended (U. S. C., Supp. VII, title 12, sec. 61), is amended to read as follows:

"In all elections of directors, each shareholder shall have the right to vote the number of shares owned by him for as many persons as there are directors to be elected, or to cumulate such shares and give one candidate as many votes as the number of directors multiplied by the number of his shares shall equal, or to distribute them on the same principle among as many candidates as he shall think fit; and in deciding all other questions at meetings of shareholders, each shareholder shall be entitled to 1 vote on each share of stock held by him; except that (1) this shall not be construed as limiting the voting rights of holders of preferred stock under the terms and provisions of articles of association, or amendments thereto, adopted pursuant to the provisions of section 302 (a) of the Emergency Banking Act of March 9, 1933, as amended, (2) in the election of directors, shares of its own stock held by a national bank as sole trustee, whether registered in its own name as such trustee or in the name of its nominee, shall not be voted by the registered owner unless under the terms of the trust the manner in which such shares shall be voted may be determined by a donor or beneficiary of the trust and unless such donor or beneficiary actually directs how such shares shall be voted, (3) shares of its own stock held by a national bank and one or more persons as trustees may be voted by such other person or persons, as trustees, in the same manner as if he or they were the sole trustee, and (4) shares controlled by any holding company affiliate of a national bank shall not be voted unless such holding company affiliate shall have first obtained a voting permit as hereinafter provided, which permit is in force at the time such shares are voted, but such holding company affiliate may, without obtaining such permit, vote in favor of placing the association in voluntary liquidation or taking any other action pertaining to the voluntary liquidation of such association. Shareholders may vote by proxies duly authorized in writing; but no officer, clerk, teller, or bookkeeper of such bank shall act as proxy; and no shareholder whose liability is past due and unpaid shall be allowed to vote. Whenever shares of stock cannot be voted by reason of being held by the bank as sole trustee, such shares shall be excluded in determining whether matters voted upon by the shareholders were adopted by the requisite percentage of shares."

(NOTE.—Sections 310 (a) and (b) of the bill amend the first paragraph of section 5144 of the Revised Statutes. In order to add three additional amendments thereto, the paragraph has been rewritten as set forth above. The first of the new amendments is contained in the clause no. (1) in the rewritten section. This amendment is for the purpose of preserving the right which the Reconstruction Finance Corporation and other holders of preferred stock now have in certain cases to cast more than 1 vote on each share of preferred stock in the event of default. The new amendment contained in the clause no. (2) enables a national bank to vote shares of its own stock held by it as sole trustee in cases where the bank does not in fact control the manner in which the stock is voted. The third of the new amendments adds to the provision in clause no. (4) the following words at the end of such clause: "or taking any other action pertaining to the voluntary liquidation of such association." This amendment extends the authorization of a holding company affiliate to vote, without obtaining a voting permit, to place a national bank in voluntary liquidation so as to include the authority to vote in favor of taking any other action pertaining to such liquidation.)

Section 310 (c): On page 57, line 10, substitute the letter b for the letter c in the parentheses.

(NOTE.—Since section 310 (b) has been combined with section 310 (a), section 310 (c) now becomes section 310 (b).)

Section 317. On page 61, line 20, strike out the words "to read as follows" and substitute the words "by striking out the semicolon and everything preceding it and substituting the following."

On page 62, line 5, change the period to a semicolon.

(NOTE.—In drafting the proposed amendment to section 5243, the part following the semicolon, which provides for a penalty for violating this section, was inadvertently omitted; and the purpose of the above amendments is to preserve the penalty provision as it now exists in the law.)

Section 318: On page 62, line 7, substitute the word "three" for the word "two".

On page 62, after line 25, insert the following new paragraph:

"Section 6 of the Federal Reserve Act, as amended, is amended by striking out the last paragraph thereof."

(NOTE.—These amendments repeal the provisions of sections 5 and 6 of the Federal Reserve Act which require the board of directors of a Federal Reserve bank to execute a certificate to the Comptroller of the Currency showing an increase or decrease in the capital stock of the Federal Reserve bank. Inasmuch as every adjustment in Federal Reserve bank stock is approved by the Federal Reserve Board before the stock is issued or cancelled, the filing of such certificates with the Comptroller of the Currency is a useless formality involving duplication of work.)

Section 321: On page 64, line 1, strike out "and/or" and substitute therefor the word "or".

(NOTE.—This is merely for the purpose of improving the language of the section by eliminating the "and/or".)

Section 323 (a): On page 64, line 22, change the period to a colon and insert before the quotation marks the following: "*Provided, however*, That, within the meaning of the provisions of this section regarding the reserves required of member banks, the term 'time deposits' shall include 'savings deposits'".

(NOTE.—The provisions regarding reserves only require reserves against "demand deposits" and "time deposits", in view of the fact that the present statutory definition of time deposits includes savings accounts. The provisions regarding interest, however, make a distinction between time deposits and savings deposits in that they forbid the payment of any time deposit before maturity and forbid the waiver of any requirement of notice before payment of any savings deposit except as to all savings deposits having the same requirement. This amendment is for the purpose of making it clear that reserves are required against savings deposits as well as other time deposits.)

Section 323 (b): On page 65, line 3, strike out everything after the parenthesis to the end of line 5 and substitute therefor the following: "and cash items in process of collection payable immediately upon presentation in the United States, within the meaning of these terms as defined by the Federal Reserve Board."

(NOTE.—This would bring the language of the section into conformity with the language recommended by the Federal Reserve System's committee on reserves and would leave with the Federal Reserve Board the right to determine within limitations what items may be deducted from gross demand deposits for the purpose of determining the amount of net demand deposits on which reserves are required.)

Section 323 (d): On page 67, line 10, strike out the words "section 7 of"; in line 11, strike out the words "section 8 of"; in line 12, strike out the words "section 8 of".

(NOTE.—This is merely to eliminate any doubt as to the correctness of the statutory references.)

Section 325 (a): On page 68, line 11, insert a comma after the words "assistant examiner".

(NOTE.—This is to make clear that the restrictive clause, "who examines or has authority to examine such bank", applies to the words, "bank examiner", as well as to the words "assistant examiner".)

Section 325 (b): On page 69, line 3, insert before the word "section" the word "such".)

On page 69, line 9, strike out everything in line 9 and substitute therefor the following: "as to a national bank, the Federal Reserve Board as to a State member bank, or the Federal Deposit Insurance Corporation as to any other insured bank,".

(NOTE.—The first amendment is for the purpose of making clear that the section 22 referred to is section 22 of the Federal Reserve Act. The purpose of the second amendment is to make it clear that the consent of the appropriate supervisory authority is to be obtained with respect to the disclosure of information relating to national banks, State member banks, and other insured banks, and to eliminate doubt as to whose consent is necessary in a particular case.)

Section 326: On page 72, line 8, after the word "Government" strike out the comma and insert the following words: "or obligations fully guaranteed by the United States Government as to principal and interest,".

On page 72, line 25, strike out the period and the quotation marks and insert the following: "or to loans secured by, extensions of credit against, or purchases under repurchase agreement of, obligations of the United States Government or obligations fully guaranteed by the United States Government as to principal and interest."

(NOTE.—The first of the above amendments extends the exemption of affiliates engaged solely in holding certain obligations to include affiliates engaged solely in holding obligations guaranteed by the United States Government. The second amendment exempts from the limitations of the first paragraph of section 23A loans secured by, extensions of credit against, and purchases under repurchase agreement of United States Government obligations and obligations guaranteed by the United States Government and extends the exemption now contained in the second paragraph of section 23A to obligations guaranteed by the United States.)

Section 327: On page 73, line 4, substitute the word "established" for the word "establish".

(NOTE.—This merely corrects a typographical error.)

Mr. O'CONNOR. There are one or two of these technical changes that I want to call the attention of the committee to, for, really, they are more than technical. For instance, where we are giving the Reconstruction Finance Corporation the right to accumulate their funds, and so forth, which they should have where the Government has an interest in these banks, I wish to call attention especially to that, and then if you will be good enough to let whoever is drafting the bill finally get in touch with Mr. Awalt, we will be glad to assist you, if that meets with the approval of the committee.

Now, Mr. Chairman, the committee had considerable interest this morning in this question of loans to officers, and I think it might be worth while to give you what we have taken out of the Congressional Record of the House of a year ago.

For the purpose of indicating the intent of Congress with respect to this general question, quotations follow from the debates involving this particular section of the Banking Act of 1933.

In the House, when this section was under consideration, Mr. Bailey offered the following amendment:

After the word "officer" insert the words "or director" and add the same language at each point in section (g) after the word "officer" each time such word is used.

Mr. Bailey stated:

Mr. Chairman, this apparently is but a simple amendment but in fact it will have considerable to do with the final result of the operation of this bill. * * * One of the greatest troubles, one of the worst banking practices, has been loans made to people connected with banks. For that reason, I believe this Congress should add in this law a prohibition against borrowing by a director from a bank in which he is a director. * * * This amendment simply changes the wording of this section so as to include the directors of banks with executive officers.

The amendment was put to a vote and was rejected.

In the Senate, the following took place:

Mr. GLASS. Mr. President, may I inquire of the Senator from Oklahoma, for whose judgment I have the utmost respect, if the prohibition would apply to the directors of a bank or to the executive officers of a bank.

Mr. GORE. It was not my intention, when I conferred with the Comptroller, that it should apply to directors. I do not think that it does. I think it would apply to officers only.

Mr. GLASS. I think the Senator will concede that if it would apply to the directors of a bank, it would be very difficult to get any directors.

Mr. GORE. I think that is true and yet I think we ought to amend the existing law. * * * There ought to be a limit to the total borrowings which could be made by the directors of a bank. But that is not involved in this amendment, I would say.

Mr. GLASS. Usually the directors of a bank are among its largest depositors. If they were prohibited from patronizing the bank of which they were directors, it would be an extremely difficult thing to get any directors for the bank. * * * I would suggest that the Senator, if the language does not already imply what I mean, ought to use the term "executive" officers of the bank so that it may be understood that it does not apply to directors, because if it should there would be no directors.

Mr. GORE. I accept that suggestion from the Senator from Virginia.

Mr. GLASS. I would unhesitatingly say that the president of the bank, whether a salaried officer or not, would come within the definition of an "executive officer." The chairman of the board would be an executive officer and the cashier would be an executive officer. I do not think that a director is an executive officer, and I am perfectly certain that if it is intended to comprehend directors, we will not have any directors.

Mr. COUZENS. May I ask the Senator whether or not he would construe as executive officers the members of the executive committee who are only directors and yet pass upon loans?

Mr. GLASS. No. It is their business to pass upon loans and not to borrow. I would not regard them as executive officers. They simply pass upon loans. I think the executive officers of a bank are the salaried or nonsalaried officers, such as the president, cashier, and chairman of the board who is usually a higher-priced executive than the president himself. But what I desire to do is to exclude the directors of the bank from this requirement because as the Senator knows—he is a business man and knows better than I—usually the directors of a bank are among its largest depositors.

I thought that the committee might be interested in getting this reaction from both the House and the Senate, because it was raised by several Members here this morning.

Then, one of the members of the committee this morning also asked about the opinion of the Attorney General, and that is in three paragraphs, and I would like very much to give you that. [Reading:]

Upon the question who are executive officers, your Solicitor quotes from *Arkansas Amusement Corporation* v. *Kempner* (33 S. W. (2d) 42), to the effect that "an executive officer or employee is one who assumes command or control and directs the course of the business, or some part thereof, and who outlines the duties and directs the work of subordinate employees", as usually provided for in the articles of association, the bylaws or a resolution of the directors. The Supreme Court of Oklahoma, determining that "the cashier of a national bank clearly is an executive officer", derived assistance from statutory provisions concerning his duties (*First National Bank* v. *Mee*, 126 Okla. 265, 269).

I approve these general conclusions, but they permit no categorical answer to the question which you have submitted. "It is not the designation under which one is known but the nature of his duties which characterizes him as an 'executive officer'" (*Small* v. *Gibbs Press*, 225 N. Y. S. 141, 142).

It is the duty of the banks and of all officers who by any possibility might be affected to keep within the statute and to weigh carefully all the facts and circumstances (peculiarly within their possession) before acting. If cases arise in which it appears that the statute may have been violated, I shall be glad to consider the advisability of prosecutions; and I shall, of course, be glad to advise you in connection with any such cases wherein you may have some duty to perform. In either event, however, it would be necessary that I be fully informed as to the facts.

That bears out my statement this morning, that we did not know what an executive officer was.

That is all that I have to offer, unless there is something else.

The CHAIRMAN. Mr. Brown, you had some further questions.

Mr. BROWN of Michigan. I asked questions of the representatives of the Federal Deposit Insurance Corporation and of the Governor of the Federal Reserve Board on this matter, which to me is of considerable importance, the duplication of organizations that we have and propose in this bill for the examination of banks.

I want to say now that I think that the examining division of the Comptroller's office has been most efficient and has done an excellent work, particularly during this period of bank difficulties. I feel that the criticism made of my views on this thing is to a certain extent justified, and that there is not a great deal of duplication of effort.

In section II of the bill we have the first and possibly the second instance of where we provide for two Government examinations. Calling your attention, Mr. O'Connor, to that, the section provides in substance that the Federal Deposit Insurance Corporation may examine any national bank upon the written consent of the Comptroller.

Now, my purpose in bringing up this subject is to see if we cannot avoid duplication of organizations in the matter of the examination of banks. Going back a little into the history of the legislation, when the Federal Reserve System was set up, undoubtedly the idea of those who wrote the law was to provide for examination of Federal Reserve banks by the Comptroller's office, and the law still so provides, but by subsequent enactment, and, I think, Mr. Wyatt, that was about 1921?

Mr. WYATT. June 21, 1917.

Mr. Brown of Michigan. In 1917 the provisions of section 481 of the United States Code, insofar as they apply to the examination of Federal Reserve member banks, were eliminated, and I understand now that your office does not designate any examiners out of your staff for the purpose of examining member banks of the Federal Reserve System which are not national banks. Is that a fact?

Mr. O'Connor. Yes. There is one examination a year, as I understand it, made by the Federal Reserve Board of their member banks, because there are also the State examinations of those institutions.

Mr. Brown of Michigan. I think that in section 330 of the United States Code, the idea was that it was hoped that the State examinations would be sufficient to satisfy the Federal Reserve Board, but, as a matter of fact, we have a considerable force of examiners now under the Federal Reserve banks' jurisdiction, of the individual banks, I take it, rather than the Federal Reserve Board.

Now we are proposing to set up an examining division in the office of the Federal Deposit Insurance Corporation. Therefore, if we include the Reconstruction Finance Corporation, which likewise had a corps of examiners, and I think have some yet, we have four Government agencies at the present time examining banks, and if we eliminate the Reconstruction Finance Corporation, we have three, assuming that H. R. 5357 goes into effect as written.

Now, I recognize that it is going to be difficult to settle this problem before we settle the problem of the right of nonmember banks to the benefits of the insurance provisions of the law. I realize that that is a big problem that perhaps ought to be settled first, but I made this statement, having in mind the hope that the Treasury Department, the Federal Reserve Board, and the Federal Deposit Insurance Corporation can present some plan to this committee by which this duplication of organization can be eliminated.

It seems to me that a national bank ought not to have two governmental masters, that the regulations ought to come from one general head, one banking department.

I also recognize, Mr. O'Connor, that this is a statement, rather than a question, but I do want to ask you if you do not think that more efficient examination of our banks could be had if we consolidated the examining departments that we now have into one organization?

Mr. O'Connor. Mr. Congressman, you have made a very clear distinction that is not usually made by people who talk about the duplication of examinations by Federal agencies, of which there is no such thing, and you have made a very careful discrimination between those, and you are correct in that statement where you referred to different agencies making examinations rather than duplications of examinations.

There is no such thing in the Federal Government as the duplication of a single examination. In the first place, there is no examiner that enters a national bank except an examiner who is duly authorized to enter that bank on authority of the Comptroller of the Currency, with one exception. If the bank invites the Reconstruction Finance Corporation to become, so to speak, a partner in that bank, as it does when it makes an investment in the preferred stock of the bank, then the bank and the Reconstruction Finance Corporation, like any two contracting parties, sit down and make any agreement or arrangement that they want to make. I have nothing to do with it at that stage of the proceeding. The Reconstruction Finance Corporation can say, "We insist on having the examiner go in here once a year." That is all right if the bank agrees to it; I will not complain. The bank can invite in, as some of the larger do, certified public accountants and auditors, and they have the right to do that. I am merely making the point that at no time does anyone enter a national bank except the duly authorized representative of the Comptroller's office.

The national banking act provides that I must examine national banks at least twice a year, and oftener if found necessary. The law also provides that the Federal Reserve Board may examine banks in special instances, and, as I understand it, they examine their member banks once a year, and the State examiners examine them once or twice, or whatever the State law provides.

Now, that brings us to the third examination, and that is by the Federal Deposit Insurance Corporation. There is a question as to just how far that examination should go, and what the regulations should be with respect to it.

We must never forget that that is an insurance corporation, and we have insurance corporations in this country which are underwriting bonds against embezzlement, theft, robbery in State and national banks in this country, carrying a liability of many hundreds of millions of dollars, and when they pay a loss, as they had to do in about every month in the days past, there is no subrugation, there is no right. That is a complete, straight loss. Those insurance companies underwrite those losses, and have no recourse, so to speak, against the assets of the bank at all. They just write a check for $50,000, or $100,000, or whatever the amount may be, and they have no right of examination, or no right to go into any of these banks.

I am just pointing that out——

Mr. Brown of Michigan. You are not speaking of the Federal Deposit Insurance Corporation?

Mr. O'Connor. No; private companies that are insuring against embezzlement, robbery, and all of those things, that carry that without examination at all, and that have no subrugation rights.

Now, it is for the committee to determine just how far they want the Federal Deposit Insurance Corporation to go, or what attitude they should take toward these State banks, which are not chartered by the Federal Government, and with the States jealous of their supervision over them, and where their examinations are in good shape, properly so, and some of the States are very proud of their examining system.

I just want to point out, in passing, that the Federal Deposit Insurance Corporation has 16 percent of the total deposits outside of the Federal Reserve System. In other words, 84 percent of the deposits are in the Federal Reserve System. As to 16 percent of those outside of the System, your examinations would apply so far as the Federal Deposit Insurance Corporation is concerned.

Now, in the national banking system, as you know, we have about 5,467 national banks, about 3,000 less than we had at the peak, and the State member banks of the Federal Reserve System, as I remember, number about 976.

So we have three things in mind in discussing your problem, Mr. Congressman; that is, first, that the Comptroller's office is responsible for the examination of 5,467 national banks. You have given limited examination to the Federal Reserve Board over 976 banks, and the Federal Deposit Insurance Corporation has 16 percent of the total deposits, so that there is no duplication of examination, but there are, as you well pointed out, these agencies examining these particular banks; but that is a matter for this committee.

Mr. BROWN of Michigan. Well, of course, under section 11——

Mr. O'CONNOR. I wanted to discuss that, Mr. Congressman. You called attention to that, and here is the reason for it, and I think it is very important.

The Federal Deposit Insurance Corporation, if you pass the bill as it has been suggested to you, will give us the right to buy the assets of a bank before we have to close it. If it is a bank getting into bad shape, it is worth more as a going institution if we can go into that town and buy it or merge it, and the Federal Deposit Insurance Corporation in those instances may say, "We would like, if we should disagree with your examination, the right to go in there and make an examination in event we are going to buy the assets", and we say that we have no objection, that we will give them the written permission to go in there, and that is the only reason that that was put in the bill, Mr. Congressman. We could not write it in, but I am glad to clear that up.

Mr. BROWN of Michigan. That is the only reason for it?

Mr. O'CONNOR. That is the sole reason for it.

Mr. BROWN of Michigan. Well, do you think, Mr. Comptroller, that it would be advisable for the Government to give consideration to the question of turning over the matter of the examination of banks to one governmental agency?

Mr. O'CONNOR. I know, Mr. Congressman, that you will appreciate my embarrassment in answering that question. It is just not quite fair to me to answer it, because each of us would probably say, "Why yes; we will do it", so that I would rather leave it to the committee. Whatever you fellows do, we will do at our end of it.

Mr. BROWN of Michigan. I may say that while I think it is a big subject, and that we ought to do something about it, as I said before I do not think that we can really go into that until we have settled this other question.

Mr. O'CONNOR. That is right.

Mr. BROWN of Michigan. Of the nonmember State banks, and their relationship to the Federal Deposit Insurance Corporation. Just one other subject——

Mr. HANCOCK. May I ask one question here?

You say that under the law as it is now written, the office of the Comptroller is required to make two examinations a year?

Mr. O'CONNOR. That is right.

Mr. HANCOCK. Then you later said that under the law, the Federal Reserve Board may require an examination. Do they have to make an examination of member banks?

Mr. O'CONNOR. No.

Mr. BROWN of Michigan. That is not what he said. He said that in certain instances, if necessary, further examinations are made.

That is, of course, when banks are possibly in a shaky condition, something of that kind.

Is that the idea?

Mr. O'CONNOR. Yes, sir; as to national banks.

Mr. BROWN of Michigan. The Federal Reserve Board accepts your examination of national banks, and they examine State member banks of the Federal Reserve System?

Mr. O'CONNOR. That is right.

Mr. HANCOCK. Do they have to examine them?

Mr. O'CONNOR. No. In other words, they can take the State examination if they want to.

Mr. HANCOCK. What has been their policy?

Mr. O'CONNOR. I think that they have examined them pretty well around the country.

Mr. HANCOCK. At least once a year?

Mr. O'CONNOR. I think so.

Mr. Wyatt clears that up further, and I think it is very important; he says that their policy is to work with the State examiners of each State, and to send their men in with them when they find it necessary to make an examination.

Mr. BROWN of Michigan. Section 481 of the United States Code, which relates to the examination of member banks which are not national banks by the Federal Reserve bank, through examiners appointed by the Comptroller, is practically a dead letter now, is it not?

Mr. O'CONNOR. I do not appoint their examiners.

Mr. BROWN of Michigan. But under section 481 you can?

Mr. O'CONNOR. No. I can only appoint national bank examiners.

Mr. BROWN of Michigan. Now, the final subject that I have is the question of small branch banks. I am speaking for the smaller communities. A great many of them have been deprived of banking facilities by reason of the closing of something around one-half of the banks, and I have the feeling that to reorganize banks in towns of from 800 to 2,000 in population is not for the best interests of the business public.

In several States, and the State that I have in mind principally is the State of Wisconsin, provision has been made by State law for the establishment of what they call "receiving and paying stations", where a banking business consisting solely of the receiving of deposits and the paying out of the deposits is carried on in offices located in those small communities, controlled by banks in larger nearby towns. I think that the Wisconsin statute confines the establishment of such offices to the county in which the parent bank is located, and I think one State law provides a radius of 30 miles from the home office.

Most of those communities had banking service before the collapse, and it seems to me that we ought to liberalize the law to permit the establishment of stations of that character, with also the authority to receive applications for loans in such banks, both for the purpose of convenience to the public in those communities, and to prevent the establishment of a larger number of banks with very small capital.

The collapse that we had largely originated in smaller places, and if we could prevent the establishment of banks in those smaller places by giving such service, it seems to me that it would be a wise thing.

To show you how chary the legislature seemed to be, in the State of Wisconsin, they limited the effect of that law to a period of about 2 years from the time when it was enacted. It expires on July 1, 1935.

My attention has been called to a statute somewhat similar in the State of New Jersey.

I happen to live in a section of Michigan largely given over to the resort business, the island of Mackinac. It had a State bank. It was inadequately capitalized, and it fell down. That community has for 9 months of the year, a population of 450 people. For 3 months of the year, in the summertime, it has from 10,000 to 20,000 people. It ought to have banking facilities during that period of time, but you cannot set up a bank there that could make any money, but a branch bank of a national or State bank could be established there for that period, a branch office, and business could be conducted that would be reasonably satisfactory for the needs of the people.

I discussed it with the chairman of the committee, and I have discussed it with Mr. Goldsborough and some of the other members of the committee, and I would just like to have the reaction of your Department to such a set-up.

Mr. Goldsborough. You did not mean to indicate that I approved such a set-up?

Mr. Brown of Michigan. No; I did not say so. I said that I discussed it with you.

Mr. Dirksen. Do you have in mind a currency exchange, rather than a bank?

Mr. Brown of Michigan. A receiving and paying station.

Mr. Dirksen. There is nothing to prevent anybody from setting up a place to change money, and to do anything except to accept deposits.

Mr. Brown of Michigan. Yes; there is.

Mr. Dirksen. I mean so far as the ordinary medium of exchange in a community is concerned. I have been through some of those resort areas in your State, and this is purely a private notion on my part, but it seems to me that most any one of those chain stores in a little town can fit itself up with a little booth, with some wire netting, and make exchanges there, for you do not need any banking facilities in the ordinary accepted sense of a commercial bank.

Mr. Brown of Michigan. You would have to provide a place for a considerable amount of currency, which is somewhat dangerous, and the insurance companies will not accept a risk of that sort, and the Comptroller's office has, in the past, held that where such a business has a connection with another banking institution, it is engaging in branch banking.

Of course, I am very desirous of confining this to small communities, as I am not in favor of the spread of extensive branch banking.

Mr. Dirksen. May I observe, for the purpose of the record, in connection with your remark a moment ago, that so many of the failures took place in banks with small capitalization, that when the Bank of the United States failed, the losses probably exceeded those of every small bank that failed in the entire State of Illinois, outside of Cook County.

Numbers do not mean anything. You have to think of it in terms of the amount of losses.

Mr. HANCOCK. I hope that the Comptroller's answer to my good friend's question will not be construed as meaning that he thought that the small banks broke the large ones.

Mr. GOLDSBOROUGH. In the State of Maryland, only 2 country banks failed in 40 years up until the time of the failure of the Baltimore Trust Co., and the Union Trust Co. They were 2 banks which very largely held the reserves of the country banks, and, when those banks failed, the fact that the country banks had deposits in those banks made the country banks fail.

Mr. BROWN of Michigan. I am one of those who believes that the people of the country and the city, so far as honesty and integrity are concerned, are about equal, but I think that towns of from 800 to 1,000 in population are perhaps a little too small, unless the country is very well settled, to maintain a bank. Of course, if they can get adequate capitalization, it is all right, but in a sparsely settled country like northern Michigan it is quite essential that those smaller communities should have some banking service.

Mr. DIRKSEN. May I interpose at that point and say that 41 percent of all of the banks of the United States today are in towns of less than 1,000, and in your great rural States, such as Iowa, for example, 56 percent of all the banks are in towns of less than 1,000.

Mr. BROWN of Michigan. Of course, Iowa is a very well-settled State, but I am speaking of very large sections of the country, with an average county population of somewhere around 12,000 or 15,000 people, and having 2 or 3 towns of 800 to 1,200 population, with a county seat of 3,000 or 4,000 population, and I think that a county-seat bank in a county of that kind should be permitted to establish the receiving stations that I have mentioned.

That is the situation that I seek to improve.

Mr. HANCOCK. I want state at that point, if I may, that, of course, our whole system is so closely interrelated that what happens to one bank has its repercussions with other banks, but down my way, in North Carolina, and particularly in my own community, the serious losses which resulted to the depositors in the banks in the community were due largely to a policy on the part of several big banks in the northern cities which were correspondents of the small banks, which at that time seemed to have had the approval of the Comptroller's office, whereby examiners out of that office, from the information that has come to me, encouraged these small banks to build up secondary reserves by purchasing substandard bonds.

I think that ought to go into the record.

The CHAIRMAN. That went on all over the country.

Mr. HANCOCK. I know that in my own little bank in Oxford, N. C., upon the recommendation of an examiner, though he was not entirely to blame for it, for the officers had to assume their part of the responsibility, the bank purchased around half a million dollars of substandard bonds through the National City Co. of New York City.

Mr. FORD. What year?

Mr. HANCOCK. 1928 and 1929, and 65 percent of those investments turned out to be rotten.

The CHAIRMAN. Let me add right there that while that was going on, the officials of these big banks, and I can call their names, but I will not, for some of them are quite familiar——

Mr. Goldsborough (interrupting). Almost household words.

The Chairman (continuing). Some of them are familiar courthouse words now, and while that was going on, the officials of those banks were before our committee telling us that the trouble with the country was that we did not have any bankers, that the country bankers did not have intelligence enough to run a bank.

Of course, everybody knew that that was not so. New York replenishes its banking brains every year from the same towns and communities of the United States, and has done it from time immemorial.

Mr. Ford. May I make an observation?

The Chairman. Yes, sir.

Mr. Ford. Right along that line, is it not true that these country banks that bought these "submarginal" bonds, if you want to call them that, did so under this kind of pressure, that they had been let in by the bigger banks on juicy investments that they were able to hand out to their depositors in the past, and if they were to get their quota as it came along; and they were given a quota, and lots of them made a good profit, but if they were to continue to do that, they had to buy these bonds, and they were just as culpable in the matter as the big banks.

Mr. Hancock. I want to make a statement in the record to the effect that I do not believe that all of the large banks or institutions were culpable of practices of that kind.

Mr. Goldsborough. The National City Bank in New York kas the one that spread the misery in Maryland.

Mr. Hancock. The thing that we resented down there was the fact that some of these examiners went so far as to tell the officers of the bank that they could not keep good real-estate paper, because it is not liquid, but that they should take these funds and build up these secondary reserves and purchase these substandard bonds, and I think that the record will show that 85 percent of the real-estate paper in the bank at that time turned out to be good, but 65 percent of these bonds turned out to be bad.

Mr. Goldsborough. We all want to emphasize the fact that Mr. O'Connor was not Comptroller at that time.

Mr. Hancock. We want to make that clear, and I do not mean by my remarks to reflect upon any one public official. I am criticizing the policy that obtained at that time.

The Chairman. I do not want to say any mean things about anybody. All that I am trying to say is that they all made mistakes, and no one class had all of the wisdom and foresight.

Mr. Hancock. I think that it would be well to insert right here that one of the biggest officials connected with the Government at the present time, and a man who knows as much about banking as any other man, has recently said that these large bankers could very well afford to sit at the feet of the country bankers, like St. Paul did before the Messiah.

Mr. Dirksen. I assume that in their official capacity, the bank examiners are absolutely beyond all legal responsibility insofar as their supposedly official acts are concerned?

May I just illustrate that by citing the case of an examiner who examined two national banks in the same town, and then insisted that there be a joining of the two banks. The one was admittedly bad. The other doubtless would have weathered the storm.

I thought at the time that it was rather an arbitrary attitude on the part of the examiner to insist that the two banks be brought together, but apparently the boards of directors of both banks were persuaded to that course of action, and the sum and substance of the whole action when it was wound up resulted in the closing of the so-called "joint bank", or, rather, the residuary bank resulting from the joining of those two banks.

It was quite a long time after that that I went to the Federal Reserve, and to the examiner in charge, at Chicago, and we had any number of conferences, and, as I remember, the examiner who made this recommendation was there at the time. He was reproached by the president of the bank that did not weather the storm, but said nothing about it and admitted no liability or responsibility for the action.

I believe that if a thorough examination had been made, doubtless the responsibility could be laid upon the shoulders of the examiner, but I assume, however, that even if that could be done, or even if the liability and responsibility were admitted, despite that no legal action would lie for restitution either against him or against the United States in a suit in the Court of Claims, he being the duly authorized agent of the Government.

Is not that true?

Mr. O'Connor. You have to look at that from both sides. We can give you a good many illustrations in this country where our examiners have gone in and saved whole communities and whole cities from terrific financial crises by working together with the banks, but, as I understand it, men in public service are never to be rewarded, but always criticized.

So, when the examiner has by his action saved a great many communities, nothing is said, even though the contempt of silence rests upon him, but if he makes an error, even though at that time everybody thought that it was the right thing to do, and the bank officials do not have to do it unless they decide that it is the right thing to do—I say, if in 4 or 5 years that course of action is determined to have been in error, then you will look for some civil liability against him—is that the question?

Mr. Dirksen. Meaning that it is rather to be charged up as an error in judgment.

Mr. O'Connor. You can blame that not only on the examiner, but on all of the men who participated, because they did not have to do it. God knows that we are all human, but unless you can show incompetency, or dishonesty, or a personal interest on the part of the man doing it, for those are the things that I am most interested in finding out about these men who participate in these transactions, and if they are capable and honest, and if the examiner has done a fine job in many sections, I do not know that there is anything for me to do. It may be that in one case the officials and he agree that a course of action is all right, and 2 or 3 years later competition comes in and ruins one of the biggest banks in that city, which is something that nobody could foresee. Then, of course, the bank has to blame somebody, and they say that the examiner told them to do it.

Mr. Brown of Michigan. I do not think that an examiner is authorized to recommend the purchase of any given bond.

Mr. O'CONNOR. Never; and if you will give me the name of any that has, he will not be an examiner any more.

Mr. BROWN of Michigan. I would like to go back to my question, which seems to have aroused considerable controversy here, and a little display of heat.

The Wisconsin law provides substantially as follows: That, first, said receiving stations shall be established only in towns of 800 population or less, and they may not be established in any community which has an existing bank. The permit to establish that station is for 3 years only, and if any institution is organized for the purpose of taking care of the banking facilities of that community, the permit shall be immediately revoked.

Furthermore, it is provided that no such central bank should be permitted to maintain more than three such stations, nor shall they be maintained beyond the limits of the county, nor more than 35 miles from the central or main office. Their business is confined to the receiving and paying out of deposits, to the issuing of drafts and traveling checks, and to the cashing of checks and drafts.

Now, having in mind those limitations, do you think that it would be advisable to authorize the operation of such business offices for the reason, first, that it would tend to discourage the reopening of a multitude of small banks in small communities, and, second, that it will give a banking service in reasonably strong institutions to small communities?

Mr. O'CONNOR. Well, Mr. Chairman, I have not given that the consideration that it merits, but I think, as I rather closely followed your question, and also some of the argument, that, broadly speaking, there is something that we have to watch with great care in this country. We have got to encourage community life in the small centers of this Nation, and to do what we can to discourage the complete absorption by the large centers of a great percentage of our population, and my general thought is that anything that tends to encourage centralization of population, and wealth, and industry, is to be discouraged, and I think that we ought to always watch very carefully to do what we can toward saving these little communities and little towns, where I believe that the greatest happiness has come to families and to American life.

Now, back of your question, therefore, is this problem, which is one for serious consideration. If you establish a paying and receiving station you have discouraged, of course, in that community, even when the time comes for the establishment of an independent unit, a bank of its own, and I think that that has to be watched.

Relative to your other point, may I just make this suggestion, because it comes in with, and is applicable to, title I of the bill, that we ought to discourage, both on the part of the States and on the part of the Federal Government, the chartering of banks opposite every gasoline station in this country. Let us build and consolidate the banking structure, whether it be State or whether it be national, and if you give us the power that we are asking for in title I, we are going to have the right to determine the economic necessity as well as those other questions with reference to the necessity of a bank and with reference to the prevention of the destruction of other banks, for a State bank should no more be created to destroy another State bank than a national bank should be created to destroy another national bank.

We are trying to look at the problem from both angles in our office, and I would like to give you one illustration, although I would rather not name the State.

An application was made for permission to locate a branch in a certain town. Following our usual procedure, our examiners went to this town to make a complete check-up of the business, of the postal receipts, of the population, industry, of the surrounding communities that would be served, and of the banking facilities in the community.

We found that there was a State bank there owned by the people of that community, and that it had some $300,000 in deposits, and it was about 6 months old, and I declined to license a branch of the national bank in that town in competition with that little State bank that I thought was serving the community.

However, I am sorry to tell you that after I did that, these people also had a State bank, and they went to the State Department and they got a branch of the State bank and put it in competition with this other State bank in that little town. So I think that we have to work together.

I want to call your attention to this fact, that last year there were only 20 new national banks chartered in the United States. That had no reference to where we merged a bank, or where a new bank was set up under the assets of an old bank, but there were only 20 new national banks in all of the United States chartered last year.

Mr. Brown of Michigan. I think that I agree with your philosophy regarding the encouragement of small-town life. I think that there is a need for the kind of legislation that I have proposed here. There are a great many communities having a population from 800 to 1,000, and that, in my judgment, is about the right limitation as to size, where there is not sufficient capital for the establishment of a bank, and yet they ought to have some banking facilities, and I think that the only reason that we have not had them is because of the fear of a great many Congressmen that we would be encouraging the branch-banking business. But it does seem to me that we would be supplying a necessary need, and at the same time be doing what I know your Department thinks should be done, that is, the establishment of banks in communities that are two small to support them with sufficient and adequate capital.

As I said, it seems to me that there is need for that kind of legislation, with proper limitations, and I have read a good many of them to you, particularly having in mind that there would be no discouragement to the establishment of a bank if the community is big enough to need one.

Mr. Ford. Is there not another factor in there, Mr. Brown? We will take a community such as you describe. There are a great many objections that we hear to branch banking, but what is the objection, in a case of that kind, to a strong bank, with a number of branches, that is willing to put a branch in there and to possibly go along at cost for 2 or 3 years, on the assumption that the banking facilities being afforded to that community will develop the community and will bring it up to a point where it will be profitable to have a bank there.

Mr. O'CONNOR. Mr. Ford, you, of course, have stated the general principle underlying the licensing of a branch wherever we are permitted to do it, and those are the questions that are investigated and determined before we license the bank.

Mr. FORD. Surely, but it seems to me that if a bank with branches goes into a community and finds that there is not enough business there to warrant a bank, but if that institution is willing to go in there and probably for 3 or 4 years not make their expenses, or just barely make them, and by so doing they will attract enough business there ultimately to make a branch bank profitable, where a small bank could not afford it or the community could not afford to organize a bank, but the branch bank can give all of the facilities that a banking institution could afford such a town, they ought to be permitted to do it.

Mr. DIRKSEN. You advocate branch banking, I take it?

Mr. FORD. I do, yes. I think that it is a good thing.

Mr. DIRKSEN. I might just as well state my objection right now as well as any other time. I am absolutely and unequivocally averse to vesting the control of these little communities in some group or agency that may be 300, 400, or 500 miles away.

Mr. FORD. I do not think that I would let it go that far.

The CHAIRMAN. Who is going to say how far it should go?

Mr. DIRKSEN. That is right.

The CHAIRMAN. Branch banking is either a good thing or a bad thing. If it is a good thing, we ought to say so, and enact it into law, and let the Federal Reserve System adopt the best plan for the banking business. If it is vicious, and wrong, and monopolistic, un-American, and destructive of community life and financial independence, we ought to repudiate it, and never allow it to be extended in the United States.

We ought to take one position or the other. Of course I have a very definite view about it myself.

Mr. BROWN of Michigan. Of course, we have a good deal of branch banking now, Mr. Chairman.

The CHAIRMAN. I know we have, and we are going to have more. This is just a repetition of the discussion that we had a long time ago. Of course, we start with a county, and then as soon as the necessity arises, we extend it beyond the county line, and after a while the bridle is off. We have adopted the policy of letting the States decide whether branch banking is or is not a good thing for this country, because we have said that we will permit the establishment of branches by national banks in any State where the legislature of that State decides that branch banking is a good thing.

Of course, while I am not one of them, there are a great many people who take the position that there is not very much intelligence in the State legislatures with reference to banking or anything else, but we are on record as committing this country to whatever policy may be determined upon by the legislature of each particular State so far as branch banking is concerned.

I may be not without shame entirely for having taken that attitude, but it never represented a view of mine, or any desire of mine.

Mr. GOLDSBOROUGH. I want to say that I fought the thing, as far as I could, but I did succeed in keeping Maryland out of the picture, and that is as far as I could get.

Mr. CROSS. As far as I see, the branch bank in a little while would be such that every State could dictate to its legislature, through them, and it would spread all over the country, and everybody could dictate to Congress.

Mr. HANCOCK. If it were confined to county lines, there would be no serious objection to it, would there, Mr. Chairman?

The CHAIRMAN. There is no way in the world to confine it. That is the history of it. If it is a good thing it ought not to be confined.

Mr. GOLDSBOROUGH. I remember the time when there was only one bank in my county, and you had to take off your shoes and carry in in a petition to get a loan, not a promissory note but a petition.

Mr. FORD. You have to do that now.

Mr. GOLDSBOROUGH. Since we have seven banks there now we have a very much better situation, more democracy in our banking, and in our community life.

Mr. FORD. You paid a big price for it.

Mr. GOLDSBOROUGH. You cannot pay too much of a price for it.

Mr. FORD. Yes, you can.

Mr. BROWN of Michigan. Let me say, I have been in opposition to general branch banking, and I so voted heretofore, but I do not like an attitude which blindly shuts out consideration of a meritorious proposition. It will, I think, prevent the establishment of a number of under-capitalized State banks. The proposition puts proper limitations around the establishment of these so-called "receiving stations." It would be a good thing, and I am going to do my utmost to bring it about.

The CHAIRMAN. All right, gentlemen.

Mr. O'CONNOR. Mr. Chairman, could I ask that Mr. Wyatt, who represents the Federal Reserve, be added to the technical staff on the committee?

The CHAIRMAN. Yes, sir.

Mr. O'CONNOR. May I, with your permission, submit to you the corrections which I have suggested, so that it will aid the committee in your work?

The CHAIRMAN. Very well, we will be glad to have them.

Mr. O'CONNOR. The other day, when I was testifying on title I, I would like to mark in green, on the two main matters which I suggested, so that the committee would not confuse my opinion with the consensus of the committee who passed on it. I would like to have the privilege of calling your attention to that by marking it in color in title 1.

Mr. FORD. Mr. Chairman.

The CHAIRMAN. Yes, Mr. Ford.

Mr. FORD. Mr. Controller, two or three times the statement has been made that examiners borrowed money from banks that they were examining. Is there any case of that on record?

Mr. AWALT. It is a criminal offense.

Mr. FORD. Do you know any such cases?

Mr. O'CONNOR. I have heard that, Mr. Congressman, any my attention has not been called to a single instance where it has been done, because it is a criminal offense, and if I find it out, two things will happen, which I do not need to state. If anybody has got any information, I would like to have it.

Mr. FORD. I wanted to get that in the record.

Mr. O'CONNOR. I would like awfully well to have them, because two things will happen to the examiner.

Mr. DIRKSEN. Mr. O'Connor, do you not think any bank examiner who would do that, when it is so easy to do the same thing in a roundabout way should be treated in that manner?

Mr. O'CONNOR. I believe any man who evades the law indirectly is just as guilty as anyone who evades it directly.

Mr. HANCOCK. Mr. Chairman, I would like to ask the Controller a question. I was sick and absent, therefore, 2 or 3 days when title I was under discussion. I had it in mind at the time to ask Judge Burke his opinion. Under the present law the Controller of the Currency, as I understand it, cannot, during his term of office, have any financial connection with any institution. Is that correct?

Mr. O'CONNOR. I cannot own any stock in any bank.

Mr. HANCOCK. You are also limited by law from resuming financial connections, are you not?

Mr. O'CONNOR. Yes, sir; for 2 years—not mine, because I have not got any.

Mr. HANCOCK. A controller.

Mr. O'CONNOR. A controller; yes, sir.

Mr. HANCOCK. Are there such provisions in the law now with respect to directors and the Federal Deposit Insurance Corporation?

Mr. O'CONNOR. No, Mr. Congressman; there are not.

Mr. HANCOCK. In other words, a director of the Federal Deposit Insurance Corporation might be actively connected with banking institutions, which his staff had some supervision over?

Mr. O'CONNOR. Oh, yes.

Mr. HANCOCK. What is your opinion with respect to whether such a provision as that should also apply to the directors of the Federal Deposit Insurance Corporation?

Mr. O'CONNOR. Fundamentally, no man can serve two masters. You cannot serve both the Government and a private interest that you represent, in my estimation. I think it is a very good provision.

Mr. HANCOCK. Was that matter considered by the committee that framed this legislation?

Mr. O'CONNOR. No, sir. That is a very good rule, and I think so because it relieves a Controller of any temptation in making relationships during his office that he might expect in a year or 6 months or so, right after he left to go with some institution. I do not see any reason for challenging that set-up.

I think it would be unfair to apply that rule to the present two directors of the Federal Deposit Insurance Corporation.

Mr. HANCOCK. I was just fixing to ask you if that would not be the fair way to approach it, exempting them, but make it apply to all those affiliated with the Corporation hereafter?

Mr. O'CONNOR. It has never occurred to me and the matter has never been suggested until this moment, and I have never discussed it with anybody, and I am giving it to you as I think about it—but I think it would be unfair to apply it to the two members now in the Federal Deposit Insurance Corporation, because one of them, the Republican member, has been anxious to resign, and has banking interests, and we knew it, and everybody was advised of it. He did a fine job, and I am sure nothing he did was colored by his interests. It it not often you can get men of that kind. I want to say that for him.

Mr. HANCOCK. I am addressing myself to the principle.

Mr. O'CONNOR. That is what I am coming to. When these men were appointed by the President and confirmed by the Senate and accepted office, they did so under the law in operation at that time. I think it is an excellent suggestion and should apply, that is, in the matter of future appointments, divorcement entirely from any personal matter which they are called upon officially to determine for the Government.

Mr. HANCOCK. In fairness to them.

Mr. O'CONNOR. In fairness to the people of the country, the public, because the public official that they want should have just one interest and that is the interest of the people, and no personal interest, and whenever you mix the two, you are apt to get in trouble.

Mr. HANCOCK. That is all.

Mr. WILLIAMS. Did I understand you to say, Mr. Controller, that you are opposed to that provision of this bill which places the receivership in the hands of the Corporation?

Mr. O'CONNOR. Yes, sir.

Mr. WILLIAMS. The bill, as written, provides for a complete liquidation of the banks under the Corporation, does it not?

Mr. O'CONNOR. Yes, sir.

Mr. WILLIAMS. There would be no necessity of maintaining two sets or two organizations for that purpose, would there?

Mr. O'CONNOR. That is not correct. That is my objection.

Mr. WILLIAMS. If this law was passed, would there be any necessity for having two sets of liquidations?

Mr. O'CONNOR. I just want one.

Mr. WILLIAMS. Will this create two? That is what I am trying to get at.

Mr. O'CONNOR. Yes.

Mr. WILLIAMS. In what way?

Mr. O'CONNOR. Your law says that I shall appoint the Federal Deposit Insurance Corporation, this receiver.

Mr. WILLIAMS. Yes, sir.

Mr. O'CONNOR. Last year only one national bank failed in this country, in 1934; therefore, under the law, you have got to set up an entirely new insolvent division over in the Federal Deposit Insurance Corporation to take care of that one bank, exactly what I have got now, in 1,500 receiverships over in the Comptroller's office.

Secondly: The Federal Deposit Insurance Corporation insures only 42 percent of the deposits in national banks. The Comptroller is responsible for the other 58 percent.

Mr. WILLIAMS. Let us see right there. Do you mean that the Corporation would liquidate so far only as the insured assets are concerned, and then turn those remaining assets over to somebody else to finish the liquidation?

Mr. O'CONNOR. I do not want them in the picture at all.

Mr. WILLIAMS. Would that be the effect if this law were passed?

Mr. O'CONNOR. No.

Mr. WILLIAMS. In other words, there would be a complete and final liquidation?

Mr. O'CONNOR. By two organizations.

Mr. WILLIAMS. It would not affect future liquidations, would it?

Mr. O'CONNOR. Yes.

Mr. WILLIAMS. Does not the Comptroller pass out of the picture if this law is passed so far as the liquidation is concerned?

Mr. O'CONNOR. Pardon me, I will make it clear, Mr. Williams, if I can, again.

The law provides that the Comptroller shall appoint as a receiver the Federal Deposit Insurance Corporation.

Mr. WILLIAMS. I understand that. They take charge of it.

Mr. O'CONNOR. They take charge of it, and liquidate it, but I am responsible under the law, and must approve claims, compromises, and so forth, and all of this must come to my insolvent division, because ultimately they have got to pass on these things for me, and make all the reports. I appoint them receiver instead of an individual receiver, and they set up an insolvent division, and I have an insolvent division.

Mr. WILLIAMS. Why cannot they liquidate in full?

Mr. O'CONNOR. They can, if you want to set up two. They can.

Mr. WILLIAMS. I do not see any necessity for two under this law.

The CHAIRMAN. Of course, this was the reason which brought about this situation: It was for the purpose of continuing the banking service in the community and absorbing the shock of a failure to authorize the Federal Deposit Insurance Corporation, when the bank failed, to go in and continue to operate the bank for a period of 2 years, giving an opportunity during that time to the people in the community to set up a bank, if they saw fit, and, if not, at the end of 2 years liquidation would be complete. That was the way the legislation came about originally.

Mr. O'CONNOR. And, also, Mr. Chairman, was it not this: That in the original bill, because it temporarily was put on afterward, the original bill would have taken practically 100 percent of the insurance?

The CHAIRMAN. Yes; that is true, too. Under the plan contemplated, we had a plan or system in which deposits would all be insured up to $25,000, and 75 percent of the deposits between $25,000 and $50,000, and 50 percent above $50,000, which would, of course, insure a much larger amount of deposits than was provided for under the temporary plan, and which will be provided for under this legislation, if it is adopted, to supplant the permanent plan to which I referred.

Mr. O'CONNOR. Yes, sir.

The CHAIRMAN. That is quite true. Undoubtedly it may be said that we are drifting into a certain duplication of work and lost motion in the administration of the banks that are closed under this plan.

Mr. O'CONNOR. As I look at it, gentlemen, where they have insured, as I say, 42 percent of the deposits, and the Comptroller is still liable for the balance of it, say, taking that little national bank which failed last year, a receiver is appointed, and what does the Federal Deposit Insurance Corporation do? They may just pay the deposits up to $5,000, take an assignment of those claims, and pass them the same as one individual would do for any insolvent division, and as fast as they cleaned up in the usual way, with a fine record back 70 years—not mine, but all Comptrollers—they would go ahead and have one simple process. That is the only thing I am asking for.

The CHAIRMAN. Any further questions, gentlemen? If not, you may conclude, Mr. O'Connor, if you have anything further to say.

Mr. O'CONNOR. No, sir.

The CHAIRMAN. We want to thank you very much for your assistance and your very able statement.

Mr. O'CONNOR. I want to thank the committee for their courtesy.

(Whereupon, the committee adjourned until tomorrow, Wednesday, Mar. 27, 1935, at 10:30 a. m.)

BANKING ACT OF 1935

WEDNESDAY, MARCH 27, 1935

House of Representatives,
Committee on Banking and Currency,
Washington, D. C.

The committee met at 10:30 a. m., Hon. Henry B. Steagall (chairman) presiding.

The Chairman. We have with us this morning Prof. Walter E. Spahr, of New York University.

I assume, you desire to address yourself to title II of the bill, and that you desire to make a general statement. So you may proceed without interruption, and after you finish your general statement members of the committee will desire to discuss the proposal with you.

Will you state to the reporter your connection, and your experience?

STATEMENT OF DR. WALTER E. SPAHR, PROFESSOR OF ECONOMICS, NEW YORK UNIVERSITY, NEW YORK

Dr. Spahr. My name is Walter E. Spahr; I am professor of economics at New York University, and my subject includes money and banking.

Do you desire to have my previous connections?

The Chairman. Yes.

Dr. Spahr. I have been a professor since 1913 in various institutions in this country. First I was at the Pacific College, at Newberg, Oreg; then at the University of Wisconsin, at Madison, Wis.; then at Muskingum College, New Concord, Ohio; then at Dartmouth, Columbia, Princeton, and New York University.

My field of specialization is money and banking, Mr. Chairman.

I desire to make some comments on title II of the banking bill of 1935.

There are no circumstances calling for legislation dealing with the fundamentals of the Federal Reserve System at this time. Legislation of this type should not be undertaken until after a commission of competent experts has made a thorough study of the money and banking problems of this country, and, on the basis of adequate evidence and after careful deliberations, has drafted a plan which offers real promise of providing this country with appropriate and workable money and banking systems. Both systems have suffered sad mutilation in recent years, and what is needed now is careful and deliberate overhauling and reconstruction, rather than further mutilation and distortion such as will result if title II of this bill is passed under the administrative whip and in the atmosphere of tense emotionalism now prevailing with respect to our money and banking problems.

It is very important that there be no legislation at this time beyond that necessary to correct technical difficulties, or to remove crude inconsistencies, in existing laws. And even this type of legislation should be undertaken only upon the recommendation of the Federal Reserve Board and in strict accord with specific proposals drafted by the Board.

The Senate and House Committees on Banking and Currency, I think, could perform no better service at this time, with respect to the proposed legislation, as embodied in this bill—S. 1715, and H. R. 5357—than to refuse to vote it out of committee and to substitute in its stead a bill of technical corrections embodying the recommendations of the Federal Reserve Board on specific difficulties.

At the same time a joint resolution should be prepared providing for the creation of a national commission on money and banking to gather evidence on our money and banking problems, and to draft bills to provide this country with the proper type of money and banking systems. This commission, I believe, should be composed of leading money and banking authorities of this country. Its membership might well be composed of, first, those members of the Senate and House Committees on Banking and Currency who have devoted years to the study of problems of money and banking; second, the most outstanding and experienced professors of money and banking in our leading universities, men whose repuation, intellectual integrity, and capacity are beyond question; third, outstanding bankers who are men of experience, maturity, and social vision; and, fourth, other students of money and banking, drawn from other fields of activity, if they are recognized as thorough students of money and banking problems.

The delay in legislation which would result from the adoption of such a program is eminently desirable. Money and banking mechanisms are probably the most delicate and, at the same time, most vital of all instrumentalities in our economic system; and it is for this reason that hasty and ill-conceived legislation in such a field is very unwise and is to be deplored. In its stead there should be substituted legislation growing out of careful deliberation by our most competent experts.

Title II of the banking bill of 1935 is particularly dangerous, when viewed in its entirety, because it is a manifestation of the unsound philosophy held by some officials in this administration regarding the causal relationships existing between the supply of currency, on the one hand, and prices, recovery, and prosperity on the other. Involved in this false philosophy are also misconceptions as to, first, the proper functions of central banking systems, especially with respect to the appropriate relation between a nation's central banking system and governmental financing; second, the appropriate functions and powers of the central banks with respect to the control of the money and credit supply; and, above all, third, the appropriate relationship between the Government, acting in its supervisory capacity, and a properly constituted central banking system.

These false notions and misconceptions show themselves clearly in those sections of title II which will enable the party in power—I mean any party in power, of course—to control completely the personnel of the Federal Reserve Board. They are revealed in those sections which will enable this politically controlled board to attempt to put into effect the theories of money and credit control held by many of those in power. They are seen in those sections of the bill which will enable the Government to force the central and commercial banking structure to aid the Government in carrying out the fiscal policies regardless of their wisdom, to give Government credit an artificially high rating, and to use the banking system and people's savings without their approval and regardless of the effect upon commerce, agriculture, and industry.

In short, nearly all the fundamental conceptions regarding the appropriate functions, the methods of operation of a well-conceived central banking system, and the proper relation of the Government to such a banking system, are false, are contrary to the most outstanding lessons learned from central-banking experiences, are dangerous, and are almost certain to lead to great trouble in the future.

The following analysis of the various sections of title II of the banking bill of 1935 support the accuracy of the preceding general observations.

Section 201 (a) provides the means by which the board of directors of each Federal Reserve bank will be brought under the control of the Federal Reserve Board, which, in turn, will be politically controlled. This means of control is found in the fact that the governor and vice governor of each Federal Reserve bank can be appointed only with the approval of the Federal Reserve Board.

The governor and vice governor can come from any district. In this manner the Federal Reserve Board can inflict any outsider on a Federal Reserve bank as governor or vice governor.

Since the governor and vice governor are approved by the Federal Reserve Board, and since 2 other class C directors, other than the governor, are representatives of the Federal Reserve Board, the Government can have 4 representatives as against the present 3, since the vice governor need not be appointed a class C director. Why the office of deputy chairman is not combined with that of the vice governor is not clear unless the purpose be to enlarge the number of Government representatives on the board of directors of each Federal Reserve bank.

It is to be noticed also that "all other officers and employees of the bank shall be directly responsible" to the governor of the board of directors. This gives him the powers of a czar; and through him the politically controlled Federal Reserve Board can reach directly and arbitrarily down to every employee in every Federal Reserve bank.

This means, of course, that the political authorities can reach any employee they please. In this manner every employee of every Federal Reserve bank will lose his independence and become, like the Federal Reserve Board, an unwilling vassal of the political party in power. Classes A and B directors will carry no weight under such a system, since the governor of each Federal Reserve bank is given this authority and is a Government agent.

Today the elected governors of the Federal Reserve banks are chairmen of the executive committees and, in this manner, they have increased their powers as against the Chairman-Federal Reserve agent. This bill makes a Government agent chairman of the executive committee, and thus the Government worms its way into the direct operation of each Federal Reserve bank.

The slightest reflection upon such a proposed arrangement should convince one that all activities of each Federal Reserve bank can be brought under the absolute control and domination of the political party in power. These governors and vice governors may be as arbitrary as they please, so long as they satisfy the politically controlled Federal Reserve Board. In this manner the political party in power can lay its rough hands on the Federal Reserve banks, which the Government does not own, but which are owned by the member banks that, in turn, are owned largely by private individuals.

Such an arrangement provides conclusive evidence of the intent of the present party in power to extend its political tentacles over the banking system. In this case, it is attempting to lay hold of one of the most delicate and most vital agencies of our economic system, an agency that must be free from such domination if our economic system and our people in it are to maintain any appreciable amount of their traditional freedom.

When a nation's banking system passes into control of the political party in power, the freedom of a people can speedily disappear. And certainly there is no reason to expect that better banking can or will result from any such proposal as this one in section 201 (e) of this bill.

It is to be observed that one of the class C directors shall be appointed deputy chairman of the board of directors, and that the vice governor may be appointed a class C director. It is because of this word "may" that the Federal Reserve Board may have four representatives on the board of directors of each Federal Reserve bank.

The duties now performed by the Federal Reserve agent "shall be performed by such person as the Federal Reserve Board shall designate." This provides the Reserve Board with another representative at each Federal Reserve bank. In this manner it can have five agents there at the Federal Reserve bank.

The last paragraph of section 201 (a), on page 40, lines 17 to 22, permitting the present incumbents of the boards of directors to serve out their terms would seem to require a modification of the parts of the bill which provide that this section shall be effective 90 days after enactment.

Section 202 is one of those coaxing, half-hearted measures by which attempts are made to persuade nonmember banks to become members of the Federal Reserve System. Our statute books are cluttered up with these conciliatory provisions in law. That particular provision merely lowers still further the capital requirements of banks which may enter the System. At present the capital requirements are too low. And, if it is believed that nonmember banks should be members of the System, then the Federal Reserve Act should be amended so as to provide that all banks should, after a certain date, be members of the System. If the capital requirements of some of the banks are too small, such banks should be made branches of larger member banks. But all legislation of this type probably should be left until a competent money and banking commission makes its report.

Section 203 provides the means by which the Federal Reserve Board is to be made into a politically controlled and dominated agent of the President. Lines 1 to 3, page 42, of section 203 (1), are probably the worst, if not the most subtle, in the bill. They provide that the President "shall choose persons well qualified by education or experience or both to participate in the formulation of national economic and monetary policies." It will be noticed that these members of the Board are to be qualified to participate in the formulation of national economic policies as well as monetary policies. Does this mean that they are to participate in the formulation of national economic policies? If this sentence means what it appears to mean, then this Board will become a part of the planning bureaucracy of the Government, and the Federal Reserve System can become, and can be made to become, the financial agent of the Government in carrying out its planning policies. It can be made an engine of oppression, rather than a neutral agent to finance commerce, agriculture, and industry.

This section of the bill is either subtle or stupid. In any case, it is dangerous. It reveals how far removed its drafters are, in their notions of how to constitute a central bank board, from those who would profit from experience.

Section 203 (2) provides a means by which Mr. Hamlin may retire at once and Messrs. Miller and James in 1936, thus removing from the board in a very short time, even if more arbitrary methods are not used, its three most experienced members. If this provision is to be enacted into law, it would seem that it should be so amended that all ex-members of the board would become ex-officio members of some advisory body, such as the Federal Advisory Council, in order that the benefits of the knowledge and experience of such men are not lost to the younger members of the board. Such an arrangement could be an effective factor in developing fine traditions in central banking.

Lines 17 to 25, on page 42, are awkward and confusing. Lines 17 to 22 say literally that "each member of the board so retired from active service who shall have served for at least 5 years shall receive, during the remainder of his life, retirement pay in an amount equal to the annual salary paid" now. Thus he would receive a total pension of $12,000 for the rest of his life, if you take those words literally. How much will he be paid the first year of retirement? Or is he to be paid $12,000 in a lump sum? This sentence probably was intended to give the retired members, who have reached 70 years of age and who have served 5 or more years, an annual pension based upon the years served, the yearly amount to be determined by the number of years served multiplied by $1,000, but the bill certainly does not make this point clear.

According to the first proviso, a person who has served, say, 8 years, will receive $8,000 per year, and if he lives 3 years thereafter he will receive $24,000 in a pension, whereas lines 17 to 22 preceding the proviso would give him only $12,000, regardless of how long he lived.

This proviso also omits the 5-year minimum, and, il line 25, the word "served" apparently should be inserted after the third word "year." The entire section is badly muddled, and it should be rewritten and made to say what the authors intended that it should say.

Nor is the second proviso, on page 43, clear or sufficiently specific in its meaning. Furthermore, it is to be noted that, according to section 203 (3), every governor appointed and removed will come in for this pension if he is 65 years of age, since he shall be deemed to have served the full term for which he was appointed, even though he may have served only 1 month or even 1 day. What a great opportunity this provides a President to place his friends on a fine pension for life. In 30 days he could give 30 of his friends who had reached 65 years of age a $12,000 pension for life. In 4 years he could develop a large pension list, all to be paid by the Federal Reserve banks. The vice governor apparently can have his term of service terminated by the President without the benefit of it being deemed that he served his full term. It would appear that no member of the board could afford to accept the office of vice governor.

This section 203 (3) reveals clearly the method by which a President can change the board's personnel within the space of a week to suit his particular wishes. It would be difficult to conceive of a more dangerous provision written into any central banking law. It reveals beyond the shadow of a doubt the purpose of the authors of this measure. They propose to convert the Federal Reserve System into a political instrumentality of the party in power. This section of the bill reflects clearly the authors' motives and concepts regarding central banking. It shows that they stand ready to destroy our Federal Reserve System, which we have tried to evolve into a useful system over a period of 20 years.

If every other section of the bill and of the Federal Reserve Act, as amended by the bill, were perfect, the system still could be destroyed and the bill still would be dangerous. Considering the dangers in sections 201 and 203 of this bill, the possibilities of dangers in the other sections of title II are accentuated. For this reason there are many today who oppose other sections of title II principally because they would be administered by a politically controlled Federal Reserve Board.

The answer to this proposed amendment to the Federal Reserve Act is that it must not be permitted to pass. The lessons of central banking teach that the farther the central banking administrative authorities are removed from political domination the better for the country concerned. The independence of the Federal Reserve Board should be strengthened, and not weakened, and our Federal Reserve System will not be what it should be until this is accomplished.

There are various ways in which this can be done. Indeed, there are so many devices available that it would be absurd for any one to insist that he can suggest the best one. My contention is that our lessons have taught us that our Federal Reserve Board has not been sufficiently independent of the Government and that the method of nomination and final selection should be so changed as to remove the board as far from political control as is the United States Supreme Court.

Of course, every central banking system must come under the control of the Government in some degree; but this control should be exercised through the passage of the proper organic act providing for the proper type of banking system and administrative boards, after which the Government should leave the system to operate, free from partisan politics, within the limits of the organic act. As the Board is reconstituted and strengthened after a careful study of the problem by our best experts, I should like to see the Secretary of the Treasury removed from the Board, though I think he should be a nonvoting auditor or participant in the Board's discussions; and I should like to see the office and functions of the Comptroller of the Currency absorbed by the Board.

Everything that any central banking system can be expected to accomplish can be written into the organic Banking Act, and thereafter the administration of the system should be left to independent, nonpolitical administrative bodies.

Section 204 appears to be free from criticism.

Section 205, creating a new type of Federal open-market committee, might have many virtues if the Federal Reserve Board were a properly constituted independent board. But considering how the Board is to politically controlled, this section of the bill merely provides additional means by which the Government can extend its powers over the activities of the Federal Reserve banks.

Government financing, in the final analysis, should be looked upon as an intrusion into, and a disturbing factor in, the fields of private finance. And if a well-ordered central banking system performs its functions properly, there will be many times in which it must and should go into the open money markets to combat the effects of Government financing.

It is not the function of a central banking system to give Government credit a higher rating than it would otherwise have in the open money markets to which non-Government borrowers and lenders must go. It is the function of all commercial banks to give borrowers the exact rating to which they are entitled, and it is the function of these banks and the central banking authorities to give Government borrowers exactly the same type of credit rating. To assume that Government credit should be given an artificially high value by a central banking system is to assume that it is the function of a central banking system to inflate the currency.

This section 205 recognizes no such principle of central banking and opens the way by which the banking system can be made to absorb Government securities on terms satisfactory to the Government and is, for this reason, unsound in principle. The section provides the means by which the Government can compel open-market operations to suit its particular notions and purposes regardless of the needs of commerce, agriculture, and industry, and regardless of any principles of sound central banking.

All five members of the Federal Open-Market Committee are to be Government agents. The fact that two of the members are to be selected from the governors of the Reserve banks by the governors does not change this fact, since all these governors will be Government agents.

This Committee is also given the power to make recommendations to the Federal Reserve Board from time to time regarding the discount rates of the Federal Reserve banks. It may be presumed that giving this Committee this power has no particular significance unless it be assumed that the Reserve Board exercises the power of prescribing discount rates for the Reserve banks. It would seem preferable that the present method of having rates initiated by the respective Reserve banks, subject to the approval of the Board, is preferable. But if the Reserve Board were properly constituted and independent of political influences, I should advocate that the Board be given the power not only to review discount rates but to institute the rates when a Federal Reserve bank is clearly running counter to sound national banking policies.

Section 206, which opens the way for discounting any commercial, agricultural, or industrial paper and for advances secured by any sound assets of such member bank, seems to be tacked on to the preceding parts of section 13 of the Federal Reserve Act without any regard to how it affects the preceding paragraphs of that section. It would appear that most of the preceding paragraphs are nullified. Just what the law is would be difficult to determine. It reveals a hasty and careless type of bill drafting.

It is doubtful whether, under the best type of central banking system, such a provision can be defended. It would seem that, under such a system, this wide-open provision should be reserved for emergencies.

Under a politically dominated system of central banking, as provided by this bill, section 206 provides the means by which the Reserve Board can admit to the portfolios of the Federal Reserve banks any kind of paper, regardless of its illiquidity, and fix the maturity of the paper at any distant date it chooses to adopt.

Since it is not the function of a central banking system to accept illiquid paper, the proper restrictions against such acceptance should be set up. Wise exceptions to meet emergencies can be provided, and the proper penalties and handicaps attached, so that emergency transactions will not become the normal ones. This section, as it stands, is unsound and unwise.

Section 207 provides the means by which the Federal Reserve banks can be compelled to absorb Government securities regardless of maturities. In this manner the Reserve banks can become gorged with Government securities with long maturities and consequently can become very illiquid. Under a properly organized Federal Reserve Board, and with other appropriate administrative machinery, such a provision might be safe enough, but under the system provided in this bill, this section adds another dangerous provision to the Federal Reserve Act.

Section 208 (1) provides the means by which Federal Reserve notes are to be issued against the general assets of the Reserve banks in addition to requiring the 40-percent reserve of gold certificates. If these assets were liquid, this provision would not be objectionable, but since the way it is opened by this bill for admitting all kinds of illiquid paper to the portfolios of the Reserve banks, this section provides the way for converting illiquid assets into legal tender paper money. This, of course, means inflation and is unsound in principle.

Then the question may be raised as to why the Federal Reserve notes are made legal tender for all purposes? When a money is legal tender for all purposes it can be used to pay all debts, public and private. This means, literally, that these notes could be used for lawful reserves and could be used to redeem any other currency. It is intended that these notes shall be "lawful money" for reserve purposes, thus converting a liability into an asset? This, of course, is not a rational procedure, and yet this is what lines 22 and 23, page 46, really provides.

In contradiction to this, lines 24 and 25 exclude these notes from the lawful money for reserve purposes in the Federal Reserve banks. This means that the Federal Reserve notes are not permitted to fulfill their functions as full legal tender money. The two provisions are in direct conflict and should make clear the fact that it is irrational to attempt to make Federal Reserve notes full legal tender.

This section provides, in lines 8 to 10, page 47, that the Treasurer of the United States shall cancel and retire unfit Federal Reserve notes coming from a source other than a Federal Reserve bank, but it does not specify or provide any fund for such retirement. The last sentence of this section lines 10 to 12, page 48, provides that notes unfit for circulation shall be returned by the Reserve banks to the Comptroller of the Currency for cancelation and destruction. Just why both the Comptroller of the Currency and the Treasurer of the United States should be involved in canceling unfit notes is not clear.

This bill abolishes the 5-percent redemption fund with the Treasurer of the United States. It also permits one Reserve bank to pay out the reserve notes of other Reserve banks without any penalties, and in this manner one of the factors forcing a retirement of these notes is removed. There appears to be no good reason for repealing either of these prevailing requirements. The omission of the latter requirement merely serves as another means of inviting a looser type of banking. The omission of the redemption fund may be due to careless bill drafting.

Section 208 (2) reveals careless bill drafting in the fact that care was not taken to strike out all words which should be deleted. For example, in the second line following the last deletion the words "or subtreasuries" appear again and are permitted to stand by this repealing section.

Section 209, which permits the Federal Reserve Board to change the Reserve requirements of the Reserve banks as they see fit, is a dangerous weapon to put into the hands of a politically dominated board. The preceding sections of title II of this bill, combined with this section, make it possible for the Board to pack Government securities and other illiquid paper into the portfolios of the Federal Reserve banks until the surplus reserves are exhausted, and then the reserve requirements of member banks can be reduced, thus permitting the Board and banks to proceed with their inflation without let or hindrance. The provision that the reserve requirements of these banks may be changed "in order to prevent injurious credit expansion or contraction" is merely the statement of a pious hope. It would mean nothing in the hands of a politically controlled Reserve Board.

Section 210, stipulating conditions under which member banks may lend on real estate, flies in the face of all practical experience with such loans by commercial banks. Provisions for such loans should be restricted, not enlarged. To raise the percentage of the value of the property for lending purposes from 50 to 60 percent is unwise, as is the 75-percent provision for loans amortized within 20 years. To raise the limits of such investments from 50 to 60 percent of time and savings deposits and from 25 to 100 percent of the bank's capital and surplus is a brazen denial of the value of our past experience with such loans.

In lines 13 to 18, page 50, in which the real-estate loans are insured by the provisions of title II of the National Housing Act, all restrictions appear to be removed. The answer to this is that in sound commercial banking the question of the proper type of loans is not one of insurance and ultimate liquidation but one of maturity and immediate liquidity.

Thus, we see in title II of this bill a multitude of illustrations of the dangerous banking philosophy held by the advocates and authors of this bill. It must not be passed. It is extremely dangerous. The conceptions underlying it run counter to the best opinion on central banking. If I may say it in that connection, I would like to remind the committee that 66 of the leading monetary economists of this country, men with established reputations on that particular thing, came out in support of this contention I have just made. I should be glad to submit a list of those people to the committee.

The bill is another, and probably the most brazen, daring, and dangerous attempt of politically minded planners to increase their destructive and devastating hold on business enterprise in this country. There are no sound defenses that can be afforded for the bill. If its advocates insist that they have the welfare of this Nation at heart, let them prove it by submitting the bill to a national commission of experts for analysis.

The authors of this bill would not risk such an analysis. What they want is not better central banking but more political banking by political planners. They want to build a bigger and better political machine. Professions to the contrary are annihilated by the sections of this bill which provide the means desired by the political planners, and which are in harmony with the immature and muddled notions regarding principles of money and banking expressed from time to time by the chief backers of the type of proposals incorporated in this bill.

No person well trained in the principles of money and banking could examine the theories set forth by the present Acting Governor of the Federal Reserve Board in his testimony before the Senate Committee on Finance in its investigation of economic problems in February 1933 without perceiving the dangers in this bill and the dangers in having our Federal Reserve System, as amended by this bill, administered by an official holding such views.

In that testimony is revealed a confusion of understanding as to the causal relationship between the currency supply and a sound business recovery; in that testimony the currency is held responsible for conditions which can only be traced properly to the maladjustments created by the World War. There is advocacy of the issue of fiat money, of currency manipulation to raise the price level artificially, and it is even proposed that money be given away. There is revealed an appalling lack of understanding of the nature and consequences of inflation; more inflation is recommended to correct the difficulties caused by inflation. Economic planning is an obsession, and it is proposed to use the Federal Reserve System to make such planning effective.

These disconcerting facts are pointed out, and I say it with all deference, because this bill apparently has been drafted for the purpose of providing the means by which these unsound and dangerous theories of money and of banking and of currency control can be thrust upon the people of this Nation.

If this bill becomes law I believe only the most providential good luck will prevent this country from suffering severely as a consequence.

I firmly believe the best interests of the people of this Nation are served by registering as vigorously as one can his protests and objections to this bill. It was born in secrecy. No known or trusted experts attended its birth. Its parentage is hidden largely in obscurity and anonymity, although the Acting Governor of the Reserve Board, in his Columbus, Ohio, address of February 12, 1935, speaks of what "we propose" in referring to the changes provided by the bill. It reveals traits found in political and economic concepts alien to the best principles of central banking and the best traditions of the people of this Nation. It is an un-American, unsound creation that must never be permitted to find its way into our statute books.

The CHAIRMAN. Professor Spahr, are you satisfied with the existing economic status in the United States?

Dr. SPAHR. Not at all.

The CHAIRMAN. What would you do about it?

Dr. SPAHR. I would give business a chance to recover.

The CHAIRMAN. What you mean is you would do nothing?

Dr. SPAHR. That is not what I mean at all.

The CHAIRMAN. If I understand you, if things were left alone, that would be the case.

Dr. SPAHR. I said I would give business a chance to recover, and would make every effort to cooperate with business, and would endeavor to remove all difficulties in the way of recovery. I would give them every encouragement to believe that we are going to give them a sound currency at the earliest possible date, and not obstruct recovery.

The CHAIRMAN. Do you think that that assurance would cure the situation?

Dr. SPAHR. I would not say it would cure it, but it would be an encouraging factor.

The CHAIRMAN. Doctor Spahr, I think most of us in this country are interested in a cure, and not an encouragement or promotion of helpful tendencies. Some of us would like to find a cure, if we could. Have you anything to suggest as a cure?

Dr. SPAHR. Yes; I think so.

The CHAIRMAN. Besides giving business a chance, something that would cure the situation?

Dr. SPAHR. I think, so far as money and banking are concerned, that the cures that can be exercised are the cures to use when business is expanding; but when you come down into a depression, there is very little the Government can do except to cooperate and encourage business to come back. Very little can be done through money and banking. They are merely the machinery to provide an easy means of exchange for business, and the sooner it is done the better it works.

The CHAIRMAN. What I am directing your attention to is this: You are an expert in this field of study, and we are practical laymen, representing the public, and in an official capacity are looking for practical results. We want to find some way out, if you can tell us how to find it.

Maybe you are right, if you say that is what should be done, that we should do nothing; that may be true.

I am only undertaking to get your view.

If you say we should do nothing, I am glad to have your opinion about it. But if there is anything we could do I would like to have you point that out.

Dr. SPAHR. I would not say we should do nothing. I say if we would do all we could to help business it would encourage business men tremendously. I want to emphasize this point, that there seems to be some confusion in the banking bill regarding the relationship between currency supply and recovery.

The CHAIRMAN. You have pointed that out in your preliminary statement.

Dr. SPAHR. Not as well as I would like to, because it would answer your question.

The CHAIRMAN. If it is an answer to my question, you may proceed.

Dr. SPAHR. There are two types of rising prices. There may be a sound rising in prices that accompanies a sound recovery, and that is what people want. Then there may be a rise in prices due to inflation. That is an artificial forcing up of prices. If you have a sound rise in prices, the initial emphasis for that comes from the business men, it comes from the producers who have been able to reduce their inventory cost to a sufficient point to enable them to resume operations at a profit. Any Government program that enables the producers to put themselves in that position would generate recovery.

I say there are two types of rising prices. The causal factors in each case are different. The reactions of the country to these two types of rising prices are different, and the economic consequences are different. A sound rise in prices which accompanies a sound recovery is generated by business men; it can not be generated in any other way.

An unsound rise in prices is generated by currency inflation, and the reactions of the country are different. The reaction of people to a rise in prices generated by currency inflation is one of fear, and the effect of depreciating the currency is in harmony with that response.

The reaction to a sound rise in prices is one of confidence. There is increased production and increased purchasing power.

The CHAIRMAN. How would you bring about this sound method of improvement?

Dr. SPAHR. I would do everything I could to restore our credit to the sound basis it had before 1933. That would be one of the first things I would do.

Then I would remove every obstacle from the paths of business men, such as the National Recovery Administration and any other restrictive provision. I would do as much as possible to protect the public, such as was done through the Securities Act. I would do everything possible to make it easy for business men to start again.

The CHAIRMAN. But you have never yet told us a single thing we should do affirmatively. You are now telling us some things that should be undone.

Dr. SPAHR. I think they would be affirmative acts.

The CHAIRMAN. Insofar as they repeal this particular legislation and terminate the endeavors to which you have referred.

Let me ask you this question. What had we done toward inflation, or toward establishing an unsound currency, prior to these inflationary developments from which you are suffering?

Dr. SPAHR. We had inflation without doing anything to provide for it. We had a system that permitted it, because the Federal Reserve Board and the bankers were all permitting it. It was the general psychology in this country which encouraged it through installment buying.

The CHAIRMAN. I am asking you what there was in our banking or money system prior to these developments that was unsound, or that looked toward inflation. You say these evils result from inflation. Had we had inflation before this trouble came?

Dr. SPAHR. I would say the system, as constructed, permitted inflation prior to 1929, you say, as I understand it, that that is your date.

The CHAIRMAN. Your contention would be that we can never cure the situation, or safeguard ourselves against a repetition so long as there is a possibility of inflation, or the power to inflate the currency in the United States. If that is so, then would you say our situation is forever hopeless?

Dr. SPAHR. I think you will always have inflation. That depends on how you define deflation. I would define inflation as being the result from an expansion of purchasing power being in the country, not backed by sufficient resources or commodities to liquidate it.

The CHAIRMAN. What would you have done to make the development of such a situation impossible in the future?

Dr. SPAHR. You will never make it impossible; you can not do it, so long as any individual can make a loan to another one.

The CHAIRMAN. Your contention is that these things are going to happen.

Dr. SPAHR. No. You made a very extreme statement. You said "cure." I say you cannot cure it.

The CHAIRMAN. Assuming that providence will lift us out of it; what can we do to prevent a repetition?

Dr. SPAHR. I would just build a strong, sound money system and banking system in this country.

The CHAIRMAN. Will you tell us how to do it? That is what we want to know. Tell us what sort of a system you would have.

Dr. SPAHR. I would have an intelligent, strongly administered central banking system; I mean a Federal Reserve Board; an intelligence, strong Federal Reserve Board operating under an act that it simplified, and drafted in accordance with the best principles of central banking, as we know them today.

Then I would encourage recovery, remove all the obstacles in the country that are holding business men back, and then let recovery start, before you start to put on your controls.

The CHAIRMAN. We were taught for a long time that the gold standard would protect us and give us a sound money system in this country, and we attempted to establish it and maintain it for that purpose. We did maintain it, and while maintaining it, everything collapsed.

Dr. SPAHR. But the gold standard was not to blame for what happened.

The CHAIRMAN. I am not talking about who is to blame. I am talking about preventives. The gold standard did not prevent it.

Dr. SPAHR. No.

The CHAIRMAN. So that will not save us.

Dr. SPAHR. No; you are quite right about that.

A gold standard means that your currency is brought back to something that is universally acceptable, and creates confidence and facilitates exchange. Business thrives with a sound, and not an unsound currency.

Of course, the gold standard cannot cause prosperity to return, but it is a facilitating factor.

The CHAIRMAN. If we ever get out of this situation, we would like to prevent its recurrence, and the gold standard cannot be relied upon, because we tried it and it failed.

Dr. SPAHR. It will not cause it, but it will facilitate it.

The CHAIRMAN. We had the Federal Reserve System in operation, which you might say was universally approved by bankers and experts, and which we thought was the last word in banking, and which we thought would answer. But that did not save us.

Dr. SPAHR. No. I do not think anything could have saved us in this country, no matter what you had.

The CHAIRMAN. As I understand you, you are arguing right now that we should leave things as they are.

Dr. SPAHR. No.

The CHAIRMAN. Then what would you have us do about it?

Dr. SPAHR. I have said that we should have a strong, sound money and banking system, because that will facilitate recovery.

Mr. CROSS. Tell us what that is, in specific terms.

Mr. HANCOCK. Doctor, Spahr, are you not in effect advising us to go back to the Hoover financial policies?

Dr. SPAHR. Not at all.

The CHAIRMAN. You mean really to stay on the Hoover policy. We have not been off of the Hoover policy so far as the banking system is concerned.

This administration inherited a banking system which had been universally approved by bankers and everybody else in the United States, and which everybody told us was all right. That is so, is it not?

Dr. SPAHR. I think I can answer your question.

The CHAIRMAN. Is not that true?

Dr. SPAHR. No; I do not think so.

The CHAIRMAN. I thought it was.

We all remember quite well when we were passing the Federal Reserve Act that Congress was deluged with the same arguments, the same contentions and the same views as to that proposal that you are offering us now with respect to the actions proposed in this legislation.

Dr. SPAHR. No.

The CHAIRMAN. But later I had always understood that the passage of the Federal Reserve Act and its operation had met with general approval.

Dr. SPAHR. May I answer you in this way: You can take any type of banking system that there was in existence in the world; they all went down in the crash. Regardless of the form of government, or of the type of banking system, they all went down.

That ought to prove something. It proves that the banking systems were carried down in a great catastrophe which resulted from the conditions which resulted from the war. To blame the gold standard for what happened then is irrational.

The CHAIRMAN. I am not saying the gold standard was responsible for it. What I am attempting to say is that the gold standard did not prevent it.

Dr. SPAHR. Certainly not; everybody ought to know that. You cannot get any monetary system of that sort that can prevent it.

The CHAIRMAN. That comes back to what you said.

Dr. SPAHR. You can do some very unwise things.

The CHAIRMAN. Nobody will dispute that.

Dr. SPAHR. A lot of it was caused by the fact that we had already suffered from the preceding inflation. A sound medium of exchange is just a facility in doing business. It will not cure anything or prevent anything.

The CHAIRMAN. Every man attempts to tag that description, tie that on to his particular plan; whatever he favors as a currency system, he calls "sound."

We had a man before this committee the other morning whose views are as far from yours as the East is from the West, and he insisted his plan was "sound."

Dr. SPAHR. I think this committee thinks perhaps that I am a Republican; but I am not advocating a return to the Hoover policy.

The CHAIRMAN. If you will find us a remedy, God bless your soul, we are for you, and you may advocate anything or anybody you may wish politically, if you will tell us how to remedy this situation that distresses us.

Dr. SPAHR. I was going to answer some questions that were asked. I am interested only in presenting the economics of this proposition, and I think your practical experience will tell you whether what I say is true or false. I am glad to be put on the carpet.

Mr. GOLDSBOROUGH. Nobody is putting you on the carpet.

The CHAIRMAN. Insofar as the party you voted for is concerned, that does not make any difference; we do not know how to remedy the situation. The fact that you voted with us, if you did, in 1932, does not in any way assure us that you know just what we ought to do.

Dr. SPAHR. I think all of us know from experience, sometimes, what is the best thing to do. I feel that the best thing you can do in the way of a stimulant is to remove the barriers to recovery, because I will say that we have learned from experience that the best thing is to let nature take its course.

We have a tremendously complex economic system that is made up of individuals, each pursuing the object of his own interests, to get, all of them and individualy, all they can, trying to make a living. That is the object, to get an income, and you must bear in mind that the impetus that generates recovery comes from the operations of people working and trying to make a living.

They will not do those things if there is any doubt about the currency, and if there are any undue obstructions placed in their path, and the thing to do is to make it as easy for them as possible to make it possible for them to reduce their cost inventories and market their goods.

The CHAIRMAN. How would you do that?

Dr. SPAHR. I would say that the National Recovery Administration has deterred us. That ought to have been removed, That is an obstruction which adds to the difficulties.

The CHAIRMAN. Would you say, when a man has pneumonia, and the doctor comes in and gives him 10 drops of medicine or gives him 20 or 25 drops when he should have given him 10, that that is the cause of the pneumonia?

Dr. SPAHR. No; I would not say that.

The CHAIRMAN. You are just pointing out the trouble, but you are not telling us what we can do.

Dr. SPAHR. I am telling you that the principal thing is simply to remove every obstruction you can take away, to aid business recovery.

Mr. REILLY. Name some of the obstructions.

Dr. SPAHR. The National Recovery Administration is an obstruction.

Mr. REILLY. What are the barriers that you think ought to be removed?

Dr. SPAHR. Anything we have that increases the cost that the business man has to pay.

Mr. REILLY. Do you want us to go back to where we were when we adopted the National Recovery Administration?

Dr. SPAHR. So far as business men are concerned, yes, I do.

Mr. REILLY. Do you expect us to entertain the desire that we will go back there and stay there, and accept that situation?

Dr. SPAHR. Yes, I think it would be a very good thing. But you will not cure that situation because that did not cause the depression.

Mr. SISSON. Is there anything that has been done since the 4th of March 1933, of which you approve?

Dr. SPAHR. Yes; I approve a good many things.

Mr. SISSON. You do not approve of the Securities Act, do you?

Dr. SPAHR. Yes, sir; I do, although I think it is too stringent.

Mr. FORD. Do you think that the Reconstruction Finance Corporation was a constructive measure, and that it has done any good?

Dr. SPAHR. Yes; I think so.

The CHAIRMAN. Let me ask you about the Reconstruction Finance Corporation. I had a little bit to do with that, under a former administration, with which I cooperated, and I accept my share of the responsibility for what was done.

Do you think that the principle of the Reconstruction Finance Corporation legislation was sound?

Dr. SPAHR. Yes; Ido, in general.

The CHAIRMAN. Do you believe that the Government should open the Treasury doors and supply funds for private business and private institutions, when they find themselves in need of it?

Dr. SPAHR. That is a pretty broad statement. I could not go that far. I would put it this way, that when you get into a panic, people become panic-stricken. They toss properties overboard in an irrational manner, much more so during a period of depression than during boom times. Therefore I think that the Government can do a tremendous amount of good by stepping in and holding up properties until they get their bearings.

The CHAIRMAN. There is no doubt in the world that many of us could become great financial leaders for a while, if you would give us access to the Treasury of the United States.

Dr. SPAHR. But I understand——

The CHAIRMAN (continuing). But I am going to state for this record now that I think a resort to the Treasury of the United States for the support of private business does not represent leadership. It represents a breaking down of leadership.

Dr. SPAHR. I understood that nearly all of the funds loaned are being paid back.

The CHAIRMAN. That is not the question.

Dr. SPAHR. That is why I made my statement.

The CHAIRMAN. That involves a question only of who is a good judge of securities.

Dr. SPAHR. I implied that.

The CHAIRMAN. But the business leaders of this country upon whom we had to rely, to some extent at least, for guidance and counsel stood by and watched the developments that brought us to the brink of ruin, and then, after the greater part of the country had already been destroyed, those remaining had power enough and influence enough, and were smart enough to come to Washington and persuade us to open the doors of the Treasury of the United States to save them and enable them to carry on.

You say that is right, as I understand you.

Dr. SPAHR. I think so, but I am using your own words. If they made loans that could be repaid, I cannot see why it is not sound.

Mr. GOLDSBOROUGH. The loans will be repaid only by boosting the market, and the little fellow who failed before that time had no such help.

Dr. SPAHR. That is true.

Mr. GOLDSBOROUGH. But the railroads, the insurance companies, and the banks will gain by it.

Dr. SPAHR. I would say that it proves its soundness if all borrowers repaid.

Mr. GOLDSBOROUGH. In the judgment of many people, the country would be better off if the railroads had been running under receiverships years ago.

The CHAIRMAN. Your idea is that instead of attempting to legislate now, we should defer it, or make further studies?

Dr. SPAHR. Yes, as to title II.

The CHAIRMAN. And gather further experience?

Dr. SPAHR. Yes, sir.

The CHAIRMAN. I want to ask you this question: Suppose that we had adopted this philosophy on the 5th of March 1933?

Dr. SPAHR. Conditions are different. It would not have done in 1933.

The CHAIRMAN. That was one time when it was necessary for Congress to meet and act?

Dr. SPAHR. Certainly.

The CHAIRMAN. When business recognized that necessity?

Dr. SPAHR. Yes, sir.

Mr. REILLY. Since this panic began, is it not a fact that there have been two schools of thought in this country as to how the country was to get help? One was to do nothing, just to sit still and let the laws of economics run their course, as in former panics; and the other was that it was an extraordinary industrial and financial break-down, and unless the Government affirmatively did something to help the industrial world to get back on its feet again, we were in for a terrific economic and financial crash?

Dr. SPAHR. Those were two of the schools of thought, but there is also another one.

Mr. REILLY. Which one do you believe in?

Dr. SPAHR. I do not believe in either one of those.

Mr. REILLY. What is your school of thought?

Dr. SPAHR. I say that the Government can do certain things, and certain overt acts should be undertaken by the Government. It does not mean to go back to the Hoover Administration, or to do nothing; it does not mean that at all. I have supported the Reconstruction Finance Corporation, and I would support the Securities Act, with slight modifications, and I think that the National Industrial Recovery Act has some good features in it, but the restrictive measures on business, I think, should have been scrutinized carefully and minimized and removed, if possible.

The emergency measures on money are very sound and necessary, and a whole series of things that should have been done were done, which I approve heartily, but I do not know of an economist of reputation that would fall in the first class that you mention, to do nothing and go back. That is a common thing said by those who wish to inflate the currency to those who oppose it; they say, "You wish to go back and do nothing." They think that that is an effective and squelching answer, but the real answer is that we do not wish to go back, but we wish to remind you that the best way to come out is to have a sound currency, in which the people have confidence.

Mr. FORD. What is a sound currency?

Dr. SPAHR. One in which people have confidence.

Mr. FORD. That answer does not explain it. Tell us what it means.

Dr. SPAHR. It means a currency that is convertible into something that has universal acceptability. To me that means the gold standard.

The CHAIRMAN. I believe you say that you approve the legislation on the subject of banking and currency in the nature of emergency acts passed during the early stages of the present administration?

Dr. SPAHR. Yes.

The CHAIRMAN. That is what I understood you to say you mean.

Dr. SPAHR. Yes.

The CHAIRMAN. That you approve of that legislation.

Dr. SPAHR. It depends on the specific acts, of course.

The CHAIRMAN. In other words, take the Banking Act, by which we authorized advances to be made by the Federal Government upon "sound securities." Do you approve that?

Dr. SPAHR. Yes, as an emergency measure.

The CHAIRMAN. We authorized the Government to issue Federal Reserve bank notes against the assets of banks.

Dr. SPAHR. I approve that as an emergency measure.

The CHAIRMAN. We even extended that to State banks finally. Do you endorse all of that?

Dr. SPAHR. I think so, as an emergency measure.

The CHAIRMAN. Is not that substantially what we are trying to do in this bill?

Dr. SPAHR. No, you are not.

The CHAIRMAN. Would it not have been better, if there is any vitrue in that legislation, if we had had it on the statute books, without waiting until every bank in the United States had closed its doors and the whole economic structure had collapsed? Would it not have been better if we had anticipated that trouble?

Dr. SPAHR. Yes.

The CHAIRMAN. That is what we are trying to do in this bill.

Dr. SPAHR. No; you are doing more than that.

The CHAIRMAN. We may be doing more than that, but we are trying to do that.

Dr. SPAHR. I said in my statement that some of those provisions to serve as emergency measures are safe enough if the banking system were a nonpolitical system.

The CHAIRMAN. I read that in your statement, and I recognize the basis for the ideal that you have in mind with respect to free and independent control of our banking and currency system, but how will we get under the Constitution of the United States? How will you get away from the right of the people of this country to change administration every 4 years by electing new officials and new Representatives in Congress to run the Government?

Dr. SPAHR. You can set up any type of board you please.

The CHAIRMAN. Yes; you can set it up and then tear it down when the next administration comes in, but there is not any way, as I understand the situation under our Constitution, by which we may set up any board for a life tenure or in perpetuity and turn the country over to them.

Dr. SPAHR. Canada has done it; why can't we do it? They leave their system alone.

The CHAIRMAN. We have a different system from Canada.

Mr. CROSS. And the Constitution here says that Congress shall regulate the value of money, and every Congress can come in here and change the previous idea.

Mr. SISSON. We cannot take away from the President the power to remove the members of the Federal Reserve Board.

Dr. SPAHR. You do not have to give it to him, either.

Mr. HOLLISTER. He has not got that today.

The CHAIRMAN. You would not contend that we cannot pass a law to abolish the Federal Reserve Board?

Dr. SPAHR. You can do anything you want to.

The CHAIRMAN. So that there is no way on earth, under our Constitution, by which we can set up a perpetual control free from the wishes of the people of the United States and their will as expressed in Congress.

Dr. SPAHR. It can be done as far as human beings can do it, if you will try to do it.

The CHAIRMAN. We can make a pass at it and say that we have done it.

Dr. SPAHR. You can develop traditions of sound central, independent banking, and frown upon all of these attempts by the political party in power to keep tinkering with the most delicate mechanism that we have. Unless we start to try to make it go, it never will be done.

Mr. GOLDSBOROUGH. Do you know that this so-called "sound system of central banking" that you are talking about is the creation of private bankers, who created that system for their own private purposes? That is certainly common knowledge. It began with the goldsmiths, in London, in 1794, and comes down through the Rothschilds and the great banking houses in this country.

Dr. SPAHR. I would say that the Bank of England has demonstrated, as a private institution, the finest traditions and the finest banking of any financial institution or system in the world.

Mr. GOLDSBOROUGH. It may be the finest system in the world, although in my opinion it is not as fine as the French system, but any system that we know anything about is not the creation of society, but the creation of a class.

Dr. SPAHR. But they are all regulated by the government.

Mr. GOLDSBOROUGH. Oh, no; the Government in England has been in control of the banking system. The Government of Great Britain is almost completely under the control of the Bank of England.

Dr. SPAHR. What about the Banking Act of 1844? Was not that drafted by the British Government to regulate the bank?

Mr. GOLDSBOROUGH. It may have been drafted for that purpose just as we draft laws for certain purposes in this country, but just as this country is measurably and very substantially under the control of the bankers, the Government of England is more under the control of bankers.

Now, there is no use talking about an ideal banking system being created by those whose interest it is not to have an ideal banking system, because an ideal banking system is one created and run in the interest of the whole public.

Another thing I think you failed to distinguish is the function of banking from the function of creating the people's money. Under the Constitution of the United States, Congress is given the authority to issue money and fix its value.

Nobody else is given that power under the Constitution. Under our system, up to the present minute, that authority to issue money and to regulate its value has been delegated to a private institution, the banking institution of this country, and they have been almost the sole managers of that up to this time.

Now, it can be said that this control has been partially taken away by the control that the Government has over the rediscount banks, the Federal Reserve Syetem, but when you take into consideration the fact that the member banks can expand the money they have in their reserve on an average of ten times without violating the law, you will see that, as a matter of fact, the member banks create money just as the Federal Reserve banks do.

So I say that it is not, in my judgment, sound to base your conception of a central banking system on banking systems which are the creation of private interests, not the creation of society.

Dr. SPAHR. Did not the Government create the Federal Reserve System.

Mr. GOLDSBOROUGH. The laws of the United States created the Federal Reserve System.

Dr. SPAHR. Surely.

Mr. GOLDSBOROUGH. But the Federal Reserve System, up until the present minute, is controlled by the member banks, that is, the Federal Reserve banks are, because the majority of the members of the boards of directors of the Federal Reserve banks are elected by bankers, and every Federal Reserve bank in the United States up until the present moment has been dominated and controlled by the great banks of New York.

Dr. SPAHR. And the Board is impotent, powerless?

Mr. GOLDSBOROUGH. It has been impotent, or acquiescent. Maybe the future will be brighter.

This bill, with the amendments suggested by the acting Governor of the Federal Reserve Board, is an attempt to take that control of the Federal Reserve System away from the banking system of the country and to place it under the control of society. It does not do it perfectly; it is not what I want, but it seems to me to be a distinct advance.

Dr. SPAHR. May I answer that?

Mr. GOLDSBOROUGH. The amendments suggested to this act by the Governor of the Federal Reserve Board contain a provision which makes the Board, which controls open-market operations, the changing of the discount rates, and the raising and lowering of reserves, consist of all of the members of the Federal Reserve Board.

Now, of course, that suggestion is not in the bill, but it is suggested by him and it comes just as much from the administration as the bill itself.

Another suggestion which the Powers makes it that when the Governor of the Federal Reserve Board is removed, he shall not cease to be a member of the Federal Reserve Board. That is taking away from the President the power to change the Federal Reserve Board.

Dr. SPAHR. I think that is wise.

Mr. CROSS. I would like to ask him a few questions.

Mr. HOLLISTER. Did he want to answer Mr. Goldsborough's question?

Mr. GOLDSBOROUGH. What I asked him is how he built up his concept of what a central bank should be on the past experience of the countries whose central banks have been built up by the bankers themselves.

Dr. SPAHR. I say that the lessons of central banks are unquestionably these, that the farther removed the central bank is from government domination, provided that it is operating within a sound organic act, the better it is for the country concerned.

Mr. GOLDSBOROUGH. Give us an example of what you are talking about.

Dr. SPAHR. England, France, Germany before the collapse, and Sweden which has a Government-owned bank, have a system that keeps the bank independent of Government meddling. They have even protected that, which is a Government-owned institution, and——

Mr. GOLDSBOROUGH. Do you mean to say——

Mr. HOLLISTER. Let him finish.

Dr. SPAHR. The lessons of central banking are unquestionably that wherever a government has reached in to control the central banking system, you control your whole economic system. You can bleed your system white—that is, a dictator can.

Mr. GOLDSBOROUGH. Just give us an instance of inflation—that is always the resort of all those who believe in things as they are—in any country in the world through all history that has had a stable government at the time of inflation.

Dr. SPAHR. My definition of inflation, Mr. Goldsborough, was one that I choose to stick to, and therefore I say that you have inflation all the time to some degree.

Mr. GOLDSBOROUGH. Do you mean to say that we have had inflation between 1929 and the present time in this country?

Dr. SPAHR. Yes, sir; I do. Did you notice how I defined it?

Mr. GOLDSBOROUGH. With bankruptcies going on over the country?

Dr. SPAHR. Yes, sir.

Mr. GOLDSBOROUGH. With the debtors unable to pay their debts, and the producers unable to produce enough to pay their taxes, you say there is inflation in this country now?

Dr. SPAHR. Surely. Did you notice my definition?

Mr. GOLDSBOROUGH. Well, you can state your definition, sir.

Dr. SPAHR. I say that inflation prevails or results from the extension of purchasing power, either in the form of money or credit, which is not backed by sufficient reserves or commodities to liquidate it.

Mr. GOLDSBOROUGH. I want to know if you can give us an instance of that ever occurring in any government that was stable.

Dr. SPAHR. It is always occurring in any country, stable or unstable.

Mr. GOLDSBOROUGH. The instances that we have been given here in this committee, if I can give them briefly, are the instances of Germany after the war, the instance the French assignats issued some time during 1796 and for several years thereafter, and the Continental money. What other instances have you? Those were all instances where the government was unstable, and nobody knew what was going to happen.

Dr. SPAHR. We had more inflation from 1923 to 1929——

Mr. GOLDSBOROUGH. In this country?

Dr. SPAHR. Surely; that is what caused the collapse.

Mr. GOLDSBOROUGH. Do you mean to say that the supply of money during that period was increasing more rapidly than our productive capacity?

Dr. SPAHR. Than the productive capacity justified.

Mr. GOLDSBOROUGH. Was the difficulty in our productive capacity, or in our ability to distribute what we could product?

Dr. SPAHR. Both.

Mr. GOLDSBOROUGH. Do you mean to tell me that there has ever been a time in the history of this country when we had produced more than we could consume, provided that our people had the buying power?

Dr. SPAHR. I think that your statement is quite accurate.

Mr. GOLDSBOROUGH. What do you say?

Dr. SPAHR. I would say no to your question. I agree with your point of view there.

Mr. Goldsborough, I think that I can simplify answering you, so that you will not have to ask me so many questions, which are all pointed in one direction.

My definition of inflation means that anybody that goes to a bank, for example, and borrows can have his purchasing power inflated. If I think that I am going to engage in a profitable transaction, I will go to the banker and I will say, "I would like to borrow $1,000 from the bank." If he thinks that it is a good idea, he lets me have that, and I engage in the transaction and find that I made a mistake, and only use $500. So I go to the bank and say, "I cannot pay you", and the bank thereupon takes a loss of $500. So in that case my purchasing power was inflated by $500; that $500 was the measure of inflation which took place.

We do not talk about inflation in this country unless the great mass of people get into that position—and some individuals are there all the time—when they have overborrowed and cannot liquidate. That is when we talk about inflation.

From 1924 and 1925 to 1929, a tremendous amount of installment buying was taking place. People were getting a purchasing power completely beyond what they could repay—and the stock market crash was the final culmination of that—and then the liquidation set in, and they began to pay for that inflation.

That is what I say to you, that there is always inflation, and we were nearly misled from 1923 to 1929 by relatively stable price levels.

Mr. GOLDSBOROUGH. I agree that we can never have any prosperity where all of our money is based on debt, as it is in our present system, and which seems to be the one that you desire to perpetuate for all time.

Dr. SPAHR. I never said that, and I never implied that. There is a virtue in defining deflation accurately.

Mr. GOLDSBOROUGH. I know perfectly well that installment buying was one of the things that created this difficulty, and I know that you cannot get away from installment buying. You cannot get buying power in the hands of your people as a mass where your money is created exclusively by the creation of a debt. It just cannot be done, because you cannot distribute buying power as fast as the debt accumulates, and you are bound to have one of these crashes right after the other.

Dr. SPAHR. There is one point that I would like to answer there, and that is your assumption that you can put buying power in the hands of the people without puttting it in the hands of the producer first. Consumer purchasing power comes from production, and therefore your initial start is productive activity. You can not start anywhere else.

Mr. GOLDSBOROUGH. That does not necessarily follow.

Dr. SPAHR. It does follow.

Mr. GOLDSBOROUGH. It does not, for this reason, that we have to recognize in this country that we have an extremely mechanized system. We have an electrified system which has taken away the ability of the ordinary laborer to get work. We must recognize in this country that we are the heirs of all the ages and that all of our people are entitled to some of the results of modern invention. Unless we do recognize that concept, we will have to go into a revolution sooner or later.

Dr. SPAHR. Mr. Goldsborough and Mr. Chairman, is it objectionable if I should ask a question?

Mr. GOLDSBOROUGH. No.

Dr. SPAHR. I made the statement that there is no place where you can get consumer purchasing power except from production. You said that that is not true. Can you tell me where consumers can get it, except from production?

Mr. GOLDSBOROUGH. Of course, your question is that it has to be produced before they can get it?

Dr. SPAHR. That was my statement.

Mr. GOLDSBOROUGH. I did not understand you to mean exactly that, because everybody knows that you cannot eat bread until it is baked and properly prepared, but the point that I am making is this, that we under our present system can produce more than our consumers can consume, given the buying power which they can get under a system where our money is entirely created upon debt. That is what I am talking about, that you cannot get buying power into the hands of your people under a system where your production can only be created through debt.

Dr. SPAHR. Using deposit currency or evidences of debt as a medium of exchange, it is merely the most economical means of exchange that people have devised, and if your statement is true, you would have to say that book credit is unsound. If a woman goes into a grocery store and receives book credit for something that she has taken in there to exchange for groceries that she will take later, that is unsound, if your statement is true.

Mr. GOLDSBOROUGH. Maybe I can make you understand what I have in mind by this statement: Suppose that the people became properous, and were able to pay their debts; what would we do for money in this country?

Dr. SPAHR. Whatever is sound, and generally acceptable.

Mr. GOLDSBOROUGH. Great God, man! Under our present system, we would not have any money left, because all of our money is based on debts, and when those debts were paid, there would be nothing left.

Dr. SPAHR. You are mistaken, and let me show you why.

One day in 1919, in New York, the clearinghouse cleared over a billion and a half of deposit currency and did not use a penny. Now, all of those business transactions were liquidated because they had a clearing mechanism for clearing deposit currency which is the slickest, finest currency ever devised by human beings for the purpose of liquidating debts.

Now, if your contention is true, then that credit extension is unsound, and the question is merely one of whether it is sound or not.

Mr. GOLDSBOROUGH. Oh, no; all of the banks in the United States have capital, surpluses, and undivided profits of something less than seven billion dollars.

Dr. SPAHR. Yes.

Mr. GOLDSBOROUGH. If all of the banks' debts were paid that would be all of the money that there would be in circulation, would it not?

Dr. SPAHR. But the banks' debts will not be paid. That is a foolish assumption.

Mr. GOLDSBOROUGH. But that is not the question. The point is this, that in this country we can have no permanent prosperity, for this reason, that prosperity is indicated by the ability of a man, or corporation, or what not to pay his debts.

Mr. SPAHR. Surely.

Mr. GOLDSBOROUGH. And my contention is that under a system where your money is created by debt, as soon as you begin to pay your debts, you cause another deflation, because you destroy the money in the country.

Answer that, if you can.

Dr. SPAHR. I can.

Ninety percent of our exchange is normally done by deposit currency, which you say is debt. That means that we are exchanging 90 percent of our commodities, but if you stopped that sort of thing and reduced your medium of exchange down to just currency, how many transactions could be carried on?

Mr. GOLDSBOROUGH. That is exactly my opinion, that we have to do our business with borrowed money. But there is another way to do it.

Dr. SPAHR. On credit, surely.

Mr. GOLDSBOROUGH. You do not think it would be wise for Congress to exercise its prerogative of issuing money and regulating its value by putting money in circulation, whatever necessary, say, $250 per capita or whatnot, and prevent the banks from lending money they don't have?

Dr. SPAHR. I certainly do not think it would be wise.

Mr. GOLDSBOROUGH. And you also think that for Congress to exercise its prerogative and issue money, and regulate its value, to pay its debts would be forgery?

Dr. SPAHR. Yes, sir; I do.

Mr. GOLDSBOROUGH. Although the Constitution of the United States gives Congress the power to issue money and to regulate its value, you say that if it did that to pay off the Government debt, it would be forgery?

Dr. SPAHR. Yes; I do; and I take it you saw my article?

Mr. GOLDSBOROUGH. I saw an article that you put in the Christian Science Monitor, and it was scattered around in other newspapers controlled by the same influences. I also understood from my secretary that you had sent me an open letter. An open letter I never read, because I know it is propaganda, and I did not see it until this morning.

Now, I believe you are a member of the Economists' National Committee on Monetary Policy, and that Dr. H. Parker Wills is also a member of that organization?

Dr. SPAHR. Correct.

Mr. GOLDSBOROUGH. I have his book here, The Banking Situation, a very recent book that you may be familiar with, published in 1934, in which he says, at pages 43 and 44:

> There is probably no country in the world in which there is a greater approach to the real existence of a so-called "money trust" than in the United States, nor is there any country in which there is less assurance of nonpartisanship and fairness in the extension of credit in banks to individuals or corporations.

Do you agree with that statement?

Dr. SPAHR. I do not know the basis of facts. I would say offhand, no. I do not know what facts he based that on.

Mr. GOLDSBOROUGH. He, further, says this—and I thought that you and Dr. Wills slept in the same bed as far as economics were concerned.

Mr. REILLY. They are twin beds, probably. [Laughter.]

Mr. GOLDSBOROUGH. Maybe you know more about twin beds than I do. I do not know.

Mr. REILLY. The same room, but twin beds.

Mr. GOLDSBOROUGH. Another statement made by Dr. Wills in this new book, The Banking Situation, which sheds a great deal of light, is:

> For many years it was the practice of the banking community to secure a pigeonholing or ignoring of new legislation by the familiar methods of legislative obstruction and control.

What do you think of that?

Dr. SPAHR. That is substantially accurate.

Mr. GOLDSBOROUGH. Do you think that the control of the money ought to be left where it now is, in the hands of the bankers?

Dr. SPAHR. No; I do not like that statement.

Mr. GOLDSBOROUGH. Do you not think that it is in the hands of the bankers now?

Dr. SPAHR. To some extent, yes; to a large extent.

Mr. GOLDSBOROUGH. What would you like to do with the money? Who is going to control it if the bankers do not? You do not want society to control it.

Dr. SPAHR. A metallic currency has to be controlled by the Government, through the Treasury. The gold and silver certificates would also have to be controlled through the Treasury directly. The bank notes ought to be controlled through the central banking mechanism.

Mr. GOLDSBOROUGH. Ought not the central banking mechanism to be a governmental agency?

Dr. SPAHR. No.

Mr. GOLDSBOROUGH. A banking agency?

Dr. SPAHR. No.

Mr. GOLDSBOROUGH. Then what?

Dr. SPAHR. An independent body or board operating in the interests of commerce, agriculture, and industry, regardless of individual interests, putting the Government exactly on the same basis.

Mr. GOLDSBOROUGH. You think you want to sovietize your definition and say commerce, agriculture, and industry, or do you think that you want to say it should be in the interests of society?

Dr. SPAHR. It should be in the interests of society, but put the Government on exactly the same basis and treat it just the same, because it is a borrower, too. It is not entitled to any more favorable consideration than any other borrower in the market.

Mr. GOLDSBOROUGH. Are you familiar with the bill which was introduced in the last session, on which a subcommittee of this committee had hearings for about 7 weeks, called the monetary authority bill?

Dr. SPAHR. I have seen it.

Mr. GOLDSBOROUGH. What do you think of that sort of legislation?

Dr. SPAHR. Well, I think the fundamental philosophy underlying the thing is wrong.

Mr. GOLDSBOROUGH. I just thought you said that it was right, that there ought to be an independent organization.

Dr. SPAHR. I am not an authority on the details of that bill, but, as I recall it, it provides the machinery by which this Federal monetary authority can force the price level up by inflation to any desired price level that they think they would like to have, as, for example, in 1926. They are going to control the currency and adjust it to what this particular Federal monetary authority considers is a desirable price level, largely with the idea, as they say, to take the burdens off of the debtors of the country.

The fundamental philosophy underlying that is false.

Mr. GOLDSBOROUGH. It is false, then, to put the different classes of society on a fair basis? In other words, it is false to put the debtor on such a basis of relation to his creditor that he can pay his debt and the creditor can receive the debt. We think that it is just as much in the interests of the creditor for the debtor to be placed in position of paying, as it is in the interests of the debtor himself.

Dr. SPAHR. So do I, but what you will do is to injure the very people you think you are going to help.

The CHAIRMAN. It is 20 minutes past 12. I suggest that we come back at 3 o'clock.

That will be all right with you, Professor?

Dr. SPAHR. Yes, sir.

The CHAIRMAN. We will meet at 3 o'clock.

(Thereupon, at 12:20 p. m., a recess was taken until 3 p. m.)

AFTERNOON SESSION

(The recess having expired, the committee reconvened at 3:15 p. m., Hon. T. Alan Goldsborough, presiding.

Mr. GOLDSBOROUGH. The committee will come to order.

STATEMENT OF DR. WALTER E. SPAHR, PROFESSOR OF ECONOMICS, NEW YORK UNIVERSITY—Resumed

Mr. GOLDSBOROUGH. Dr. Spahr, there are just one or two questions that I wanted to ask, and then I will not take any more of your time.

You spoke this morning of the remarkable facility with which the banks manage the checking system and the clearing-house system, and I rather gatehred that you thought that system was an incident of the creation of money by debt, and that if we created money by any other process except through debt we would lose the benefit of that system. Is that your thought?

Dr. SPAHR. We probably would to some extent.

Mr. GOLDSBOROUGH. Why?

Dr. SPHAR. Because that is a clearing system for deposit currency and not for bank notes.

Mr. GOLDSBOROUGH. I know you do not mean to say that if we had, for instance, 100- or 50-percent deposit reserve that we could not employ a checking system, do you?

Dr. SPAHR. But it is probably an extremely wasteful system in the sense that you are going to have a 100-percent reserve against your deposits when you consider that deposit currency throughout a year is terrific, in billions.

Mr. GOLDSBOROUGH. I understand, but if the Government or someone else were to pay to the banks the probable charge for clearing checks and doing what they do now, they could carry on with equal facility as they can now, could they not?

Dr. SPAHR. But the fundamental conception, Mr. Goldsborough, there, I think, is wrong in this sense, that the function of reserves is to clear in the last analysis, and the better your clearing system functions the better your medium of exchange functions. Now, to set up a 100-percent reserve is simply to deny the functions of your reserves. Reserves are clearing. Now, what banks do is to substitute their credit, which is generally acceptable, for the borrower's credit, which is not, and then the law requires the bank to keep a reserve in lawful money against those deposits to clear.

Mr. GOLDSBOROUGH. What is the difference, insofar as clearing checks is concerned, whether the reserve is 10 or 5 or 50 or 100 percent?

Dr. SPAHR. Because what people wish is an exchange that will take care of the transactions easily. They do not want money. They want deposit currency. Ninety percent of our business is done that way.

Mr. GOLDSBOROUGH. Do you mean to say that you cannot make transfers by check, that you must use money? Do you mean to say that you cannot transfer money by check if you have 100-percent reserve?

Dr. SPAHR. What is the point on the 100-percent reserve? Of course, you can do it by check, but you have 100 percent reserve there of idle money. That is a wasteful system. That is my point.

Mr. GOLDSBOROUGH. That is a wasteful system?

Dr. SPAHR. Yes.

Mr. GOLDSBOROUGH. In your judgment?

Dr. SPAHR. Yes, in my judgment.

Mr. GOLDSBOROUGH. Yes, but I am asking you whether or not this bank-clearing process, which is a process of banking mechanics, and which is good, could not be carried on just as well under some other reserve than under our present reserve of 13, 10, and 7 percent?

Dr. SPAHR. Oh, I think so.

Mr. GOLDSBOROUGH. Yes. Now, I notice here in your set-up of your organization that Professor Kemmerer is one of your leading members. Is that correct?

Dr. SPAHR. He is the chairman of the committee.

Mr. GOLDSBOROUGH. Chairman of the committee? What is the name of it?

Dr. SPAHR. Economists' National Committee on Monetary Policy.

Mr. GOLDSBOROUGH. In December 1927 Professor Kemmerer said:

> The world sooner or later must either learn how to stabilize the gold standard or devise some other monetary standard to take its place. There is probably no defect in this economic organization today more serious than the fact that we use as our unit of value not a thing with a fixed value, but a fixed weight of gold with a widely varying value. In a little less than a half a century here in the United States we have seen our yardstick of value, namely, the value of a gold dollar, exhibit the following gyrations: From 1879 to 1896 it rose 27 percent; from 1896 to 1920 it fell 70 percent; from 1920 to September 1927 it rose 56 percent. If figuratively speaking we say that the yardstick value was 36 inches long in 1879, when the United States returned to the gold standard, then it was 46 inches long in 1896, 13½ inches long in 1920, and is 21 inches long today.

Now, are you informed as to whether or not Professor Kemmerer is still of the same opinion as he was in 1927?

Dr. SPAHR. I would not be competent to speak for him.

Mr. GOLDSBOROUGH. You do not know about that?

Dr. SPAHR. No.

Mr. GOLDSBOROUGH. That is all, Mr. Chairman.

The CHAIRMAN. All right. Mr. Cross?

Mr. CROSS. Doctor, you referred this morning to "sound money" several times. Do you mean by "sound" a sound dollar, an honest dollar?

Dr. SPAHR. Yes, an honest dollar.

Mr. CROSS. Do you figure that a dollar that will buy one particle of all the things that are necessary to feed and clothe and supply the comforts of the people today, that next year will double its purchasing power, where it will buy twice, and two particles of all those commodities, sound?

Dr. SPAHR. Mr. Cross, let me answer that this way: The value of money is a ratio between goods and services sold.

Mr. CROSS. Now, please answer that question; you know what I mean without going off into a collateral discussion.

Dr. SPAHR. I will try to answer more briefly. You seem to lay the responsibility on money, whereas it is the ratio of goods.

Mr. CROSS. No, I am not laying it on anything except the purchasing power of goods.

Dr. SPAHR. All right, I will try to answer another way. The purchasing power of money should not be stable unless our economic system is in a state of equilibrium between production and consumption.

Mr. CROSS. Then I will put the question to you like this. Certainly money is affected by supply and demand, is it not?

Dr. SPAHR. That is correct.

Mr. CROSS. Gold is just a commodity, is it not?

Dr. SPAHR. That is right.

Mr. CROSS. During the World War when 42 countries quit using gold as money and we continued to use it as money, it flooded here, did it not?

Dr. SPAHR. That is right.

Mr. CROSS. Until prices of everything shot up, because gold was plentiful and the supply was plentiful, and its purchasing power went down. Of course, we say prices go up. That simply means the purchasing power of the money goes down. That is true, is it not?

Dr. SPAHR. But that was due to credit and not to the gold.

Mr. CROSS. Why do you say "credit", when those 42 countries fought the war, and when they struggled to get gold, to get back to using gold for money, that the demand became great for gold, and of course, up shot its purchasing power, which is still a commodity, is it not? It is a commodity plus the statutory fiat money. It could pay the debts, both public and private, but still it is a commodity plus that artificial statement in the statute?

Dr. SPAHR. True enough, but I would not ignore the credit which was responsible for 90 percent of it.

Mr. CROSS. I know we had the credit, but nevertheless it had a tremendous effect upon the question of credit, because credit, of course, began to shrink whenever gold became dear, and people got frightened, and it had an effect, and they had over here hundreds of millions every week, the big birds who knew what was happening, and everybody commenced getting frightened, the banks began to burst. Naturally, it resulted from a throwing out of the gold, and they commenced shipping it off.

Dr. SPAHR. What year are you talking about now?

Mr. CROSS. Well, along in 1930 or '32, and up to 1933; and the President stopped it, and we passed an act stopping gold from going out of the Treasury.

Dr. SPAHR. But we did not have a collapse in 1929 because of any scarcity in gold.

Mr. CROSS. No; not at that particular time, but they were trying to get back. They were trying to get back on the gold standard in other countries, those 42 countries, and none of them had tried to go back, and they were struggling to get it. Do you not remember that?

Dr. SPAHR. We still had a surplus of gold in 1929.

Mr. CROSS. How is that?

Dr. SPAHR. We still had a huge surplus of gold in the United States in 1929.

Mr. CROSS. We did, I know; but the other countries were trying to get it, and we got it over here, because it flooded over here when they quit using it.

Dr. SPAHR. We had no restrictions on the out-movement of gold in 1929.

Mr. CROSS. I know we did not. I know we did not. It commenced to leave.

Dr. SPAHR. So gold could not have been responsible for the collapse in 1929 in this country.

Mr. CROSS. We have got no measure for values. When you get to length you have got a measure; and, by the way, it took the world hundreds of years to get that measure. If you remember, people used to take three grains of barleycorn and used that for a long time, just as they used to take when measuring other things, for instance, weights. We had to use grains of wheat, and yet the world thought that that was all right for a long time until finally they got down to something, of course, exact and practical.

Now, we have got no measure of value, have we? You have got a measure of the foot for length, you have got the pound to get weight; you have got the cubic foot to get volume; but you have no measure of value. In other words, we take a weight to get the measure of value, do we not? We take so many grains of a metal to measure value with?

Dr. SPAHR. I understand your point thoroughly, Mr. Cross. I would like to answer it this way, if I may: I think it covers the question. I understand what the fluctuation of the price-level means. It means fluctuation in the value and purchasing power of the currency, but there is no defense we can set up economically, of having a stable price level unless our economic system is in a state of economic equilibrium.

Mr. CROSS. I did not ask you all that. I asked you whether we had any measure of value.

Dr. SPAHR. Yes; but it fluctuates.

Mr. CROSS. No; our monetary unit.

Dr. SPAHR. It fluctuates.

Mr. CROSS. Certainly it does.

Dr. SPAHR. Yes.

Mr. CROSS. Well, when it fluctuates that is a dishonest monetary unit, is it not?

Dr. SPAHR. But is the fluctuation due to the dollar or to the goods?

Mr. CROSS. It does not make any difference what it is due to. I am trying to get an answer to a simple question. When it fluctuates it is dishonest, is it not?

Dr. SPAHR. Maybe the goods are dishonest.

Mr. CROSS. No; wheat makes flour, the wool makes clothes, and so on.

Dr. SPAHR. But value is a ratio.

Mr. CROSS. Just answer my question. If you borrow $1,000 from A today, and when A goes to pay you back you he has got to pay you back twice the true value of the things that sustain your life and give you the comforts and the necessities of life, he is paying you back in real values twice what he got from you, is he not?

Dr. SPAHR. I understand that.

Mr. CROSS. Now, if $1 of wheat will do me for a lifetime that is all I need, is it not?

Dr. SPAHR. That is right.

Mr. CROSS. So when that dollar changes in its purchasing power all these things that supply me with the comforts and necessities of life, the fellow from whom I borrowed it, or the fellow to whom I loaned it is being "stung" because he has got to give me more in true values, has he not?

Dr. SPAHR. That is right.

Mr. CROSS. That is not an honest dollar, is it?

Dr. SPAHR. It may be.

Mr. CROSS. Well, I am talking experience. It is not, however, now, in our practical experience, is it?

Dr. SPAHR. It may be.

Mr. CROSS. Well, it has not been, has it?

Dr. SPAHR. You are not accepting the notion of a radio. For example, Mr. Cross, some businesses disappear entirely. As they go down, the purchasing power declines and declines and declines. They pass out. Now, they may say that the dollar is not honest because their purchasing power is steadily declining. For example, when the carriage business had to compete with the auto, the cariage manufacturer could howl all he pleased about his declining purchasing power, it did not do him a bit of good; and the dollar was not to blame.

Mr. CROSS. But there was a thing passing out, as an economic change, going out of existence.

Dr. SPAHR. Yes.

Mr. CROSS. But you say now your position is that this weight of gold is the best thing we can get yet, this one commdity to measure all commodities, and as I have illustrated heretofore you put one commodity over there, and we will call it the gold dollar, in one bucket, and over here you put all property, lands, houses, and commodities of every description, and you lay this chain there, we will say, to pass around the pulley.

Now, this one commodity over here affects and reflects in price all the commodities?

Dr. SPAHR. True.

Mr. CROSS. So when it goes up by reason of scarcity, or the demand becomes great, which means it goes up in purchasing power, down goes the other bucket, representing prices; and of course when the demand for the gold supply becomes great it cheapens, and up goes the price of everything. Of course, along with that, now, you have got your credit proposition.

Dr. SPAHR. Yes.

Mr. CROSS. Your check dollars, and that is one of the most dangerous of inflations and deflations.

Dr. SPAHR. Right.

Mr. CROSS. The testimony here has been that you can control your credit inflation by the levers of rediscount, raising and lowering the Federal Reserve and open-market transactions, but we have gone on, and the testimony here of Governor Strong and Governor Harrison and Dr. Fisher and all those fellows who testified before this committee heretofore, has all been that we can control inflation but we are helpless when it comes to deflation.

Now, the proposition is to get a dollar, a monetary unit, whatever you call your monetary unit, so that it will have the purchasing power on a stable level, and when taken in harmony with a great number of commodities—of course, we use 784 down here, but you could use 50. Do you not think, by taking the wholesale price-level of a number of essential commodities, and keeping your dollar stable on that level, that it would be more honest than the dollar we have got today?

Dr. SPAHR. Would you like to stabilize the price of it now at this level?

Mr. CROSS. No; but you could take any standard you wanted to. I do not care whether you take '21 to '29, or '26, here, but that is a question of taking that as a standard; but do you not think you could take a standard where it would be higher than those, or lower, and keep them on that line?

Dr. SPAHR. My answer it we should do everything we can to stabilize the value of money when the price-level is in a state of economic equilibrium. We should not try to stabilize the price level now.

Mr. CROSS. But do you think that can be done?

Dr. SPAHR. It never has been done. I think we ought to try however to do the best we can. We ought to set up every mechanism we can devise to do it, when we reach a state of economic equilibrium.

Mr. CROSS. The testimony of Dr. Sprague and a number of others here was that they came to the conclusion that they could; at least, it ought to be tried, they thought it ought to be done; that heretofore they had no gold with which to go ahead. They, today, are just like a ship without a rudder, and do you not think it can be done?

Dr. SPAHR. I do not know. I think we ought to try, but notice my qualification: We ought not to try until we reach a state of economic equilibrium, and that will mean that we are going to have, as business rises, a rise in prices. I want to see it. I think most people want to see it. We ought to have it. It is the thing that will accompany prosperity. Then, when we get up to a certain level where we can see that our production and consumption and the various factors of distribution are coming into harmony, then we ought to begin to use everything that we can devise; and most of that will be on credit, because credit does about 90 percent of the business.

Mr. CROSS. Of course, we understand that.

Dr. SPAHR. And then see how well we can do it. Now, nobody can say that we can do it. The best thing we can do is try.

Mr. CROSS. Do you not think you could do it by raising and lowering reserves, rediscounts, and open-market transactions?

Dr. SPAHR. I think if you would lower reserves you would precipitate a collapse.

Mr. CROSS. You could raise them, you mean?

Dr. SPAHR. I meant to say raise. If you raised your reserve you would probably precipitate a pretty severe collapse. I think that is a dangerous weapon.

Mr. CROSS. When inflation is going on as it did here in 1929, do you not think it was a good idea to raise reserves?

Dr. SPAHR. I do not know.

Mr. CROSS. Well, you just do not know?

Dr. SPAHR. I think raising the rediscount rates——

Mr. CROSS. Now, you spoke this morning along this line. Are you familiar with what England is doing now?

Dr. SPAHR. In a general way.

Mr. CROSS. Do you know what she is doing with her so-called "Serengaria?"

Dr. SPAHR. In a general way, I think.

Mr. CROSS. Is she not getting on a managed-currency proposition with very little gold? Do you know how much she has got in her reserves now?

Dr. SPAHR. No. I would have to look it up.

Mr. CROSS. A billion and a half. France has got five and a half billion. We have got a billion, four hundred and ninety million.

Dr. SPAHR. From what has happened to her foreign-exchange rates, now, I would not think her management was successful.

Mr. CROSS. Do you not think she is doing exactly what she is doing, to get the advantage of the export trade?

Dr. SPAHR. I do not have any idea.

Mr. CROSS. I think every state and country will say she is.

Dr. SPAHR. I have not paid attention to that.

Mr. CROSS. Japan has got such a tremendous hold on it, and she is trying to touch Japan and push her off the board, and we are sitting here—do you think we should have devalued the dollar when we did?

Dr. SPAHR. No.

Mr. CROSS. Do you think France was wrong when they devalued the franc 80 percent?

Dr. SPAHR. No.

Mr. CROSS. You think she was wrong or right?

Dr. SPAHR. Right.

Mr. CROSS. Right? Why were we wrong, then, in devaluing the dollar?

Dr. SPAHR. Because France devalued at inflation, merely to stabilize. We devalued not to stabilize, but to get more currency.

Mr. CROSS. Oh, is that what happened to France?

Dr. SPAUR. Yes.

Mr. CROSS. She did that to stabilize?

Dr. SPAHR. Yes.

Mr. CROSS. And we did it just to get more currency?

Dr. SPAHR. That is right.

Mr. CROSS. And what do you think about Italy and Belgium? Belgium cut her belgas.

Dr. SPAHR. To stabilize them.

Mr. CROSS. And now she is cutting them again, or fixing to?

Dr. SPAHR. She has not done it.

Mr. CROSS. I know; but the ministry has jut changed.

Dr. SPAHR. All of those devaluations in Europe were to stabilize after inflation.

Mr. CROSS. Inflation? Why, they are deflated over there, as we are.

Dr. SPAHR. Not when they were devaluing.

Mr. CROSS. When France devalued she was in a tremendous condition of inflation; so were Belgium and Italy.

Dr. SPAHR. I remember Italy was.

Mr. CROSS. Well, Belgium is in distress, too, now?

Dr. SPAHR. That is since. She has gone through a depression since that time.

Mr. CROSS. We are in a depression here; should we not devalue?

Dr. SPAHR. Because we devalued to force the price up. They devalued to stabilize.

Mr. CROSS. Do you think it was to force the price level up, when she cut her franc into five?

Dr. SPAHR. No.

Mr. CROSS. If you owed me 1,000 francs over there, and they devalued the franc about 80 percent, and cut 1 franc into 5, you would pay me your franc by giving me 5 francs to pay off that debt, the same as 1 originally?

Dr. SPAHR. I would like to put on record here that France's price level was stable for 18 months before she devalued.

Mr. GOLDSBOROUGH. What she did was this, and this will go on the record. Her internal debt was swamping her, and she devalued for the purpose of cutting her internal debt down 80 percent. That is what she did.

Dr. SPAHR. That was merely a recognition of what had already happened.

Mr. GOLDSBOROUGH. Of course, she disregarded her debt. She repudiated her debt, that is all.

Dr. SPAHR. It was merely a recognition of what was happening.

Mr. GOLDSBOROUGH. Now, here we are in this country. I read a table into the record the other day, in which the country is shown to be loaded with debt. Debt cannot be paid unless there is a change in the price level. It just simply cannot be done. We have got to do one of two things. We have either got to raise our price level to a point where the position of the debtor and the producer will be on a plane with that of the creditor; we have got to do that, in order to pay our debts, or else we have got to complete deflation and have further bankruptcy in the country. Now, there are only two roads to take.

Dr. SPAHR. Both those statements are wrong.

Mr. GOLDSBOROUGH. I assumed that you would say so, but at the same time I still think they are are both right.

Dr. SPAHR. I can demonstrate the accuracy of that.

Mr. HOLLISTER. He can explain.

Mr. GOLDSBOROUGH. Of course, he can.

Dr. SPAHR. If you raise a price level by inflation you impoverish the mass of your people. Now, if you are assuming your debtors are the mass of the people, you are going to make them poorer. As currency is inflated prices rise, people find it more difficult to live, and you can wipe your mass out.

Mr. GOLDSBOROUGH. You are talking about retail prices?

Dr. SPAHR. I am talking about the prices that people have to pay for goods.

Mr. GOLDSBOROUGH. No, no. When you begin to inflate, the first thing you do is raise the price of your basic commodities, and when you raise the price of the basic mommodities, then you furnish buying power to those that produce the basic commodities; and when you do that you allow your factories to start and give labor to the people that buy the food and shelter, the clothing that they need. That is the process. The process of inflation does not raise the price level of the retail prices first. It first raises the prices of basic commodities; and then the rise in prices of retail commodities is a very slow process, which comes after the buying power of the public has largely been reestablished. That is what happens.

Mr. HOLLISTER. Mr. Chairman, might I ask one thing, and that is that the witness be given an opportunity to talk? The witness starts to answer and somebody interrupts him.

Mr. GOLDSBOROUGH. I do not think so.

Mr. HOLLISTER. I think he ought to be allowed to make his answers.

Mr. GOLDSBOROUGH. I did not interrupt him.

Mr. HOLLISTER. I think you did.

Mr. GOLDSBOROUGH. No.

Mr. HOLLISTER. He was in the middle of a sentence.

Dr. SPAHR. The fact is that inflation in those European countries practically ruined the masses of the people, which shows that their buying power did not keep up. Now, debts are paid out of income and not paid out of prices, and unless the rise of prices is sound and is the result of being pulled up by increased purchasing power of the people that are doing the buying, they cannot pay their debts more easily; therefore, we are back to the question we were on this morning. The point is, to have a sound rise in prices, not a price level that is forced up by inflating the currency.

Mr. HANCOCK. Mr. Cross, may I ask one simple little question right here?

Doctor, if you can buy a bushel of wheat for a dollar today, and next year you are able to buy 2 bushels of wheat for a dollar, what has happened? Has the wheat done down or has the dollar gone up?

Dr. SPAHR. We have only this way to answer that question: If the index number of the price level is steady, we say the value of the dollar has been changed and something has happened to the wheat production, because the wheat output is simply one comodity as against the dollar.

Mr. HANCOCK. Does the natural law of supply and demand play any major part in that change?

Dr. SPAHR. It certainly does.

Mr. GOLDSBOROUGH. He says when a dollar is stable.

Dr. SPAHR. Your wheat output may have doubled.

Mr. HANCOCK. I am seeking information in good faith.

Dr. SPAHR. The wheat output may have doubled. Now, we are talking about the value of money changing. We are talking about an average of all prices that compose the index number, and your wheat supply may have increased or decreased, but whether your value of money shifted or not, you have to look at your index number, and that is something else.

Mr. HANCOCK. That is all.

Mr. CROSS. If you take, say, even 50 basic commodities, and if the dollar next year will buy twice as much of those 50 basic commodities as it did this year, then which one has shifted?

Dr. SPAHR. It is a ratio again, Mr. Cross.

Mr. CROSS. I know it is ratio, but which one has shifted?

Dr. SPAHR. You cannot say.

Mr. CROSS. Now, you take 50 commodities. Here is a short crop, because of rains, in production, and here on the other side, the other part of the country raising something else, is a big crop, and so among themselves they are working up and down, going this way and that way, when you take the whole 50; but when you take the average for the whole 50, and the dollar will buy twice as much the next year as it does this year, which has shifted?

Dr. SPAHR. It is commonly said the value of money has shifted, but the facts may be otherwise. That is, you may find out the supply of currency has not changed.

Mr. CROSS. We are not talking about the volume of currency. I am talking about the purchasing power of the monetary unit.

Dr. SPAHR. But that is always a ratio.

Mr. CROSS. Yes; I know it is a ratio, but which has shifted, now, supposing that for $1 I can now buy enough to take care of me all my life, but next year it will not be enough?

Dr. SPAHR. When you see a see-saw, as you are looking at it one end goes up and the other goes down, and you say, which is see-sawing? That is your question.

Mr. CROSS. What I am trying to get is this: Here is one commodity, the gold commodity; so many grains of it this year will buy enough food to take care of me today, and next year it will buy enough to take care of me all my life. Now, which one has shifted?

Dr. SPAHR. I say it is like the see-saw. I cannot say. I cannot answer your question, in one respect. When we started liquidation in 1929 and came on down into this depression it was the liquidation of goods that was responsible for the contraction of the currency. The currency had nothing to do with it. We had surplus reserves in 1929. We had surplus gold in 1929, and the business liquidation was a thing that caused the contraction of deposits and the slowing up of velocity, and the contraction simply went along with the liquidation. Now, which is responsible?

Mr. CROSS. We have got enough gold reserves now, more than 2 billions of reserves. We could expand on check money to the extent of $25,000,000,000.

Dr. SPAHR. But I was answering your question. Which is responsible?

Mr. CROSS. But you cannot possibly get that expansion until the people will borrow, and people are not going to borrow unless they can borrow money to run their factory, to make shirts and hats, and sell them at a profit.

Dr. SPAHR. That is right.

Mr. CROSS. Therefore, they will not borrow.

Mr. SPAHR. That is right.

Mr. CROSS. Therefore, your reserves are doing you no good; therefore you are drowning, where you are now. Now, if you have got some way to tell us to do something and get us out of that condition, that is what we want to know. Just to come in and tell us that we are helpless, we have got to drown, is no consolation to us.

Dr. SPAHR. I have not said that, and I have not implied that.

Now, you have made a point that I would like to make clear. We have had currency. Currency has nothing to do with it now.

Mr. CROSS. When you say " currency ", just what do you mean?

Dr. SPAHR. I mean money and deposit currency.

Mr. CROSS. Do you mean check money?

Dr. SPAHR. I mean all that currency and deposit money.

Mr. CROSS. Well, we have followed up on the check money now.

Dr. SPAHR. By " currency " I mean metallic money, paper money, and deposit currency—it is all currency. Now, the thing to do is to get business men to start, and then they will start borrowing better grade deposits, and then your currency will flow in circulation, and your price will come right up as business expands, and that is what you want. Therefore, your problem comes back to the simple thing of enabling the business men to start. It is not a currency problem, Mr. Cross.

Mr. CROSS. Your school of thought is just the reverse of that of Dr. Warren, and Fisher, and Vanderlip, and Hemphill, and Senator Owen.

Dr. SPAHR. Just the reverse.

Mr. CROSS. They are all wrong, are they not?

Dr. SPAHR. Yes, sir; all wrong.

Mr. CROSS. Absolutely. I thought they were.

Mr. GOLDSBOROUGH (acting chairman). Mr. Hollister?

Mr. HOLLISTER. I do not want to ask very many questions, but we have a specific bill before us, and I want to bring out if I can a little bit more of the philosophy which we are entitled to. What do you conceive to be the purpose of a central bank?

Dr. SPAHR. The fundamental purpose lying back of this is to control currency with the idea that you can generate recovery by forcing currency into circulation.

Mr. HOLLISTER. That is, you say what is behind the bill? What is your conception of what the function of a central bank should be?

Dr. SPAHR. The chief function of a central bank should be to extend legitimate credit to commerce, agriculture, industry, and to Government; and by that I mean, when I say " legitimate ", I mean appraising the collateral that is offered accurately and then substituting its own credit, which is generally acceptable, for that of the borrower's, which is not. Now, that means an avoidance of inflation. That is what a bank is for, merely to substitute its credit, which can be used widely and generally, so that you can draw checks, so you can carry on your exchange without inflating your currency.

Now, that means if that is done the institution must be free to do just those things, which means it cannot be subjected to political influences and be made to accomodate a government. Now, in this bill is the notion that the Government credit should be favored, it should be given a special rating. The only real test we have of the validity and the soundness of Government credit is for the Government to go into the open market like every other borrower and ask terms. Therefore, it is not proper for a central bank to give an artificial rating or to provide an isolated market for Government securities. Therefore, it forces us back to this point, that any independent bank, to perform its functions properly, must be so constituted that it can do it, and that means it must be free to act as an independent agent. It provides our chief medium of exchange. It enables business men to go on about their business and to carry on their exchange freely and without disturbance. Now, that philosophy is not in this bill.

Mr. HOLLISTER. What do you read into the philosophy of this bill?

Dr. SPAHR. A belief that a Government body can regulate the price level as it sees fit, and that it can put currency in circulation as it sees fit and get a sound rise in price level when it chooses, whereas as a matter of fact it will give an unsound rise in price level because it will be the result of an inflation; and then also, that it can do something to prevent a collapse after the currrency has been inflated, whereas the experience of the world is that once you have inflated a currency there are only three possible results. If you stop inflation at any point there will be a collapse, or if you wish to avoid that collapse, the thing to do is to inflate right on to the bitter end, to avoid the collapse; then you will reach repudiation. In between those you have another. You can inflate up to a certain point, as others do, for example, and then you can leave your people in doubt for say a period of a year or more as to what you are going to do sometime, so as to let prices become stabilized there, and then you will have to devalue in order to peg things right where they are.

France, Italy, and Belgium did that. Italy was not very wise in the way she did it. Now, those are the only three things you can expect if you inflate.

This bill has lying behind it the philosophy that some Government board can raise the price level by raising the currency and then avoid any one of those three consequences, and the lessons of the world are that it cannot be done.

What we need is to let prices come up normally and naturally, and that forces us back to this point, that there is nothing that needs to be done at this time. We have more currency than we need, that is available. All we need to do is to let it be drawn into circulation, and it should not come until business can again use it soundly. No man has any business borrowing unless he can repay. There is no such thing as forcing currency into circulation on any sound method whatsoever that is known. You cannot do it.

Mr. GOLDSBOROUGH. I know you say you cannot do it, but what proof have you from any stable government, that it cannot be done?

Dr. SPAHR. You will inflate if you do.

Mr. GOLDSBOROUGH. When did it ever happen that a stable governmen went to pieces through inflation by issuing its own money to pay its own obligations at a time when it was in a condition of depression?

Dr. SPAHR. Of course, a government like that is not stable. That is the point of your question.

Mr. GOLDSBOROUGH. Oh, well, that is begging the question.

Dr. SPAHR. A government that would do that is not stable. I know of no stable government that would do it. Now, our Government is fairly stable, and still we collasped in 1929 as a result of inflation. That was bad enough.

Mr. GOLDSBOROUGH. We collapsed in 1929 because we deflated when we were on a stable basis. We deflated in 1920. That is what happened.

Dr. SPAHR. That illustrates the point I made a moment ago, Mr. Goldsborough.

Mr. GOLDSBOROUGH. And we cut the stability out of our monetary system at that time, and then when we began to try to creep back. What happened was that from 1924 to 1929 we went into a period of speculation and the Federal Reserve System did not know what to do with it; and they finally acted to raise rediscount rates, and that actually caused the collapse of the New York stock market; and in view of the fact that the whole country was in the New York stock market it just stopped the whole machinery right there. That is what happened.

Dr. SPAHR. I would answer that this way, that apparently stable price level from 1924 to 1929 to an illustration of the point I was trying to make to Mr. Cross, that a stable price level that is maintained by artificial means when your economic system is not in a state of economic equilibrium is a dangerous thing, because it was supported by inflation and the underpinnings gave way in 1929, which ought to be conclusive proof that a stable price level under and conditions is not a thing that can maintain itself, and you cannot maintain it. That price level from 1925 to 1929 was supported to a large degree by inflation, and the reason of that was that we tried to avoid the maladjustments or readjustments which the war had created. Therefore, we bolstered up that thing with every device we could think of.

Mr. GOLDSBOROUGH. Was not the first mistake made in 1920 when the deflation took place?

Mr. SPAHR. Our reserves were exhausted in 1920. That was a different system the Federal Reserve banks had to pick up.

Mr. CROSS. You mean they had to do it?

Dr. SPAHR. They had to do it. They had to; yes, sir.

Mr. GOLDSBOROUGH. In other words, we had money of so little use that we were not in a position to expand it further in order to maintain the stability of our price level and the stability of business, and is not that a situation bound to be created under this gold standard you are talking about?

Dr. SPAHR. Yes; but the reason for that was that we had inflated so much prior to 1920 that our reserves could not stand it, and we reaped the consequences of inflation again. That is why I am arguing so strongly against inflating again. The experience after 1920 illustrates it. The one at 1929 illustrates it.

Mr. GOLDSBOROUGH. You agree with me that we were in good shape in 1920, and that if we could have continued without inflation we would have been all right; do you not agree on that?

Dr. SPAHR. But we could not continue, because we were inflated.

Mr. GOLDSBOROUGH. We could not continue because we did not have the money. That is what you mean, is it not?

Dr. SPAHR. That is always the case when you are inflated.

Mr. GOLDSBOROUGH. We did not have the money?

Dr. SPAHR. We did not, but that is always the case when you are inflated, you do not have the money.

Mr. GOLDSBOROUGH. You think that for the Congress to exercise the prerogative to create its own medium of exchange, in order to maintain the stability of society, would be wrong and a "forgery"?

Dr. SPAHR. Yes, sir.

Mr. GOLDSBOROUGH. All right.

Dr. SPAHR. May I define that term "forgery", Mr. Goldsborough, for you?

Mr. GOLDSBOROUGH. Well, you defined it pretty well in your article. If you desire to do it again it is all right with me.

Dr. SPAHR. I used that term. It is from the dictionary.

Mr. GOLDSBOROUGH. No; you went further than that. You defined it, too. I read what you said. You reflected very greatly on me personally in this statement you made. Now, what you said was this:

> Mr. Goldsborough proposes to have the Government pay off these investors, not by money raised through borrowing or taxation, but by means of paper money printed by the Government. Such money is in the nature of forged notes, forged by a Government against its people. He is asking the Government to go into the business of forging notes. If in his private affairs a man borrows at a bank or elsewhere, then finds them calling it, and gives a forged note or a changed note, in settlement, he is put behind the bars.
>
> We demand that he live up to his contract and that he get the wealth with which to pay his debt. We do not allow him to issue forged notes or to set up a printing press and run off the necessary amount of notes with which to pay his debt.
>
> In simple and accurate terms, this is exactly what Mr. Goldsborough and several others in Congress are proposing to do. Elected to high office to legislate in behalf of the people, they are devising schemes to forge notes against the people of this Nation and to defraud them of their savings.

Now, if you want to give a different definition from what you have given in this article, that is up to you.

Dr. SPAHR. It is not different. I want to show how accurate it is. This is the dictionary definition of "forgery" which I used there:

> Forgery—the act of feigning; fiction. A common form of forgery is the false making and signing of evidences of debt as notes.

That is what your issue of paper money is.

Mr. GOLDSBOROUGH. Do you mean to tell me that a sovereign government, even aside from what is in the Constitution of the United States, has not a right to issue its own medium of exchange?

Dr. SPAHR. I did not say it did not have the right, but I said that is what it is doing.

Mr. GOLDSBOROUGH. Do you mean to say it is forgery when a sovereign people does that?

Dr. SPAHR. Yes; exactly. That is what I mean to say.

Mr. WILLIAMS. Were all the "greenbacks" forgeries?

Dr. SPAHR. Yes.

Mr. GOLDSBOROUGH. And the only way that a government, which has behind it as its resources the wealth of all the people, could get money would be to borrow it from some bank?

Dr. Spahr. No. When the government is set up, it is presumed that the government will raise its funds in two ways—either by borrowing or taxation. That is what is always presumed. Now, when it turns around and prints paper money, which is a promise to pay money, and it has no intention of paying money, it comes under this definition exactly. Let me read it again:

A common form of forgery is the false making and signing of evidences of debt as notes. That which is falsely devised, or counterfeited.

The Chairman. I think Mr. Hollister desires to ask a question.

Mr. Hollister. I yield to Mr. Ford. I do not mind who asks the questions, but just let him finish.

The Chairman. Mr. Ford.

Mr. Ford. In your opinion, President Lincoln and the Congress of the United States committed forgery when they issued the "greenbacks"?

Dr. Spahr. Yes; that is right.

Mr. Ford. They did, they committed forgery?

Dr. Spahr. Yes. I use that term for the reason it is accurate, but is not the common one we use in every-day life.

Mr. Goldsborough. No; but you use it as comparable to the man who forges a paper in private business?

Dr. Spahr. Yes.

Mr. Goldsborough. That is the way you used it in this article?

Dr. Spahr. Yes; because I wanted the public to see that your plan is exactly that, except that you are doing it in the name of the people of the United States.

Mr. Goldsborough. Well, I say, your contention is that the only way for a soverign people to get their medium of exchange is to borrow it from one of the soverign people?

Dr. Spahr. Or from taxation.

Mr. Goldsborough. In spite of the fact that the Government has as its resources to pay off the obligation that it issues, all the wealth and all the resources of all the people of the United States?

Dr. Spahr. I am not talking about the power of the Government. I am talking about the nature of the transaction.

Mr. Cross. "Honesty."

Mr. Goldsborough. Well, whoever heard before that it was dishonest for any Government to issue its own medium of exchange?

Dr. Spahr. That is what I am trying to make clear, that it is. The people ought to understand it.

Mr. Cross. Does he think President Lincoln and the Members of Congress at that time ought to have been sent to the penitentiary when they enacted that law?

Mr. Hancock. May I inject one question, Mr. Chairman?

The Chairman. Certainly.

Mr. Hancock. Do you maintain that a Government like the United States under its soverign power cannot legally and validly issue its notes against future taxes?

Dr. Spahr. No; it can do it.

Mr. Goldsborough. You have just said it is forgery to do it.

Dr. Spahr. It is.

The Chairman. Dr. Spahr, let me make you a suggestion. I want to help you out. I think you have made an extreme statement when you attempt to attach to the act of a sovereign government in issuing money the elements of legal forgery as a crime. You are not a lawyer, are you?

Dr. SPAHR. No.

The CHAIRMAN. If you will read the law on forgery——

Mr. SPAHR. Pardon me—I qualify that. I am something of a constitutional lawyer. I used to teach constitutional law.

The CHAIRMAN. I mean if you will study the law of forgery, while I think I know what was in your mind in making the statement, I think you will agree that probably your language is not well chosen to convey the idea you have in mind. In any event, I do not desire to take any time. If you gentlemen are through questioning the witness I should be glad to have Mr. Hollister resume his discussion.

Mr. GOLDSBOROUGH. I want to say this, because I do not want any misunderstanding about how I feel about it. I want to say that when a man says that I am engaged in a business or in conduct which is equally culpable with forging a note as a private citizen, which is a crime for which imprisonment is provided, I say it is a very personal reflection, and that is the way I regard it.

Dr. SPAHR. I am sorry, Mr. Goldsborough. I am interested only in the welfare of the country, as I presume you are, and not concerned with personalities at all.

Mr. GOLDSBOROUGH. Well, that is what you engaged in, all over the country, and you got this article in the subsidized press all over the country. Of course, you did. That was for the purpose of discrediting me; it could have been for not other purpose.

Dr. SPAHR. No; to discredit your plan.

Mr. HOLLISTER. You mean when you say that such a note issued by the Government is a forgery that it is really a fraud on the person who is asked to take that piece of paper as something of value?

Dr. SPAHR. Exactly.

Mr. GOLDSBOROUGH. Even though the purchasing power is just as good as any other obligation or any other piece of money?

Dr. SPAHR. But it is not.

Mr GOLDSBOROUGH. Well, the Supreme Court did not agree with you, I will say that. I only want to call attention to the fact that you and the Supreme Court are not in agreement at all on the value of money issued by the Government.

Dr. SPAHR. I never questioned the legal capacity of the Government to do it; never questioned it. I was merely pointing out the nature of the transaction. Governments frequently do it. All of them have done it, I presume, but they defraud their people when they do it.

Mr. CROSS. I just want to ask this, because I feel somehow as if there is a reflection there that ought not to be in the record. Maybe you have some explanation. Of course, forgery is stealing, is it not?

Dr. SPAHR No. I used the definition I read you there.

Mr. CROSS. I am an old prosecuting attorney, and you say you are a constitutional lawyer, and if you know anything about the law, forgery is stealing of the worst type. Now, you say that President Lincoln and Congress committed forgery, and you say they committed theft, they stole, and I do not think that that slur ought to be left on the memory of those men.

Dr. SPAHR. Mr. Cross, the definition I used is this one. I did not use the one you say.

Mr. CROSS I am not talking about definitions. You said you thought that all of them, President Lincoln and the Congress that issued that "greenback" money to save this country when it was sinking, and was helpless to save its life—you say that they committed forgery, and forgery means stealing, if you will go and look in any law book, and if you know anything about law.

Dr. SPAHR. I used "forgery", Mr. Cross, as I defined it. I cannot permit you to put words into my mouth.

Mr. CROSS. You are putting words into your own mouth, that they committed forgery.

Dr. SPAHR. And this is forgery, according to the definition as I used it, and I put it into that letter that I released. This is the same thing that I have used: A common form of forgery is the false making and signing of evidences of debt as notes." The "greenbacks" were promises to pay money. It said that on them.

Mr. FORD. How about the bank which issues a check when the amount is 10 times in excess of its reserve and it cannot pay it when there is a demand. Is that forgery?

Dr. SPAHR. No; not at all.

Mr. FORD. Oh, the bank has got $2,000,000 in reserves, and they have got outstanding obligations, 10 times the amount, and that is not forgery?

Dr. SPAHR. No.

Mr. FORD. Under your definition?

Dr. SPAHR. They have assets against those which can be liquidated for cash to meet those checks if the reserves will not.

Mr. FORD. Is a $2,000,000 reserve an asset against $10,000,000?

Dr. SPAHR. Surely.

Mr. FORD. Or $20,000,000?

Dr. SPAHR. Surely, it is an asset.

Mr. FORD. Suppose it were demanded immediately?

Dr. SPAHR. Then the bank would have to sell its other assets to get enough to meet the deposits.

Mr. FORD. Supposing they could not?

Dr. SPAHR. Then the bank would close up.

Mr. FORD. Then they would not have committed a forgery?

Dr. SPAHR. No; they would have engaged in bad banking.

Mr. FORD. Oh, I see. Then the United States Government would not be engaging in bad practice—it would just be committing forgery—a distinction without a difference.

Mr. CAVICCHIA. What I have in mind, Profesor, is this, that Germany when she started her inflation had practically made the people of Germany and of the world believe that all the resources of the national government were behind those notes, those marks. Isn't that a fact?

Dr. SPAHR. Yes; that is right.

Mr. CAVICCHIA. And later she practically repudiated her internal debt because she could not meet her obligations?

Dr. SPAHR. That is right.

Mr. CAVICCHIA. In that sense you use the word "forgery", that was a forgery against the people? Am I correct?

Dr. SPAHR. That is, the mass of people. That is right.

Mr. CAVICCHIA. And you are using it, I take it, in the same sense?

Dr. SPAHR. Yes; that is right.

Mr. CAVICCHIA. If the United States were to issue billions and billions of dollars in paper money——

Dr. SPAHR. That is right.

Mr. CAVIACCHIA. And then this inflation would grow to such an extent that it could not meet its obligations, it would be forced to do the same thing that Germany and other nations that engaged in inflation have come to, repudiation?

Dr. SPAHR. That is right.

Mr. CAVICCHIA. That is right. I pointed out that inflation always leads to one of three results, all of which mean losses, and your government is causing them. In other words, it is causing you people to take those losses, which is defrauding them of their accumulated wealth. It may be repudiation; it may be devaluation; it may be a collapse in the market, all caused by inflation.

Mr. HOLLISTER. Mr. Chairman, I am not interested in terminology; I am trying to bring out the witness' views as to the philosophy of this bill and what may be accomplished by it, and I am interested in what is the proper philosophy and proper function of a central bank. That, after all, is what this committee is trying to decide. Whether or not it is fair play to use the term he used and another gentleman took another term I do not believe would be very material to what we are trying to get at here.

This bill gives the power in the Open Market Committee to compel the Reserve banks to acquire Government securities without any limitation whatsoever, merely by orders of the Committee. Would you comment particularly on that phase and possibility of it?

Dr. SPAHR. Yes; It is not the function of a central banking system to be forced to absorb Government securities. The Government should have to go into the open market to borrow its funds, just as any other individual has to go there. Therefore, if a banking system is so constructed that a government can force the bank to absorb the debt, what is happening is this: The government's deficit is being made an asset of a bank against which deposit currency is being issued. That is an unsound inflationary procedure. No new wealth is being accumulated. No new reserves have been added to the system. But you are pumping additional deposit currency into circulation as a result of the government activities.

Now, the function of a government in raising funds is to simply go into the market and borrow and transfer a corresponding amount of funds from savers to the government. Then your currency system is undisturbed. By that I mean either borrow or tax.

When you set up a banking bill like this that is going to enable the Government to go into your banks and put the deficit into the banks as assets and then create deposit currency, of course you have just started a spiral of inflation there which can just go without limit.

Let me remind you, Germany never issued any currency except against the government securities. There is no limit to what you can do with this if the government chooses to do it, but you can do it for quite a while before the public is aware of it. If you issue paper money, fiat money, as proposed by the Patman bill, for example, there is likely to be a very quick psychological response there, because it is fiat money rather than money issued against bonds. But you can go for two, three, four years probably, probably longer, by issuing deposit currency against bonds, or even currency against bonds, and the public will not detect, will not be concerned as to what is going on, until it gets released, and then the dam breaks.

There is that difference, of course, between that type of inflation creating currency against governmental bonds and an outright issue of fiat money. We all have to recognize that. One is a little slower than the other.

Mr. HANCOCK. Suppose those bonds are issued against gold reserves; will they be fiat money, too?

Dr. SPAHR. No; not at all. It is just an expansion of your currency.

Mr. HANCOCK. That is my veiw exactly.

Dr. SPAHR. An expansion of currency and inflation are two different things.

Mr. HANCOCK. I have always appreciated the real difference.

Mr. GOLDSBOROUGH. You mean to say the accident of somebody's production of gold out of the ground creates a healthy expansion, whereas if it is done in another way it is inflation? Is that what you mean?

Dr. SPAHR. Yes; because the currency is self-liquidating. Nothing can ever happen to it. Your prices, though, will go up, tend to. But there is nothing there that will not liquidate itself, because it is gold, gold certificates.

Mr. GOLDSBOROUGH. What value is there in gold except the imaginary value that was first created in the minds of our ancestors when they began to use it as a medium of exchange?

Dr. SPAHR. It is not an imaginary value, Mr. Goldsborough. It is a thing that satisfies human beings that have doubts about the currency. That is, it is universally accepted. When they have doubts about the currency they rush to get gold.

Mr. GOLDSBOROUGH. When you say "people" what kind of people do you mean?

Dr. SPAHR. Intelligent people of the United States.

Mr. GOLDSBOROUGH. I have never heard anybody except some banker make the statement that you are making now.

Dr. SPAHR. I think the finest evidence in the world of that is the fact that we had the greatest hoarding episode in this country in 1932 and '33 that was ever seen in the history of the world.

Mr. HANCOCK. You regard as a contributing circumstance the money that was outstanding, don't you?

Dr. SPAHR. No; I regard it as supporting my theory that in times of stress people will rush for the thing in which they have confidence.

Mr. HOLLISTER. Which is really an unsound habit of the people, to shift confidence completely in a time like that.

Mr. HANCOCK. May I clarify that—why would a man want to put anything away that was not worth something? Hoarding was act of confidence in the soundness of our money. They knew this Government would always keep it good and sound.

Dr. SPAHR. He would not.

Mr. HANCOCK. Why, of course he would not.

Mr. CLARK. I do not know what the parliamentary situation is, Mr. Chairman, but sometime along here I would like to ask some questions.

Mr. HOLLISTER. My possession of the floor is purely hypothetical.

Mr. CLARK. I understand so but I do not want to break into your train of thought. However, if we do not break in we will never get in.

I just want to ask Dr. Spahr: Did you ever hear of or read the testimony of Governor Eccles before this committee?

Dr. SPAHR. Only the newspaper reports.

Mr. CLARK. You know, so much misunderstanding comes from misunderstanding. I think you might well read it. I have studied your statement with some care as to the language used, and I believe you have, if I observe your statements correctly, a false conception of his philosophy of money.

Dr. SPAHR. I based it on his testimony of 1933 before the Senate Finance Committee, which I read in detail.

Mr. CLARK. On page 2 you make this statement:

Title II of the banking bill of 1935 is particularly dangerous when viewed in its entirety, because it is a manifestation of the unsound philosophy held by some officials of this administration regarding the causual relationships existing between the supply of currency on the one hand and taxes, recovery, and prosperity on the other.

I want to state to you this, that if you will read Mr. Eccles' statement before this committee—and I am not familiar with his other hearings—you will find that he denied that casual relationship. In answer to a question from Mr. Cross whether, if he were given this power in the Federal Reserve Board, he could bring about stable prices, full employment, and business stability, he specifically stated that the money system alone would not enable him to do that, or the control of the money system.

Dr. SPAHR. I saw that in the paper, but that is directly contrary to his testimony of 1933.

Mr. CLARK. I will go into that in a minute. Did you go into the reasons why that could not be done by the control of the money system?

Dr. SPAHR. I would not attempt to hold him responsible for a newspaper report. I could not tell that fully.

Mr. CLARK. He said this: That the most he could do if he had sole control of our money system was to control the volume of money; that is, deposit money and currency. He said:

Control of the volume of money is not of itself sufficient to either fix prices or bring about a condition of employment or business stability.

He used a philosophy factor in there which had to exist, a philosophy of money; that is, the national income or the ratio between the volume of money and the national income. He said he could not control that philosophy of money and to do that he would have to have factors completely outside of the banking system.

Now, I am not asking you whether that is right or wrong, because I am not sufficient of an economist to get into a controversy with you on that power, but I do want to say that I believe if you had read Mr. Eccles' testimony you would have found that he had his feet on the ground and that statement of his philosophy here at least at this time is not justified, and that is where so many of our misunderstandings arise.

Now, you made this statement——

Dr. Spahr (interposing). I am sorry; may I interrupt?

Mr. Clark. You certainly may.

Dr. Spahr. I have some excerpts from his 1933 statement which will support my statement. In the 1933 report, page 75, he points out that—

This recovery can only be brought about by providing purchasing power sufficiently adequate to enable the people to obtain consumption of goods which we, as a Nation, are able to produce.

Of course, that is only part of it, but that thought runs all through.

Mr. Clark. And that is just the point he made here, Doctor, that the control of a money system could not do it, but that you have to balance with that an income-tax program and a program of long-range Government spending.

Now, your suggestion here is that the drafters of this bill—and Governor Eccles takes the chief responsibility, or did take it—that he believes that by control of money he can do this, and you will note in his own statement that he says that he believes that that will not do it, but that you will have to put the purchasing power in the people, and he wants to do that in several ways, which it is not necessary to go into.

Dr. Spahr. I think you will be interested in this. While this is from the newspapers and perhaps is not accurate, I notice he says, "the question of velocity and supply of money relates to the national income."

Mr. Clark. That is true.

Dr. Spahr. And he pointed out, from the newspaper account, that the velocity was fairly steady.

Mr. Clark. No; quite the contrary. He had charts here which showed that that velocity dropped an enormously greater amount during the depression than did the supply, and he had graphs here to illustrate that very point.

Dr. Spahr. Yes; that is true.

Mr. Clark. Yes. That is what he said, and he had graphs here.

Now, the whole tenor of your statement here, in my humble judgment, is a difference of viewpoint, if I may say it, to be mild, with the philosophy that, honestly, Doctor, I do not believe you understand. I believe if you will read Governor Eccles' statement you will get a better idea of what he really thinks now.

Dr. Spahr. May I ask, to enlighten myself——

Mr. Clark. Yes.

Dr. Spahr. According to newspaper accounts, he related the supply and philosophy to national income?

Mr. Clark. No. He said that the philosophy of money was determined by the ratio between the supply of money and the national income.

Dr. Spahr. That is the point.

Mr. Clark. That is, how fast the money moves.

Dr. Spahr. That is false.

Mr. Clark. Well, now, that may be false; but he never said, as you say here, or he never intimated to this committee, I think, that the volume of money itself and its regulation, which is all under this bill that the Federal Reserve Board could ever control, could be used as an instrument, of itself, to raise or lower prices.

Dr. SPAHR. Do you know that that statement by Mr. Eccles, as I got it from the paper and as you confirmed it, was almost identical, even to the figures, to one that was published by Mr. Hempfield? As I understand it, he relates currency supply and velocity to national income, whereas, as a matter of fact, there is no relationship that is known. Now, if that were true——

Mr. CLARK (interposing). Of course, there is not. There is no way of controlling it.

Dr. SPAHR. Now, if that were true, if you increase the the supply of currency as they did in Germany, the national income would go to preposterous heights, whereas the people would be impoverished when the income went down.

Mr. CLARK. That is the point; from that we conclude that you cannot increase the velocity or diminish the velocity merely by increasing the supply.

Dr. SPAHR. Yes; you can. That is false. If you inflate the currency, the velocity of course will be terrific.

Mr. CLARK. I think not. I think that when the volume of money remains practically the same—well, it will not remain steady, but reasonably steady—the velocity decreases enormously.

Dr. SPAHR. The velocity would depend upon whether the currency is sound or unsound. If you inflate the currency, of course, the velocity will be terrific.

Mr. CLARK. He says he is not an inflationist. He laughs at inflationists. He laughs at the people who call him an inflationist.

Dr. SPAHR. All I ask is that you compare his present testimony with what he said in 1933. He has changed his mind, perhaps.

Mr. CLARK.. Not from what you read. Well, now, one more question: You said here on page 6—am I taking too much of your time, Mr. Hollister?

Mr. HOLLISTER. No. Go right ahead. You are bringing out just the point I wanted to bring out.

Mr. CLARK. You say this on page 6:

> This section of the bill—

referring to section 203—

> is either subtle or stupid. In any case it is dangerous. It reveals how far removed its drafters are in their notions of how to constitute a central bank board from those who would profit from experience.

Now, of course, that is a general statement, but I do want to ask you this, in all fairness, Doctor, inasmuch as you have not familiarized yourself with Mr. ECCLES' testimony here: Do you know anything of Mr. Eccles' history?

Dr. SPAHR. Yes; I do. That statement is very specific. It is based on the exact statement that Mr. Eccles made in 1933. That statement links the Federal Reserve Board to the planning agencies. This is what Mr. Eccles said in 1933 in those hearings, on page 731:

> A national planning board similar to the Industries Board during the war is the necessary and proper coordination of public and private activities of the economic world.

If you go through his testimony you will see that he wanted the whole money and the banking system related to that, and that is why I made that statement.

Now, that clause, that sentence, is in this bill. So I say if it is put in there inadvertently it had better be watched. It may have been put in there out of a determination or intention to use it. Anyway, it is in perfect harmony with what he said in 1933. Now, that is my reason for stating that. Perhaps he has changed his mind.

Mr. CLARK. But it is possible that he may have thought that he was profiting from experience. Of course, you realize that Mr. Eccles is one of the country's most successful, hard-headed business men, do you not?

Dr. SPAHR. Yes, sir.

Mr. CLARK. You realize that?

Dr. SPAHR. Yes, sir.

Mr. CLARK. You realize he is not a theorist. That is, at least if he is a theorist he has had an exceedingly successful career in the banking field.

Dr. SPAHR. I know many of his very intimate friends. I do not know him personally.

Mr. CLARK. Well, he is a fine gentleman. Now this is my last on this: You were saying, referring to 203, subsection 3,

> It reveals beyond the shadow of a doubt the purposes of the authors of this bill. They propose to convert the Federad Reserve System into a political instrumentality of the party in power. This section of the bill clearly reflects the author's motives and concepts regarding central banking.

Of course, that is a direct challenge, Doctor, to the motives of Governor Eccles, not to his theories. Many people on this committee disagree with his theories. Some people I think disagree with all of them. But I do not think anyone on the committee challenges his motives, to the extent at least of calling him—and I think it is true—a political shark. Now, why do you question his motives?

Dr. SPAHR. His motive is to make it a political institution.

Mr. CLARK. You say his motives are to create a political instrumentality of the party in power, and I want to know why you think that.

Dr. SPAHR. Because every line in title II does that thing. His testimony of 1933 indicated he wanted to do it.

Mr. CLARK. All right, now; as I understand, you propose to turn this over to a commission. That is your suggestion, the constructive suggestion in your statement?

Dr. SPAHR. Yes.

Mr. CLARK. Who would appoint that commission?

Dr. SPAHR. I think this committee, followed up by the Senate.

Mr. CLARK. Any commission, in order to be a fair commission, would have to represent very divergent views?

Dr. SPAHR. Yes; I think so.

Mr. CLARK. Now, can you imagine a committee on this question ever coming to any conclusion as to what part of a banking bill should be written?

Dr. SPAHR. It has been done in the past.

Mr. CLARK. On a matter of this kind?

Dr. SPAHR. We had a National Monetary Commission in 1911.

Mr. CLARK. Ah yes; but there never was the controversial question about overhaling the entire money system then as we have now.

Dr. SPAHR. We had the McMillan Commission in England that drafted the plan for England.

Mr. CROSS. That commission never got together in England, Doctor. They all disagreed.

Dr. SPAHR. They evidently could not, because of the circumstances that followed immediately after. But my point there, Mr. Cross, is this, that any Member of Congress has a thousand and one things thrown at him. He has to be an expert on everything, and he just simply does not have the time. He cannot possibly do it. Now this is the most technical, most sensitive machine we have in our economic system, I suppose. It ought to be studied over a period of a year or more.

Mr. CROSS. This committee has held hearings for years and years and years and had at least a great many of the experienced bankers, a great many of the outstanding—of course, you say they are not outstanding unless they hold views along your line, but we have had all kinds of those here. We have had the leaders of the great agricultural organizations, and we have had men from all the different parties. When in the name of God are we going to get down to where we are going to do anything? The members of this committee, it is true, are in Congress and their time is occupied by other question, but we concentrate on one committee, though we may follow these other committees. We divide our time as best we can and study these questions. We do not try to keep up on hundreds of subjects.

Dr. SPAHR. You cannot possibly keep fully conversant with them all, Mr. Cross.

Mr. CROSS. Oh, no; but all you fellows think just like you do. Each one will come in and present his views, and you are more severe in your terms and you call it "baneful"——

Dr. SPAHR (interposing). We do not differ very much. Here are 66——

Mr. CROSS (interposing). Oh, I know, that 66. That makes me suspicious of them, Doctor, when 66 men get together. It looks like there is some big force back of them, when they all say they agree, when we cannot get a dozen of us here who will honestly get together on anything. That makes me suspicious, 66 getting together, and I think there is some kind of influence or power back of those birds. That is the way I look at it.

Dr. SPAHR. May I tell you how it is done?

Mr. CROSS. No.

Mr. HOLLISTER. Tell me.

Dr. SPAHR. I submitted a tentative draft of title II to the members—and there are 95—and asked them to criticise and to draft what they felt was the right thing to do. There were only 66 we could reach. I got those back, I dovetailed them together and sent them out again for any other corrections they cared to make, and then I sent them again and asked them if they would authorize their names to be used on that release. Some approved outright. Most of them approved it outright. Some approved it with reservations, and we published that with each man's authorized signature.

Now, there is no pressure. We cannot put the pressure on anybody. We cannot use a man's name unless he approves. That is as open and above board as anything we can have. You could not buy one of those men. You could not persuade them under any circumstances. Now, I believe that that opinion of 66 is worth something.

Mr. HANCOCK. You are the secretary of that committee?

Dr. SPAHR. I am the secretary.

Mr. HANCOCK. Is Mr. Sprague a member?

Dr. SPAHR. Mr. Sprague is a member of the executive committee.

Mr. HANCOCK. And Mr. Parker Willis?

Dr. SPAHR. Mr. Parker Willis is on the executive committee.

Mr. HANCOCK. You have studied under Mr. Willis, have you not?

Dr. SPAHR. Yes; I have.

Mr. HANCOCK. Is it not a fact that you and Mr. Willis, both, Doctor, have consistently been political opponents of everything that has been proposed by the "new deal" since Mr. Roosevelt was inaugurated?

Dr. SPAHR. No. I said this morning that I approved a tremendous amount of things that this "new deal" has done.

Mr. HANCOCK. Have you not written a number of articles and issued a number of pamphlets criticising most of the financial policies that this administration has inaugurated since it came into power?

Dr. SPAHR. No; I don't think so. This committee is a money and banking committee. This committee was formed with the original idea of helping the President if he would permit them.

Mr. HANCOCK. And you feel that you have been helping the President?

Dr. SPAHR. Certainly; because we stood for sound money and banking.

Mr. HANCOCK. President Roosevelt does, too.

Mr. GOLDSBOROUGH. You say "Every member of this committee." Do you mean to say that every member of this committee would say that a government is guilty of robbing its people and guilty of forgery when it issues its own money to pay its own obligations to its own people?

Dr. SPAHR. No; that statement was issued on my responsibility, not in the name of the committee.

Mr. GOLDSBOROUGH. Well, let us go back and see whether you mean what you say. If an individual creates money in this country without the authority of the Government of the United States, he is guilty of forgery.

Dr. SPAHR. That is right.

Mr. GOLDSBOROUGH. The only authority to issue money, to the banks or anybody else, is authority given them by the Federal Government. Then why do you say that when the Federal Government gives a bank the right to expand its money 10 times, and it does it, that is good money, but when the Government, that gave the authority to the banks, undertakes to issue its own money it is forgery and bad money?

Dr. SPAHR. When a bank issues money it issues against assets, which is something which is payable, a promise to pay that is good. Perhaps it is the Government's own bonds, but it is a good asset.

Mr. GOLDSBOROUGH. When the bank isues money through the Federal Government, it issues it on the Government's bond, which is nothing in the world but the Government's credit. Now what is the difference between the Government's issuing the Government's credit to a bank and getting the money from the bank, and issuing the money directly?

Dr. SPAHR. There is as much difference as night and day.

Mr. GOLDSBOROUGH. But what is it?

Dr. SPAHR. When the Government issues fiat money it has no intention of paying it, there is no provision for paying it, and it is payable on demand and there is no reserve there to meet it. Now, a bond is an interest-bearing obligation and it is sold to the people. The people turn over their savings, or the banks turn over their savings created by deposits, to the Government.

A bond is evidence of a debt that bears interest. As a consequence it is not payable on demand. It is payable at some definite future date. It is an entirely different proposition.

Mr. GOLDSBOROUGH. The Government is not limited in the amount of bonds it can issue.

Dr. SPAHR. Certainly not.

Mr. GOLDSBOROUGH. It is not limited. It can issue bonds indefinitely.

Dr. SPAHR. Certainly not; that is true.

Mr. GOLDSBOROUGH. Is that forgery?

Dr. SPAHR. No; not necessarily. "No" is the answer.

Mr. GOLDSBOROUGH. Now, then, tell us this: The Government issues, I will say, $100,000,000 worth of bonds and sends those bonds to the Chase National Bank. The Chase National Bank gets some bookkeeper that it pays $25 a week to make a credit on its books in favor of the United States Government for $100,000,000, which means that the bank, if it is doing business profitably, has already loaned to private interests much more than its entire capital and surplus; it has already done that before it begins to operate on the Government at all, so when the Government sends its bonds to the Chase National Bank, the Chase National Bank actually has nothing at all left. It has already loaned more than its capital and surplus. The Government sends it bonds down there and gets this book credit, which means that the bank, which has nothing, loans the Government, which has everything, $100,000,000, and the Government loans that money back to the bank and then proceeds to pay it interest on it.

Do you mean that that is a business proposition, or is it a racket?

Dr. SPAHR. It is an inaccurate statement.

Mr. GOLDSBOROUGH. How is it inaccurate?

Dr. SPAHR. Because when the Government sends the bonds to the bank or the bank buys them, the bank has to maintain legal reserves against the deposit which is created. The law requires it.

Mr. GOLDSBOROUGH. One-tenth reserve, of course.

Dr. SPAHR. All right; the law requires that. That is an asset.

Mr. GOLDSBOROUGH. I would say so.

Dr. SPAHR. When the Government issues paper money it has no reserve against it.

Mr. GOLDSBOROUGH. It has the reserve of every resource in the country, including the banks' resources.

Dr. SPAHR. Nothing at all.

Mr. GOLDSBOROUGH. Oh, yes, it does. It can tax the banks, or any individual, or any corporation, or any business to the extent necessary to carry on its finances.

Dr. SPAHR. But it does not when it issues fiat money.

Mr. GOLDSBOROUGH. Oh, yes; that fiat money, as you call it, is redeemable just as much as any other money. You would have to redeem it with some other kind of money that the Government issues, just like you would have to redeem any Government obligation by some sort of money that the Government issues.

Dr. SPAHR. But the point is the bond is presumed to be payable at a certain date in money that is universally accepted by the people. But paper money——

Mr. GOLDSBOROUGH (interposing). Has anything happened in this country since the Government decided to abrogate the gold clause? Has that caused any terrible condition in this country? Has anything happened?

Dr. SPAHR. No; but that is merely a temporary situation. It can happen.

Mr. GOLDSBOROUGH. What is temporary?

Dr. SPAHR. The maintenance of a fairly stable price level and fairly stable foreign-exchange rates and good credit conditions. That can continue for 2, 3, 4, 5, or 6 years. Nobody knows.

Mr. GOLDSBOROUGH. You mean that the Government has got to resume the statement that it is going to pay in gold these bonds in order to permanently maintain the Government's credit, when everybody knows that the money is not in existence to redeem the bonds?

Dr. SPAHR. Yes; to the extent that the time is going to come when the Government is going to have to resume its payments in specie in order to maintain its currency and to maintain its credit.

Mr. GOLDSBOROUGH. The Government now has something over $8,000,000,000 in gold. It has bonds which were formerly redeemable in gold to the extent of about twenty-eight or twenty-nine billions of dollars, right now. What is that gold clause in the bond, except a fraud on the purchaser of the bond, when everybody knows that the gold is not in existence to redeem that bond with?

Dr. SPAHR. That presented no problem until we had to suspend specie payments, did it? You could not pay all your bank deposits, either, in terms of gold, if they were all due at once. The point is bonds are not payable at once. They come due in series. Deposits do not become payable all at once. They come in rotation. That is the reason banks are able to pay out money as loans against deposits, because they know that the gold is merely a clearing fund.

Let me illustrate that another way. There is hardly an economic instrument that you can think of that could carry the load that could be thrown upon it at once. For example, suppose all the Senators and Representatives wanted to use the same elevators at once. They could not possibly do that. The elevators are physically incapable of carrying them all at once, though they can carry the normal number that would use them.

Suppose everybody wanted to use the railroads at once in this country. It could not be done. Suppose everybody wanted to use the airplanes in this country. It could not be done all at once. That is true of practically everything you could point your finger at.

Mr. GOLDSBOROUGH. Yes, but the railroads do not guarantee to carry 120,000,000 people at once; but these bonds do say that they are all payable whenever they are due when we do not have the gold to pay them.

Dr. SPAHR. The railroads have to carry anybody that wishes to ride. They offer themselves to the public. The same is true of our reserves. They support all of the deposits that are created, but it is known from practical experience that everybody is not going to draw at once. Therefore the reserves can be smaller than the deposits, and properly so.

Mr. GOLDSBOROUGH. You are aware of the fact, of course, that the Supreme Court of the United States has said in a very recent case that, in view of the fact that the money the bondholder gets is just as good as the gold, there is no right of action in the Court of Claims?

Dr. SPAHR. Yes; I read that case.

Mr. GOLDSBOROUGH. You think that the Supreme Court is wring, don't you?

Dr. SPAHR. I do not care to comment on that.

Mr. GOLDSBOROUGH. What is that?

Dr. SPAHR. I do not think I should comment.

Mr. GOLDSBOROUGH. You prefer not to comment on the Supreme Court's action, but it is not in line with the contention you have made today, is it?

Dr. SPAHR. I would rather say that your contention is not in line with mine, if I may.

Mr. GOLDSBOROUGH. Well, that is not the question I asked you. Of course, I knew all the time you didn't agree with me.

Mr. HOLLISTER. Dr. Spahr, at the same time, eight members of the Supreme Court said that Congress committeed an unconstitutional act, did it not, when it passed the act of June 25, 1933?

Dr. SPAHR. Yes, sir.

Mr. HOLLISTER. Eight of the nine Justices have said that, merely in different ways. Some of them found that there was no right of action in that particular case.

Mr. GOLDSBOBORUGH. Because there was no loss.

Mr. HOLLISTER. I know, but four judges intimated that. The fifth judge went the whole way and said that Congress had committed a constitutional act, unconscionable though it was. The single judge said that, that is the way a majority against the four was created in that particular case.

Mr. FORD. Dr. Spahr, might I ask you a question with reference to this reserve matter: Assuming that the reserves are good on a basis of 10 to 1 and the Government is going to use gold as a basis; with $8,000,000,000 of gold in its possession could it not still by sound mony issue $80,000,000,000 of obligations against that eight billion on a 10-percent reserve basis?

Dr. SPAHR. If it chooses to do it.

Mr. FORD. Why?

Dr. SPAHR. Because the Government's note issue does not operate the way currency does with the banks. The Government has to stand ready to meet the full amount. Consequently, it is normal for a Government to issue merely certificates and then let the banks hold the reserves against deposits, for the reason that banks will take other types of assets, for instance, the commercial paper, which the Government cannot do.

Mr. FORD. You are assuming that the United States Government has no assets. What kind of an asset is the taxing power of the the Uniter States Government?

Dr. SPAHR. It is not an asset against which it can issue its currency.

Mr. FORD. It is an asset by which it has complete power to tax everything within its jurisdiction.

Dr. SPAHR. That is true.

Mr. FORD. And all the wealth within its jurisdiction. It has that, plus, at the present time, $8,000,000,000 worth of gold. Now, if there is anybody mathematician enough in this crowd to tell me just what the limit of its assets is, I would like to now, under those circumstances.

Dr. SPAHR. There is no limit to the Government's power to tax except the limit of the power of the people to pay.

Mr. FORD. But it is not sound. But it is sound for a bank to issue 10 times its reserves.

Dr. SPAHR. Because a bank would take in liquid assets; but its reserves are not adequate to meet cash demand. The Government is not doing that because it is not doing that class of business. The Government only issues gold certificates and silver certificates, if it engages in the right type of currency issue, and then it supports the banks by putting the certificates on hand for use.

Mr. FORD. I thought we were talking about the basis for sound money?

Dr. SPAHR. We are.

Mr. FORD. Now you say we have got to get back to specie payments.

Dr. SPAHR. That is right.

Mr. FORD. And we have only got to issue $8,000,000,000 worth of money, because we have only $8,000,000,000 worth of gold?

Dr. SPAHR. If those 8 billons could get issued under a banking system, those 8 billions could be multiplied by eight and a half.

Mr. FORD. But that cannot be done by the Government?

Dr. SPAHR. No; not soundly. I am glad you brought that point out.

Mr. HOLLISTER. Will you go a little further than that?

Why can't the Government do it soundly and it can be done by a banking house?

Dr. SPAHR. Because the function of a bank is to take the borrower's paper as an asset. When you create a deposit, of course you have to stand ready to pay out currency if the people want their currency. But the Government requires it to maintain only a 17 or 18 percent reserve.

Now, the Government is not engaged in running a private business. Therefore, it does not take the type of assets that the banks take. The only type of assets it has is either bonds or currency, metallic currency. Therefore, if it attempts to issue any other type of currency it is issuing it against nothing except its taxing power, and of course it does not use its taxing power to redeem that currency. The currency is just outstanding, the way the greenbacks are outstanding, until the Government is ready to resume specie payments.

Mr. HOLLISTER. That was illustrated, and is being illustrated, we might say now, by the example that has been set in the last 2 or 3 years, when the taxing power has run far behind the expenditures of the Government?

Dr. SPAHR. Surely.

Mr. HOLLISTER. I do not want to put the words in your mouth, but will you say whether I am correct or not, with this further explanation: The difference is that the Government is not in the banking business?

Dr. SPAHR. That is right.

Mr. HOLLISTER. The Government could, of course, have a superbank which would be entirely Government run?

Dr. SPAHR. That is right.

Mr. HOLLISTER. But it is not in that business today?

Dr. SPAHR. That is right.

Mr. HOLLISTER. So, therefore, it should not be performing the functions of a bank?

Dr. SPAHR. Yes, sir; that is right.

Mr. HOLLISTER. Unless we want to face the issue and put the Government absolutely in the banking business?

Dr. SPAHR. That is right.

Mr. HOLLISTER. Is that a fair statement?

Dr. SPAHR. That is right.

Mr. GIFFORD. I want to ask you, Dr. Spahr, if the necessities of the hour are sufficient to demand the passage of this legislation.

Dr. SPAHR. I think not of title II. I hope that title II will not be passed, because I know no necessity demanding that.

Mr. GIFFORD. We have to make large borrowings for the Government, and you think the banks will conform to the needs of the Government without any pressure?

Dr. SPAHR. There is ample power in the Federal Reserve Act now for that—too much.

Mr. GIFFORD. What have you to say after reading Governor Eccles' testimony where he stated it would be just too bad for the banks if they did not?

Dr. SPAHR. That implies, of course, the philosophy to which I refer, that there is some way to force banks to make loans. There is always a proper time and place to make a loan.

Mr. GOLDSBOROUGH. What Governor Eccles said was that if the banks did not loan they would probably regreat it, because the Government would assume its own function and issue its own money. That is what he said. I just wanted to explain that.

Mr. GIFFORD. I am satisfied with that.

Dr. SPAHR. So am I.

Mr. GIFFORD. There is a further threat here made before the committee that if any further instrumentalities of the Government are set up to carry on private busines, if business did not assume its legitimate field and bring about a substantial recovery we would be faced with the performance of such threats as that made here. And then there must be a good deal more money diverted from the banks to the Federal Treasury in order to support those, would there not?

Dr. SPAHR. That is right. You are on your road.

Mr. GIFFORD. I want to know when I vote on this bill whether or not the necessities of financing the Federal Government are such as to demand the passage of this bill.

Dr. SPAHR. They are not.

Mr. GIFFORD. Don't you think that is an important consideration?

Dr. SPAHR. It is an important consideration.

Mr. GIFFORD. Have you considered how much Federal financing must be done within the next year and a half possibly?

Dr. SPAHR. The Government should be compelled to resort for its funds to the open market. The banks are taking too much already. The Federal Reserve Act is loose enough now. It can be compelled, and it is being compelled, to absorb too much now. Therefore, to go any further on this line is simply inviting future trouble.

Mr. GIFFORD. I am trying to simplify that in my own mind, and I have suggested if a member bank holds my note for $50,000 it can discount that note and loan me another $50,000, and then discount that again and loan me another $50,000, and it can go on indefinitely, can it not?

Dr. SPAHR. I do not understand that. I am sorry.

Mr. GIFFORD. Well, in order for member banks to finance me—I am not the Government, but if they hold my note for $50,000 they can discount it?

Dr. SPAHR. Yes, sir; that is right.

Mr. GIFFORD. If it is a solvent, liquid asset, and it would be if it is a Government bond. And then it can loan me more money and keep going indefinitely in that way?

Dr. SPAHR. Until the reserves are exhausted; that is right.

Mr. GIFFORD. I want to ask you one other question while I am asking these questions: Did the people of Germany regard their Governmen as dishonest when they took away practically the entire value of their internal debt?

Dr. SPAHR. I cannot say. I would assume they did.

Mr. GIFFORD. Our people might consider we were a little dishonest if we brought about a condition of that sort, would they not?

Dr. SPAHR. I think so. I have talked to a good many Germans who have lived through it, and I presume so. You know what they say about it. What would anybody say if he has his wealth taken away from him and his government is responsible?

Mr. GIFFORD. I would ask you if the terms of this bill would not allow the process I have explained to continue.

Dr. SPAHR. Absolutely.

Mr. GIFFORD. And it does appear to me as giving the preferred place to the Government in financing, but it may be necessary, is what I fear.

Dr. SPAHR. I do not think it is necessary.

Mr. GIFFORD. You anticipate that the banks will have to absorb some 14 billion more? Have you thought of that?

Dr. SPAHR. That is right.

Mr. GIFFORD. And 14 billion—will they have to absorb 14 billion more?

Dr. SPAHR. They may have to under compulsion, as it has been exercised thus far.

Mr. GOLDSBOROUGH. Do you think that the banks want to give up that privilege that they now have?

Dr. SPAHR. I think they would like to.

Mr. GOLDSBOROUGH. Of getting the benefit of buying these bonds?

Dr. SPAHR. I think they would like to loan on legitimate, sound, commercial paper.

The CHAIRMAN. Let me ask you this, Dr. Spahr, on the subject of the loans: What would you have the banks do with reference to Government securities?

Dr. SPAHR. I do not feel that they can do anything. They cannot find good loans to make. They are buying bonds because they cannot find anything else in which to invest to make a small earning.

Mr. GOLDSBOROUGH. I understand you to say a moment ago that they are already holding a much larger quantity of Government bonds than they should hold.

Dr. SPAHR. That is so; they are.

Mr. GOLDSBOROUGH. Then they ought to get rid of them?

Dr. SPAHR. They ought to, but they cannot do anything.

Mr. GOLDSBOROUGH. Then you are mistaken when you say that they should not hold it?

Dr. SPAHR. I say it is a dangerous situation. It is too bad that they do hold them, but they cannot do anything about it under the present circumstances.

The CHAIRMAN. How will they dispose of them if they want to or if they are compelled to?

Dr. SPAHR. That is the interesting thing here, in my opinion. The banks are in a paradoxical condition. They are in a position where they are absorbing notes, and then when business picks up and prices begin to rise the eligible paper comes into the market and prices will fall and then the banks' assets will be reduced in value and the banks will take a terrific lacing.

Mr. GIFFORD. Do not the necessities demand some kind of emergency measure whereby they can dump them into the Federal Reserve?

Mr. GOLDSBOROUGH. You say the banks are taking a lacing?

Dr. SPAHR. Yes, sir; they are.

Mr. GOLDSBOROUGH. How can they be taking any lacing at all; they have not done a thing except put a credit on their books? That is all it has cost them.

Dr. SPAHR. The banks have invested your money and mine in those bonds.

Mr. GOLDSBOROUGH. Well, I don't say whose money they have invested, but the cost of that investment has been negligible insofar as the banks are concerned.

Dr. SPAHR. What any bank does is to take the people's promises to pay, your promise, my promise, or the Government's, as an asset, and create a deposit and say it stands ready to meet that demand on demand in good money, in cash.

Now, to be able to do that the Government requires them to maintain lawful reserves. A bank can only do that to the extent its reserves will permit. The assumption is that those bonds, which are a promise of the Government to pay, can be converted into cash. They are not buying those bonds out of nothing; they are merely substituting their credit.

Mr. GOLDSBOROUGH. Of course they are. They are taking the bonds and making the bonds an asset upon which they issue this money.

Dr. SPAHR. Every time a bank buys a bond its reserve ratio declines, because it creates a deposit.

Mr. GOLDSBOROUGH. Of course it does, but the reason it buys these bonds is because it has reserves that are not working.

Dr. SPAHR. That is right.

Mr. GOLDSBOROUGH. Therefore, I say that it amounts to a gift from the Government in bonds.

Dr. SPAHR. No.

Mr. GOLDSBOROUGH. That the banks are growing fat under.

Dr. SPAHR. No.

Mr. GOLDSBOROUGH. The banks are not suffering an awful lot, not the large banks. The large banks that are able to carry these Government bonds are doing very nicely in a very smug way and standing the chance of losing nothing, and that is the reason when these refundings take place they are always oversubscribed. The banks are grabbing them.

Dr. SPAHR. Because they haven't anything else in which to invest.

Mr. CROSS. I want to ask you a question there, Dr. Spahr: You said that the banks ought not to be in a position to have to take these things, or at least put pressure on them; they ought to get out and sell them on the open market. Is that right?

Dr. SPAHR. Yes.

Mr. CROSS. The open market is in such condition that the chances are they could not sell them, is that true?

Dr. SPAHR. I don't think so.

Mr. CROSS. Well, it probably would be, and in case it was, then what would you say to it?

Dr. SPAHR. I say the Government should have to take what it can get in the open market.

Mr. CROSS. What it can get. Now, listen: You have got some 12,000,000 people out of work, angry, mad. You have got to feed them; you have got to keep them from starving, or you are going to have a revolution. Don't you think it is far better that the Government use the banks if necessary in order to keep down revolution and destroying the whole country and chopping people's necks off and all that?

Dr. SPAHR. I think with inflated currency you will have reached the point of revolution——

Mr. CROSS (interposing). Oh, now—I don't know whether you know it or not, but when you get 12,000,000 people and their families hungry they don't care anything about theories. They want something to eat, and they are desperate. Now, what are you going to do, just say, sit down and let it go, and not take care of that situation?

Dr. SPAHR. In every country that inflated its currency, as a consequence——

Mr. CROSS (interposing). You know what happened in France? It was the question of money that brought on the French Revolution. They had got control of the wealth of France and there was no money. You know that if you have read the old history. The people became desperate.

Dr. SPAHR. May I answer that? When Napoleon came in France——

Mr. CROSS (interposing). Oh, Napoleon came in away after. This was in 1779.

Dr. Spahr. The first thing he did to get France on a solid basis was to get France back on the gold standard and establish a strong central bank.

Mr. Goldsborough. But Napoleon refused to borrow money from the banks. That is the reason he got into trouble with the international banks.

Mr. Cross. You have a history there of the taking of the lands of France from the nobility and issuing only 4,000,000 francs, to begin with, which was sound. But as the Revolution went on and kept increasing and increasing it was really a mortgage over their land. But finally they issued 49,000,000 of them, of course worth nothing. Yet it served its purpose, because any historian will tell you that they could not have won the Revolution without it. It was an inflation which was bad, uncontrolled. But it enabled France to win the Revolution, just like our continental money enabled us to win the Revolution, just like possibly in Germany, where there was a bad, uncontrolled inflation, it helped win the Revolution. Yet if they had not done it they would probably have gone into bolshevism.

Dr. Spahr. Are you not aware that inflation impoverished the masses of the people?

Mr. Cross. Oh, no; they are impoverished now. They are broke. You talk about a man owning these houses and these farms. He has a paper title that is nothing in the world but an interest-paying note, and the fellows up there are collecting off of him, and he is desperate and he is mentally desperate and he is wild.

Dr. Spahr. Yes.

Mr. Cross. You could not make it any worse condition.

Dr. Spahr. And the reason he is in that position, Mr. Cross, is because our currency is inflated and he is now paying for it.

Mr. Cross. Who inflated it? The banks.

Dr. Spahr. Everybody—our Government.

Mr. Cross. The banks were loaning and getting rediscounts.

Dr. Spahr. And you want the banks to do it again.

Mr. Cross. And then when the crash comes you say, "Wipe out the whole structure."

Dr. Spahr. That is what you are proposing.

Mr. Cross. And the people won't stand for it. You will have a revolution on your hands.

Dr. Spahr. That is exactly what you are proposing here; inflate the currency and let the people suffer again.

Mr. Cross. You have got them starving here, and they are not going to stand for it.

Dr. Spahr. They probably won't.

Mr. Goldsborough. If we had a system based on money and not wind, when you reached a certain point you could not go any further. It is this infamous system that you appear to advocate which makes these periods of extreme inflation and depression possible.

Dr. Spahr. No; you are advocating inflation. I am the one that is opposing it.

Mr. Goldsborough. That is what you say.

Dr. Spahr. I know it.

Mr. Cross. Aren't we already deflated and deflated and deflated?

Dr. Spahr. Yes, sir—and what caused it?

Mr. CROSS. Now, hold on now—no matter what caused it. Aren't we deflated to the bottom?

Dr. SPAHR. Yes, sir.

Mr. CROSS. Now, don't you think we ought to have some reflation?

Dr. SPAHR. No. That is not the alternative. The alternative is a sound monetary system and a stabilized system.

Mr. CROSS. It is too late to prevent the fire after the flame breaks out.

Dr. SPAHR. Instead of attempting to tinker with the currency.

Mr. CROSS. Tinker with the currency—Congress alone has the right to tinker with the currency. Congress is the king, and the king can make anything he wants money—always could—coming on down through Parliament into this country. Who tinkers with the currency but these private individuals that manipulate credit? That is tinkering. We do not tinker. We act. We have got the power by authority of the Constitution, and we are not going to let them handle as they have been.

Dr. SPAHR. Well, let us assume that the banks inflated and are paying for it. Now you want the Government to do the same thing.

Mr. CLARK. Have we any assurance as to what this Federal Reserve Board will do hereafter?

Dr. SPAHR. I would like to see a board created that will prevent inflation.

Mr. CLARK. I am for that a hundred percent. I think we are all after that sort of thing, but we are misunderstanding our methods of approach or we disagree on our methods of approach.

Mr. FORD. Give us your idea of control. How could you control it?

Dr. SPAHR. There is never any excuse for inflation, is there?

Mr. FORD. What is your idea of control, if you will answer that for the moment?

Dr. SPAHR. I would say that there are about seven instruments of control that can be used. You can use the discount rate. You can use open-market operations. You can use warnings. You can use persuasion. You can regulate the amount of Federal Reserve notes going into circulation by different devices. You can refuse to accept paper that is unsound, and you can use your reserve if you have to.

Mr. FORD. The things that you have enumerated are not in this bill.

Dr. SPAHR. It is almost all in the present law.

Mr. FORD. It is put in there, and it should be more susceptible to control. That is all in the world this bill is doing, giving the Federal Reserve Board some recourse by which it can pull or push as the situation requires, to control expansion or contraction.

Dr. SPAHR. It has had every power thus far, had it been used.

Mr. FORD. It has none. Well, it had one power; yes. Now, take open-market operations at the present time—who initiates them?

Dr. SPAHR. The Open Market Committee.

Mr. FORD. And who are the Open Market Committee?

Dr. SPAHR. It is 5 of the Executive Committee out of that 12.

Mr. FORD. They can initiate them, but they do not have to carry them out. Suppose the Federal Reserve Board as a body wanted to start open-market operations. Could they tell the Federal Reserve Boards to cooperate, or should they ask them?

Dr. SPAHR. I understand they can force that Open Market——

Mr. FORD. No; they cannot. That is what we are trying to rectify in this bill. We are trying to take care of that so that the Federal Reserve Board can say when and at what time and to what extent open-market operations can be conducted, whether they are purchasing or selling.

Dr. SPAHR. I would not argue against that provision.

Mr. FORD. That is all it is.

Dr. SPAHR. No; if your board is independent and nonpolitical, but if it——

Mr. FORD. My God, man; how are you going to get an independent, nonpolitical board in a political country? What is politics? It is the science of government. What is a politician? He is supposed to be a man that is versed somewhat in the science of government, is he not?

Dr. SPAHR. But running a bank is a technical thing, and they are supposed to be technically trained.

Mr. FORD. There are technical men on that board and they are the best technicians we could get.

Dr. SPAHR. I doubt it.

Mr. CROSS. You have stated here, I believe, that these very men are the best brains in the country.

Dr. SPAHR. I think they are.

Mr. CROSS. Your 60 men go off and draw up a bill then, the best brains in the country, and see if it covers the whole situation. When you get those 60 men who are agreed together, let them draw up a bill and bring it in here. Why, you will have them fighting and each one saying, "That is what we want", and it will be different for every one of them. We have got to have something concrete. Bring us in something constructive here. Get your 60 men together and draw up the bill.

Dr. SPAHR. I wish you would charge the committee with that responsibility.

Mr. CROSS. It is the responsibility of you, it seems to me. You say you had the responsibility of getting out this pamphlet and the responsibility of issuing articles and statements. Now get them together. You say that you have 66 men who are the best brains in the country. So get those best minds together in a room and draw up a bill covering this thing in detail, like any other bill that has got to have mechanics back of it, and bring it in here and submit it to us. Then argue to us that it is supported by those men, and the reasons for it.

Dr. SPAHR. It would take a year to do it.

Mr. CROSS. Oh, my; haven't you been working on this, and these other 60 best minds of the country, for years?

Mr. GOLDSBOROUGH. Forty years.

Dr. SPAHR. Surely.

Mr. CROSS. And now you cannot sit down and draw up a little bill like this in a year?

Dr. Spahr. No. That is what I want to object to.

Mr. Cross. You cannot do it; you 60 fellows would get together and have a fight in no time. You would not get anywhere. It is awfully easy, Doctor, to criticize something that is faulty, but is is hard to suggest something constructive. That is what we want to do.

Dr. Spahr. I am doing that. The most constructive thing, Mr. Cross, that I can suggest is, don't pass title II.

Mr. Cross. Well, all you say is "don't." Now show us something to do.

Dr. Spahr. That is constructive.

Mr. Cross. Well, you say the present system is not right. You say that is wrong. You say "don't" to these things. You say "don't do" and here are the best 60 minds saying the other system is wrong and the Board here is wrong, and all you do is come in and just say "don't, don't, don't." Why don't you go make up a bill and bring it in here?

Dr. Spahr. Mr. Cross, if you are about to go over a precipice and I stop you, that is a constructive thing. I don't have to sit down and draw up blueprints about how to do it.

Mr. Cross. If I am so close to the edge that I am liable to fall over, I want you to throw me a rope. You are just sitting out there and saying, "Just sit still. Go on over." I say, "Throw me a rope."

Dr. Spahr. My answer is, "I will take you away from the edge of the precipice."

Mr. Cross. You don't take me away; all you say is, "Just sit still. Don't."

Dr. Spahr. We have a system functioning as well as anything needs to function now. It has every power that is essential.

Mr. Ford. What!

Dr. Spahr. It has every power that is essential.

Mr. Ford. That system that put us in the morass of depression the like of which was never known before—you want us to continue that?

Dr. Spahr. No. I say the system as it is devised under the Federal Reserve Act has all the authority that is needed so far as any Federal Reserve System goes.

Mr. Ford. Did it work?

Dr. Spahr. Certainly it did not. They inflated.

Mr. Ford. Who inflated?

Dr. Spahr. The banks.

Mr. Cross. We want all these things corrected.

Dr. Spahr. You cannot do it in 15 minutes.

Mr. Cross. We have taken a week, and we can take a little more time.

The Chairman. You say we have a good system——

Dr. Spahr (interposing). I did not say that. I say they have all the power and authority now that they need in generating recovery. There is nothing you can change about this Federal Reserve System that will generate a sound recovery. Therefore, let the System stand as it is and let us have a thoroughgoing overhauling of the Federal Reserve System, and in the meantime let us have a sound currency and let us encourage business recovery. Those are the things that are in order, as I see it.

The CHAIRMAN. Let me ask you this: How do you look upon the Federal Reserve System?

Dr. SPAHR. I think it is a pretty weak System.

The CHAIRMAN. Have you ever been for it?

Dr. SPAHR. Yes; I have. I thought it was pretty good until I saw the consequences of inflation.

The CHAIRMAN. All the bankers, as well as all the economic experts, have agreed during the years that the Federal Reserve System was very fine and a very successful System, have they not?

Dr. SPAHR. I think that is substanitally accurate.

The CHAIRMAN. And it did serve admirably and satisfactorily for quite a long time, did it not?

Dr. SPAHR. Quite a long time.

The CHAIRMAN. Do you know where we got the Federal Reserve System?

Dr. SPAHR. Yes; I think so.

The CHAIRMAN. Did you ever stop to think about its history?

Dr. SPAHR. Yes; I am acquainted with it.

The CHAIRMAN. Did you know that it was written by politicians, such men as you see sitting here this afternoon in Congress, and over the protest of almost every banker in the United States?

Dr. SPAHR. Yes.

The CHAIRMAN. And everybody else who was supposed to know anything about it? That is the history of the Federal Reserve.

Dr. SPAHR. I do know who did most of the drafting.

The CHAIRMAN. I am talking about where the Federal Reserve came from. It was the work of politicians, in fulfillment of a partisan, political party platform pledge, and written by a partisan committee. The Democrats wrote it with the Republicans excluded, and they took it to the House and held a Democratic caucus and bound every man to vote for it upon penalty of losing his standing in his party, and then brought it to the House and permitted Republicans to vote for it.

That is where the Federal Reserve System came from, not only from Congress, but from partisan politicians.

Dr. SPAHR. H. Parker Willis and Carter Glass did most of the drafting.

Mr. GOLDSBOROUGH. As to the technical work, that was all.

Dr. SPAHR. And they had a tremendous number of hearings.

Mr. GOLDSBOROUGH. Oh, yes. They had this Capitol swarmed with bankers and experts who would take a backwoods Congressman by the arm and keep after him while they were writing the Federal Reserve Act, because they knew that he did not know anything about it, and they would keep working on him and telling him that it was unsound and improper, the currency was being tinkered with and was certain to result in something that they did not know anything about. But the committee discarded all that advice and went ahead and did it. Isn't that the history of the Federal Reserve Act?

Dr. SPAHR. That is right. This title II has a fundamental conception lying behind it that is quite different from what prevailed in 1913. Here the idea is that they are going to pump currency into circulation.

Mr. GOLDSBOROUGH. You have said that now three or four times. Where do you find that in the bill?

Dr. SPAHR. I got it from all the atmosphere. I got it from Mr. Eccles' testimony.

Mr. GOLDSBOROUGH. Where is it in the bill?

Dr. SPAHR. It is not in the bill but it enables them to do it.

Mr. GOLDSBOROUGH. But we have never had a provision like that.

The CHAIRMAN. If you will permit me, Dr. Spahr—because you want to be accurate in your statements of fact, you are in error in your statement that that is in this bill. I might say that a controversial point among members of this committee hinges around the failure of the bill to undertake the proviso for carrying the thing that you have understood is in the bill.

Dr. SPAHR. My point is, it permits it.

The CHAIRMAN. Oh, well; the present system permits it, you say.

Dr. SPAHR. Yes.

The CHAIRMAN. The people who are advocating this particular thing are setting up the machinery that will make it work. The machinery will not make it work now because the Board won't permit it. I am not saying that it is the last word of wisdom on the subject; I am only speaking of the fact now.

Mr. BROWN. Doctor, I would like to ask you one question: I wonder how many of these 66 professors are now teaching school.

Dr. SPAHR. Nearly all of them.

Mr. FORD. There are several of them dissenting from this thing.

Dr. SPAHR. Yes, some of them dissented in certain paragraphs. I think six men had certain qualifications.

Mr. BANKHEAD. This is just a memorandum on it. I do not see any constructive suggestion in it.

Dr. SPAHR. Their constructive suggestion is not to pass it.

Mr. BANKHEAD. It seems to me that the six best minds would know better than that.

Dr. SPAHR. It seems to me the best thing is don't pass it.

Mr. BANKHEAD. Oh, is that your advice?

Dr. SPAHR. I am not competent to discuss titles I and III.

Mr. HOLLISTER. I would like to ask that this memorandum about that title be put in the record.

The CHAIRMAN. Without objection, it will be printed in the record.

MEMORANDUM IN OPPOSITION TO TITLE II, BANKING BILL OF 1935 (H. R. 5357—S. 1715) SUBMITTED TO CONGRESS BY ECONOMISTS' NATIONAL COMMITTEE ON MONETARY POLICY

The undersigned members of the Economists' National Committee on Monetary Policy wish to point out to the country that the so-called "Administration Banking Bill of 1935", recently introduced in Congress (H. R. 5357 and S. 1715) endangers the development of sound commercial banking in this country in the following principal respects. These warnings relate only to title II of that bill.

1. *Providing for political control of the Federal Reserve Board and Federal Reserve banks.*—The Federal Reserve administrative authorities, instead of being given the independence which is appropriate to the officers of a nonpolitical central commercial banking system, will be brought under direct control of the President. It is proposed to accomplish this end by providing that the membership of the Governor on the Federal Reserve Board shall expire when he is no longer designated as Governor by the President. This provision will enable the President to advance any member to the governorship, then remove him, and in this manner the complete personnel of the Board can be changed quickly and will be subject at all times to Presidential control. Thus the Board can become a politically-controlled Board with little opportunity to exercise independent judgment.

The same will be true of the Governors and Vice Governors of the Federal Reserve banks, since it is proposed that they be appointed by the directors of the Federal Reserve banks after approval by the politically-controlled Federal Reserve Board.

The lessons of central banking teach us that the farther a central banking system is removed from political domination, the better it is for the country.

2. *Providing for the conversion of illiquid assets of Federal Reserve banks into legal tender notes.*—The proposal to repeal the requirements with respect to commercial paper collateral for Federal Reserve notes is unsound. It will enable the Federal Reserve banks to issue legal tender notes against frozen or illiquid assets admitted under the tolerance or policies of a politically-controlled Federal Reserve Board, and will destroy the prospect of restoring the so-called "elastic" characteristics of these notes—a feature which financial leaders have striven to obtain for nearly fifty years. Although the Glass-Steagall amendment of 1932 and the emergency banking legislation of 1933 gave these notes what is commonly called an inelastic characteristic by permitting the use of government securities as collateral, it was supposed that this change was temporary and that efforts would be made, after the emergency had passed, to restore the "elastic" feature of these notes. Instead of providing us with a note currency which bears the appropriate relation to the sound short-term needs of business, thus avoiding inflationary tendencies, the bill provides the means for the issue of notes against Government bonds—and other assets, regardless of liquidity—and, consequently, opens the way for a huge bank note inflation in this country. The bill enables the Government through the banks to convert the national debt into bank notes until the surplus banking reserves of the country are exhausted. The Federal Reserve Board, furthermore, is given the power to reduce the reserve requirements of member banks as it sees fit, thus increasing immeasurably the possibilities of inflating the currency. The passage of such a measure will invite ultimate disaster for this country.

3. *Providing that noncommercial and illiquid paper may be eligible for rediscount at Federal Reserve banks.*—The proposal to make "any sound asset" of a member bank eligible for discount at a Federal Reserve bank opens the way to converting what should be a commercial banking system into an illiquid noncommercial system. The supply of noncommercial paper eligible for rediscount should be further restricted, not enlarged. This bill makes a politically controlled board the sole judge of the soundness of the assets to be admitted to the Federal Reserve banks. It is the function of a central banking system to maintain at all times a liquid portfolio, since the system holds the ultimate reserves of the nation's banks.

4. *Providing for the broadening of member bank loans on real estate.*—The proposal to permit member banks of the Federal Reserve System to loan an amount equal to 60 percent of their time and savings accounts or an amount equal to their entire capital and surplus on real estate, for periods of 20 years up to 67 or 75 percent—depending upon circumstances—of the value of property, is unsound. Making such loans is not an appropriate function of a commercial banking system. Real estate loans of a far more restricted nature have caused great losses and have been a source of great trouble for the commercial banks of this country. This is one of the outstanding lessons of the decade of 1920–30, with its holocaust of bank failures and paralyzing losses. To increase the possibility of such losses and difficulties is hardly rational.

All measures designed to correct weaknesses in the Federal Reserve System should seek to increase, rather than destroy, its independence of political influence. They should increase, not reduce, its commercial nature. They should assure, not impair, its liquidity. And they should free it from Government financing rather than link it more closely to the fiscal needs of the Government.

[Signed]: Arthur B. Adams, The University of Oklahoma; Eugene E. Agger, Rutgers University (with reservations as to par. 2); James W. Angell, Columbia University; Charles C. Arbuthnot, Western Reserve University; Leonard P. Ayres, The Cleveland Trust Company; George E. Barnett, The Johns Hopkins University; Don C. Barrett, Haverford College; James Washington Bell, Northwestern University; Ernest L. Bogart, University of Illinois; Jules L. Bogen, Journal of Commerce and New York University (with reservations as to par. 2); Frederick A. Bradford, Lehigh University; R. P. Brooks, The University of Georgia; Charles J. Bullock, Harvard University; Neil Carothers, Lehigh University; J. Ray Cable, Washington University; Wilbur P. Calhoun, University of Cincinnati; Edward H. Collins, New York Herald Tribune; Alzada Comstock, Mount Holyoke College; William W. Cumberland, Wellington & Co.; George W. Dowrie, Stanford University; Eleanor Lansing Dulles, University of Pennsylvania; William E. Dunkman, University of Rochester; D. W. Ellsworth, The Annalist; William D. Ennis, Stevens Institute of Technology; Clarence W. Fackler, New York University; Fred R. Fairchild, Yale University; J. Anderson Fitzgerald, The University of Texas; Roy L. Garis, Vanderbilt University; Lewis H. Haney, New York University; E. C. Harwood, American Institute of Economic Research; Hudson B. Hastings, Yale University; John Thom Hoedsworth, The University of Miami; F. Cyril James, University of Pennsylvania (with reservations as to par. 2); Edwin W. Kemmerer, Princeton University; Elbert Alvis Kincaid, University of Virginia; David Kinley, University of Illinois; William H. Kniffin, Bank of Rockville Centre Trust Co. (with reservations as to par. 4); Frederic E. Lee, University of Illinois; Ray V. Leffler, Dartmouth College; Esther Lowenthal, Smith College; Arthur Marget, University of Minnesota (with reservations as to pars. 2-3); A. Wilfred May, New York City; Mark C. Mills, Indiana University; Margaret Myers, Vassar College; Melchior Palyi, The University of Chicago; Ernest Minor Patterson, University of Pennsylvania; Clyde W. Phelps, Chattanooga University; Howard H. Preston, University of Washington; William A. Rawles, Indiana University; Harold L. Reed, Cornell University (with reservations); Leland Rex Robinson, New York City; R. G. Rodkey, The University of Michigan; Olin Glenn Saxon, Yale University; Joseph A. Schumpeter, Harvard University; William A. Scott, University of Wisconsin; James G. Smith, Princeton University; Walter E. Spahr, New York University; Oliver M. W. Sprague, Harvard University (with reservations as to pars. 2-4); William H. Steiner, Brooklyn College; Alvin S. Tostlebe, College of Wooster; James B. Trant, Louisiana State University; Rufus S. Tucker, Westfield, N. J.; Ray B. Westerfield, Yale University; Nathaniel R. Whitney, Procter & Gamble Co.; H. Parker Willis, Columbia University; Max Winkler, College of the City of New York; Ivan Wright, University of Illinois; John Parke Young, Occidental College; Ralph A. Young, University of Pennsylvania.

(Issued through the office of Secretary-Treasurer, 100 Washington Square, New York City. March 7, 1935.)

The CHAIRMAN. Gentlemen, we will meet at 10:30 tomorrow morning to continue with the hearing, and we certainly thank you, Dr. Spahr, for your patience and your assistance.

Dr. SPAHR. Thank you, gentlemen.

(Whereupon, at 5:10 p. m., the hearing was recessed until 10:30 a. m., the next day, Thursday, Mar. 28, 1935.)

BANKING ACT OF 1935

THURSDAY, MARCH 28, 1935

House of Representatives,
Committee on Banking and Currency,
Washington, D. C.

The committee met at 10:30 a. m., Hon. Henry B. Steagall (chairman) presiding.

The Chairman. We have with us this morning former Congressman William Schley Howard, of Atlanta, Ga., who wants to discuss one of the features of this bill with reference to savings banks.

I am quite sure, Mr. Howard, that the committee will be delighted to hear you.

STATEMENTS OF HON. WILLIAM SCHLEY HOWARD, ALTANTA, GA.; GEORGE M. BROWN, PRESIDENT GEORGIA SAVINGS BANK & TRUST CO., ATLANTA, GA.; JAMES E. CAROLAN, VICE PRESIDENT AND TREASURER ALTANTA SAVINGS & TRUST CO., SAVANNAH, GA.; AND J. P. HOULIHAN, VICE PRESIDENT GEORGIA STATE SAVINGS ASSOCIATION, SAVANNAH, GA.

Mr. Howard. Mr. Chairman and gentlemen of the committee, I will inflict myself upon you only a very few minutes.

We have a rather peculiar situation in the State of Georgia, in that we have never had any laws under which mutual savings banks could be organized. Therefore the banks that I have the honor to represent before you gentlemen are chartered banks—chartered by the superior courts of our State—doing a similar business as that of the mutual savings banks that are exempted in the bill now pending before you, and the Morris Plan Bank.

We do not commercial business whatsoever. Our banking activities are confined exclusively to savings banks' activities, and, as I say, the banks are chartered by the superior courts of our State.

We have 9 such banks in Georgia, and 4 or 5 of the officials of those banks have accompanied me here to present this phase of the subject to you, with an amendment that we are asking you gentlemen to adopt as a part of this bill, putting the savings banks in the State of Georgia, who are peculiar in their own situation, in the same category with the mutual savings banks and the Morris Plan Bank.

I know how very valuable the time of this committee is at this particular juncture, and I do not want to consume your time unnecessarily. I do not want to consume a single moment longer than necessary.

The CHAIRMAN. You may take all the time your desire, Mr. Howard. The committee will be glad to hear you.

Mr. HOWARD. I have drawn an amendment, which we desire to propose to you. If you will turn to page 37 of the pending bill, H. R. 5357, section 23, subsection (y) (1), I will indicate where our amendments would appear.

As the provision now reads it says:

No State nonmember bank, other than (a) a mutual savings bank or (b) a Morris Plan Bank—

And so forth. After the word "bank", the second time it appears in line 19, we ask the committee to insert this language:

and other incorporated savings banks, the deposits of which are not subject to check, engaged in similar business.

Then, on page 67 of the same bill, at the top of the page, after the name "Morris Plan Banks", in line 3, which contains the exception from the operation of the provisions of this bill, we ask that the same language that I have just quoted be inserted at that point, so that the language in parentheses beginning in line 2 of page 67 will read:

except mutual savings banks, Morris Plan Banks, and other incorporated savings banks, the deposits of which are not subject to check, engaged in similar business.

Gentlemen of the committee, in order that you may understand the operation of these banks in Georgia, I will try to explain them to you. For instance, I am thoroughly familiar with the operation of the Georgia Savings Bank & Trust Co. in Atlanta.

It has a capital of $500,000, and it has been in business for some 30 years. It has made, in that period of time, some 26,000 or 27,000 loans, exclusively, on real estate. Those loans have ranged from $1,000 to a maximum, in 90 percent of the cases, of $2,500. The length of time that those loans run is usually 5 years.

The borrower pays that money back at a low rate of interest, it being amortized over the period, with 60 monthly payments, including interest and a reduction in the loan in each payment. All of the other eight banks in the State have practically the same system.

In the city of Atlanta, for instance, we have aided in the erection of homes to the number of about 7,500, which have been built under that plan. We have no money that is loaned except on such paper as is not rediscountable under the Federal Reserve act.

We buy mortgages or what we call trust deeds, or loan deeds, rather.

Our business is confined exclusively to that kind of business; all of the money deposited with us seeks an outlet to small investors in homes.

If this amendment meets with the favor of the committee we can continue to do that business. If not, if the rate of interest that we can pay on the deposits is restricted to 2½ percent or 2 percent, then it means that these banks will simply have to liquidate and go out of business.

There is another matter that I would like to call your attention to in relation to one or two of these banks. As to the Georgia Savings Bank & Trust Co., we have borrowed on what are termed "capital debentures." A capital debenture is a capital note, and we have borrowed on those from the Government of the United States some $500,000 during this recent emergency. That money is to be paid back within a period of 20 years.

If we cannot pay our depositors a sufficient amount of interest to attract those depositors to our institution and they go elsewhere, inasmuch as money always does seek the highest rate of interest that it can obtain, then we will receive no deposits, and that being our business, and nothing else, it will leave us in debt to the Government in the sum of half a million dollars that we can never repay, and puts us out of business.

That is about the sum and substance of everything I have to say, Mr. Chairman. I do not think I could express myself as to our situation more elaborately than I have if I talked all day, because that is the true situation as to these banks that have several million dollars at stake in their business.

We ask that you gentlemen give consideration to this class of bank. The president and other officials of those banks are here this morning. They are thoroughly familiar with the practical end of the business that I have tried to explain to you, and if you would like to ask any of them or myself any questions, we will be glad to answer them.

Mr. BROWN of Michigan. Do you have capital stock in these banks?

Mr. HOWARD. Yes, sir.

Mr. BROWN of Michigan. So they could not come under the definition of a mutual savings bank?

Mr. HOWARD. No, sir; we have no set-up in Georgia under our law for the establishment of mutual savings banks. All of the charters of these banks were obtained through our superior courts.

The savings bank in Savannah, represented by some of its officials here this morning, has been organized for 45 years, or it has been in business for 45 years.

We have in Georgia what we consider a very fine State banking law. These banks are all chartered. In other words, the protection given to the depositors under the laws of Georgia is complete. We have the strictest sort of examination of our banks, and the banking laws of the State of Georgia are very strict. All of these banks obtain their charters under the laws of the State of Georgia.

The Georgia Savings Bank & Trust Co. has a capital, as I have said, of $500,000. Then we have the Atlantic Savings & Trust Co., of Savannah, which has a capital of $50,000, a surplus of $50,000, and undivided profits of $64,022.63.

The Albany Trust & Banking Co., of Albany, Ga., is a small bank in a small town in the southwestern portion of our State, in a very splendid, growing section. That bank has a capital stock of $100,000; it owes the Government on capital notes, $50,000; it has a surplus of $20,000, with undivided profits of $11,255.86.

Then the Home Savings Bank, of Columbus, Ga., has a capital of $150,000; a surplus of $20,000, and undivided profits of $4,509.02.

The American Savings Bank, of Atlanta, one of the first banks organized in the history of our State, has a capital stock amounting to $200,000, a surplus fund of $100,000, and undivided profits amounting to $20,724.02.

The Realty Savings & Trust Co., of Augusta, represented here this morning by Mr. Lyeth, the secretary-treasurer, has a capital stock of $100,000; it has capital notes issued under the plan I have outlined to you gentlemen, amounting to $100,000. They cover money borrowed from the Federal Government on the 20-year plan. So they owe the Government on those capital notes the amount of $100,000. They have a surplus of $26,949.07, and undivided profits of $2,426.28.

In reference to the Georgia Savings Bank & Trust Co., Atlanta, I have already told you what their capital stock is, amounting to $500,000. Then they have capital notes amounting to $500,000, a surplus fund of $100,000, and undivided profits amounting to $72,519.55.

The Georgia State Savings Association, of Savannah, Ga., is a very old and a very strong bank for the locality in which it has carried on its busines for years and years. It has a capital stock of $325,000, a surplus fund of $325,000, and undivided profits amounting to $52,524.30.

As has been stated, these are all capital-stock banks. They operate on the identical plan as mutual savings banks of other States, and also the Morris Plan Bank, and we simply ask that we be placed on the same footing with those banks, as the banks of other States that do that mutual-savings-bank business.

The CHAIRMAN. I am not sure that I understand just what your legal status is as to institutions in the State of Georgia.

Mr. HOWARD. We are incorporated under the laws of the State of Georgia, that is, under the banking laws of the State of Georgia.

Mr. HOLLISTER. Are they corporations for profit, or are they mutual?

Mr. HOWARD. They are not mutual savings banks; they are capital-stock banks.

Mr. HOLLISTER. And the profits inure to the holders of the capital stock?

Mr. HOWARD. Yes.

Mr. HOLLISTER. How do they differ from the ordinary savings banks in other States?

Mr. HOWARD. They have mutual savings banks.

Mr. HOLLISTER. How do they differ from the banks that are not mutual?

Mr. HOWARD. They do not.

Mr. HOLLISTER. Such an amendment, if adopted, would not apply specifically to that particular kind of bank, but it would apply to all savings banks?

Mr. HOWARD. That do the character of business that we do. We simply receive deposits. We have no checking account. We take the profits and pay the depositors a certain amount of interest. Under the laws of the State of Georgia the reserves are safe-guarded, and those funds are loaned.

Mr. HOLLISTER. But they could draw the money out?

Mr. HOWARD. They could draw the money out on a 90-day notice.

Mr. BROWN of Michigan. Will you turn to page 2 of the bill and tell me whether or not subsection 1 of section 3 does not cover your particular type of institution.

Mr. HOWARD. I am going to be perfectly frank with you gentlemen. I took this bill and studied it for several days, not having the original bill before me at that time, of which bill this is amendatory, and I could not comprehend all these amendments. Which provision do you refer to?

Mr. BROWN of Michigan. Page 2, section 3.

Mr. HOWARD. Where it says—

by inserting a new subsection to read as follows.

Mr. BROWN of Michigan. Starting there, and under subsection (1), I am wondering whether that would cover your particular type of bank, particularly the language in lines 17 to 23.

The CHAIRMAN. I understand it does cover them, and that is where his trouble is.

Mr. HOLLISTER. They want to be excepted.

The CHAIRMAN. That language does cover such a bank. It is a State bank within the definition under the section to which he refers, and no State bank can avail itself of the benefits of the insurance fund after the first of July 1937.

Mr. HOWARD. That is right.

Mr. BROWN of Michigan. That problem we have not yet come to.

The CHAIRMAN. I understand that, but he is not familiar with the situation we have. He is assuming this law will stand as it is.

Mr. HOWARD. Yes.

Mr. BROWN of Michigan. You stand in the same position as every other State nonmember bank.

Mr. HOWARD. Yes; savings banks. This is the reason why we ask for this exemption. We cannot avail ourselves of the rediscount privilege of the Federal Reserve banks with the character of business we do, because the banks are not permitted, or will not be permitted, I think, after January 1, 1937, to lend money at all on mortgage loans, that is, on real property.

Therefore, under this bill, we are restricted, and yet none of the benefits inure to our class of banks.

Mr. SPENCE. Are there other States where savings banks are organized similar to yours?

Mr. HOWARD. I do not know. I have a list of the banks in the United States doing a similar business.

I hope you gentlemen understand me. I do not want to leave the impression that we are not doing the same character of business that the Morris Plan banks are doing, identically the same kind of business, and the same character of business that the mutual savings banks do.

The CHAIRMAN. You do the same kind of business they do, but are you restricted to that kind of business?

Mr. HOWARD. Yes; under the charters under which we do business. We have never established any mutual savings banks in Georgia.

Mr. HOLLISTER. Your charters could be amended so as to permit you to do a different kind of business, could they not?

Mr. HOWARD. We might go into the courts and ask them to amend our charters to allow us to do a general banking business.

Mr. HOLLISTER. If this exception were put in the bill would it not include banks which do quite a different kind of business than you do?

Mr. HOWARD. I think not, because you have excepted Morris Plan Banks and you have excepted the mutual savings banks.

Mr. HOLLISTER. Yes.

Mr. HOWARD. We do not call them mutual savings banks; we call them capital stock banks, because we operate on capital stock. There is no assessment.

Mr. HOLLISTER. What I am trying to get at is how your banks are differentiated from the ordinary savings banks which are not mutual.

Mr. HOWARD. I presume they are all mutual or all capital stock savings banks.

Mr. HOLLISTER. Then do you except all savings banks?

Mr. HOWARD. We except all capital stock savings banks doing business of a similar character.

Mr. HOLLISTER. Have you discussed this provision with the Federal Deposit Insurance Corporation?

Mr. HOWARD. We have an amendment that we understand will meet their approval.

Mr. HANCOCK. Suppose an amendment were offered which would make eligible Morris Plan Banks or other similar institutions; would that take care of your situation?

Mr. HOWARD. Yes, sir.

Mr. HANCOCK. I understand that such an amendment has been approved by the officials of the Federal Deposit Insurance Corporation, subject, of course, to the approval of this committee.

Mr. HOWARD. The only difference, Congressman Hancock, between the language you have just quoted and our amendment is that our amendment reads like this:

> Other incorporated savings banks, the deposits of which are not subject to check, engaged in similar business.

That is a little more explicit.

Mr. HOLLISTER. " Similar business " there applies both to savings banks and Morris Plan Banks. That is what I do not like about your language. I think a bank which does a business similar to the Morris Plan Banks, as suggested in the amendment referred to by Mr. Hancock, perhaps would be properly excepted.

Mr. HOWARD. Or mutual savings banks.

Mr. HOLLISTER. I do not think so. The mutual-savings bank does a savings business. I am not sure we should extend the exception to all savings banks, capital-stock banks, as well as mutual banks, unless they are doing solely a business similar to that of the Morris Plan Bank.

If the Federal Deposit Insurance Corporation, or the drafters of this bill, had believed that savings banks doing solely a savings-bank business should be excepted, they probably would have said so. These are two distinct kinds of banks, and if they had wanted to exempt all savings banks doing solely a savings-bank business they probably would have said so.

It seems to me the suggestion made by Mr. Hancock is the amendment we should adopt, and that the nature of the business referred to should be that of a Morris Plan Bank rather than a mutual-savings bank.

Mr. HOWARD. We thought you had excepted mutual-savings banks and Morris Plan Banks and that, as Congressman Hancock suggested, an amendment putting us in the same category with the mutual-savings banks and Morris Plan Banks would be fair and just to us, because we do absolutely the same character of business that they do.

Mr. HOLLISTER. Then if Mr. Hancock's amendment would cover you, you would not need the language you suggest.

Mr. CAROLAN. The Morris Plan Bank is chartered just the same as we are, and if they are excepted we think we should be excepted with them, for that reason.

Mr. HOLLISTER. That is what I say; if we state in the exception that you are excepted if you do business like the Morris Plan Banks, that is enough, is it not?

Mr. CAROLAN. You refer to mutual-savings banks; they do quite a different kind of business.

Mr. HOLLISTER. If you take your language, that will put all savings banks, practically, in the excepted class. I do not think that is the request you want to make. You want to make the request that capital-stock savings banks doing a business similar to the Morris Plan Bank business should be excepted.

Mr. CAROLAN. And mutual-savings banks.

Mr. HOLLISTER. No.

Mr. CAROLAN. Why not?

Mr. HOLLISTER. Because you are a capital-stock bank.

Mr. CAROLAN. But we are doing the same kind of business as mutual-savings banks.

Mr. HOLLISTER. Does not that raise the question as to that proposition—as to making a distinction between the two banks?

Mr. CAROLAN. There are very few of these banks.

Mr. HOWARD. I have here a list showing the number of the same character of banks in the different States.

They have 2 in Alabama; 2 in Arizona; none in Arkansas; 11 in California; Colorado has none. The savings accounts there are handled through any regularly organized bank.

Florida has none; Georgia has 9; Idaho has none; Illinois has none; Indiana has none; Iowa has 2; Kansas has none; Kentucky has none; Louisiana has none; Maine has none; Maryland has none; Massachusetts has none; Michigan has 3; Minnesota has none; Mississippi has none; Missouri has none; Montana has none; Nebraska has 2; Nevada has none; New Hampshire has none. I have a notation here that they are sending their annual report.

New Jersey has 1; New Mexico has none; New York has none; North Carolina has none; North Dakota has none; Ohio has none; Oklahoma has none; Oregon has 1; Pennsylvania has 1; Rhode Island has none; South Carolina has none; South Dakota has none; Tennessee has none; Texas has none; Vermont has about 20 or 25; Virginia has none; Washington has 1; West Virginia has none; Wisconsin has none; and Wyoming has none. So, as has been stated, there are very few of this character of banks in the country. They are in a class almost by themselves.

The CHAIRMAN. Of course, it might be well to remember in that connection that the legislation we pass will probably stand for a long time and cover the developments for many years. So, of course, we cannot anticipate what the probabilities might be, as time runs along.

Mr. HOWARD. But, as has been suggested, it means that if our banks are not included in the exception, we cannot pay a sufficient rate of interest to attract savings to our banks, if we are put in a class of banks doing a commercial business as well as a savings business. If the paper that we take exclusively for the people's money that we loan out cannot be rediscounted, so that we cannot pay over 2 or 2½ percent in interest, then, as I said at the inception of my remarks, it means liquidation and nothing else, if we are not put in the same category with the Morris Plan and mutual savings banks.

Mr. CLARK. Why cannot your paper be rediscounted under this new legislation, if it is passed?

Mr. HOWARD. As I understand it—and I want to plead ignorance of the manipulations of that bill, because I have not been able to comprehend it in the bill that I have had before me—my understanding is that you cannot rediscount mortgage loans and loan deeds, or any paper that is secured by realty.

Mr. CLARK. The purpose of this legislation is to do just that thing, to enable a bank with real-estate mortgages, amortized mortgages, to go to the Federal Reserve bank and borrow money from that bank on its note and to pledge these mortgages to that bank. That is the liberalizing feature that has been written into this bill.

Mr. HOWARD. The very purpose, and the very life of a savings bank is the fact that it receives from people their very small deposits, and they accumulate those deposits, and they loan that money that has been so accumulated, with a certain safe reserve, to the poorer classes of people who seek to build homes. That is our justification, and our only right to live, doing that sort of business, and that is all we have.

Mr. FORD. It does not interfere with the other banks.

Mr. CLARK. Do you understand that this legislation will permit you to discount or borrow the money from the Federal Reserve bank on real-estate loans, if you are a member of the Federal Reserve System?

Mr. HOWARD. Yes; we understand that. But we are put in the same category with the Morris Plan Banks because they are chartered under the very same conditions that we are.

Mr. SPENCE. You loan exclusively on real estate?

Mr. HOWARD. Yes, sir.

Mr. SPENCE. You make no other loans?

Mr. HOWARD. That is our business and has been our business for 35 years, and we furnished the money with which to build 7,500 homes in the city of Atlanta through the savings of people of this kind, giving them accommodation at a low rate of interest.

If a man comes to us and wants to build a home and wants to borrow $2,000, and we loaned the $2,000, he pays it back in 60 monthly notes, reducing the loan during that period.

Mr. CLARK. You can pledge that with the Federal Reserve bank for that money, if this bill passes.

Mr. CAROLAN. That is not the objection we have. We object because of the rate of interest we would have to pay. We do not care about borrowing from the Government. We can get along without doing that. We can make sufficient connections without borrowing from the Government.

Here is the whole proposition. The Morris Plan Bank is allowed to pay a higher rate of interest than we are allowed to pay. And they are doing a similar business to ours; their set-up is just the same.

Mr. FORD. But they do not loan on real estate, do they?

Mr. CAROLAN. Yes, sir; here is a Morris Plan Bank which will be chartered by the State and examined by the State, and here is its statement published by the State. We think we should be allowed the same privileges that they are allowed in the way of an examination.

We are doing the very things now that the Government is doing in the Federal Reserve Act in making long-time loans and amortizing them over a long time.

But we are not commercial banks; we have no commercial accounts. We have not a checking account in our bank subject to demand. All of our deposits are time deposits, which require notice before there can be any withdrawal from them.

The majority of our money is on time certificates, put in the bank for a year. We could not survive unless we could get a differential in the way of higher rates of interest for our time deposits, because we make our loans on long-time contracts.

We are not competitive in any way with commercial banks, and for that reason we are not seeking any of their deposits.

Where a man comes in and puts in a thousands dollars for a year, we think we should not be limited to 2½ percent, like a commercial bank on a demand deposit. That is what it amounts to.

Mr. SPENCE. What do you pay your depositors?

Mr. HOULIHAN. We pay them 3 percent now. Under the new regulation of the Federal Deposit Insurance Corporation we will be cut down to 2½ percent. We are on the same footing as the building associations. We are in the same line of business as the building and loan associations.

Mr. CLARK. If you did not go into the Reserve System, the Federal Deposit Insurance Corporation could fix your rate of interest?

Mr. HOULIHAN. They fix the rate, and they will fix it so as to comply with that of every member of the Federal Deposit Insurance Corporation, and that is what we do not want them to do. We think we should be in the same class with the Morris Plan Bank because we are doing the same kind of business. If they are going to examine them we think they should examine us.

Mr. HOWARD. I have a letter here written by our State Bank Superintendent, Mr. R. E. Gormley, which I would like to put in the record, in which he states that our banks are on the exact basis with the Morris Plan Bank.

I would like to call your attention to this particular communication from the superintendent of banks of our State, written to Mr. George M. Brown, and received only yesterday. The letter says:

DEPARTMENT OF BANKING,
Atlanta, March 26, 1935.

Mr. GEO. M. BROWN,
President Georgia Savings Bank and Trust Co., Atlanta, Ga.

DEAR MR. BROWN: In regard to proposed revision in Federal Banking Act which permits regulation of interest by the F. D. I. C. and which will restrict rate of interest paid by your type of institution on savings to that permitted banks engaged in both commercial and savings business, I regard it very unfair to your type of institution that some differential in interest permitted paid on savings not be allowed to those banks engaged solely in the business of receiving savings deposits. As I see it, there is no distinction in the type of service performed by your bank and that performed by Morris Plan banks and mutual savings banks. In your operations in my opinion should be given the same discretion as regards payment of interest on savings accounts as that permitted to those types of banks.

My general objection to the proposed revision of the Banking Act of 1933, commonly known as the Banking Act of 1935, is the fact that complete supervisory and at least conflicting regulatory power is granted to the F. D. I. C. by the proposed bill. I also object very strenuously to the provisions of the proposed bill and the original bill regarding Federal Reserve membership as a requisite for membership in the insurance fund after July 1, 1937, due to the fact that the majority of our nonmember State banks are located in agricultural sections and also to the fact that these nonmember banks now received a considerable revenue from exchange, which source of revenue would be eliminated in the event they were forced into the Federal Reserve System and thereby endanger the safety of these banks, I deem it of the utmost importance that the proposed bill contain an amendment eliminating that section regarding Federal Reserve membership.

Very truly yours,

R. E. GORMLEY, *Superintendent of Banks.*

Mr. CLARK. There is one thing I did not quite understand. I did not get this particular point. Your entire objection is in reference to the matter of interest, is it not? You object to the interest rate being fixed?

Mr. HOWARD. Restricted. That is one objection; that is not all.

Mr. CLARK. Would you object to being forced into the Federal Reserve System if a provision was put in the bill requiring them to make an exception of your type of banks in fixing uniform interest rates?

Mr. HOWARD. These gentlemen here are in the business, and they can tell you better than I.

Mr. CLARK. As I recall the evidence that we have received, Governor Eccles expressed a desire to have a unified banking system so that in an emergency it could avail itself of the liberalized provisions of the act.

There is some sentiment against it to the effect that by this method, by requiring them to go into the system before getting the insurance, it would be a disadvantage.

Have you any objection to going into the Federal Reserve System if an exception was made in the act as to your banks, as to the system of fixing your interest rates?

Mr. CAROLAN. As to the rate of interest we could charge on loans, if they would do that, we would not have any objection. The thing we object to is as to the interest rate we pay. We cannot survive if they do that.

Mr. HOWARD. Mr. Chairman, Mr. George M. Brown, who is here, has been engaged in this particular business all his life, and he represents the largest savings bank in Georgia, with one exception, and the oldest savings bank, with one exception. He says he would like to make a statement of 2 or 3 minutes in reference to this matter.

The CHAIRMAN. We will be glad to hear him.

Mr. GEORGE M. BROWN. Our real objection to this bill as it is set up is not based on any fight we are making against the Morris Plan Bank.

I will tell you what our position in Atlanta would be. If this bill is passed, excepting Morris Plan Banks and not excepting the other savings banks—the Morris Plan Bank is chartered by our State, with the same powers we have—if they are excepted and we are left out, as the State superintendent of banks said in his letter, the result of that set-up would be this:

We would be restricted to any interest rate that the Federal Reserve bank or the Federal Deposit Insurance Corporation might name, and the Morris Plan Bank would have no restriction whatever, if the bill were passed in that way. I would rather own stock in the Morris Plan Bank in Atlanta than in any one of the commercial banks, because they have a monopoly of the savings-bank business in the city of Atlanta.

We are asking that we, doing the same type of business as the Morris Plan Bank, be excepted. The Morris Plan Bank is really a bank doing an industrial business, loaning on real estate to the working class of people. As a matter of fact, the business we do is very much more like the business of the mutual-savings banks and the building and loan associations than the Morris Plan Bank.

Mr. GOLDSBOROUGH. Did I understand you to say that you are engaged in the same type of business as the Morris Plan Bank?

Mr. GEORGE M. BROWN. We have the same charter and the same powers.

Mr. GOLDSBOROUGH. Why do you not become a Morris Plan Bank; then you would be exempt?

Mr. GEORGE M. BROWN. They picked out the Morris Plan Bank, and that it done because it is an industrial bank, dealing with real-estate loans. Instead of saying just the Morris Plan Bank, we would have no objection to it if you would say the Morris Plan Bank and all banks engaged in similar business.

Mr. HANCOCK. Have you the bill before you?

Mr. GEORGE M. BROWN. Yes, sir.

Mr. HANCOCK. Let me invite your attention to line 19 on page 37 of the bill. Suppose after the words "Morris Plan Bank" in line 19, an amendment in this language were inserted: "or other incorporated banking institutions engaged in similar business."

Mr. GEORGE M. BROWN. That would be satisfactory, but let me tell you one thing. I may be wrong about this, and I mean no offense to the committee, but I believe you failed to draw a distinction between a mutual-savings bank and a commercial bank and a capital-savings bank. The deposits are subject to 90 days' notice before you can withdraw.

We have not got a dollar on deposit in our bank that a man can withdraw without 90 days' notice. If they are not willing to let him do it, he cannot draw it out. In the commercial banks you can draw your money out at any time.

With that provision we can make long-time real-estate loans that we could not make if we were a commercial bank. It is only within the last 2 or 3 years that any commercial bank, State or national, has been allowed to make any real-estate loans whatsoever. All homes in the United States, all buildings in the United States, all factories in the United States, have been built on money secured largely from the New England and New York savings banks and mortgage companies and building and loan associations and savings banks throughout the country.

In my State, for 25 years there have been no building and loan associations in existence. They all went broke in 1893 and 1894 and have just recently been reestablished in the last 2 or 3 years.

In my city of Atlanta, if you wanted to build a home you were dependent on the Georgia Savings Bank & Trust Co., the American

Savings Bank, or the insurance company alone. You could not get such a loan from commercial banks.

Mr. HANCOCK. You have building and loan associations in Atlanta, have you not?

Mr. GEORGE M. BROWN. We have, and have had them within the last 2 or 3 years. We did not have one for about 25 years. All of them went broke in 1893 and 1894.

Mr. HANCOCK. How many have you there now?

Mr. GEORGE M. BROWN. Frankly, I do not know. I should say probably there are five of them there.

Mr. HANCOCK. Let me make again the suggestions I made before. If the committee should determine that that is a wise amendment, that is, the amendment I referred to, the same expression should be repeated in line 24 on page 37 after the words "Morris Plan Bank."

Mr. GEORGE M. BROWN. And also on page 67.

Mr. HANCOCK. On page 67, in line 3, after the words "Morris Plan Banks", the same language should be inserted.

Mr. GEORGE M. BROWN. Yes, sir.

Mr. HANCOCK. My understanding from the Federal Deposit Insurance Corporation's general counsel, Mr. Birdzell, is that this same language I have just suggested was employed in section 5 of the Banking Act of 1933, and in order to carry out the same purpose.

Mr. GEORGE M. BROWN. May I say in that connection that Mr. Gormley notified me that when he was up here about I think, within the last 5 or 6 weeks, when all the State bank superintendents in the United States, or a large number of them, were here, discussing the bill with the Federal Deposit Insurance Corporation, that his understanding was that the Federal Deposit Insurance Corporation was willing to put this language in, and that they agreed to amend the bill on page 37, line 19, by adding after the words "Morris Plan Bank" the words "and other banking institutions engaged in similar business."

They said to Mr. Gormley they did not know there were any banking institutions outside of the Morris Plan Bank in the United States that were strictly savings banks with capital stock. I think I have quoted him correctly. That is my understanding of what they stated that they did not know that.

Now, in reference to the interest rate you are confronted with this situation. We do as nearly as possible the same line of business as the building and loan associations or the New England mutual savings banks.

Under the present law the building and loan associations are allowed to pay 5 percent and the Government guarantees the 5 percent up to $5,000, just the same as they guarantee bank deposits. You can readily see that if you allow the savings banks to be cut out entirely you are going to turn the business in Atlanta over to the building and loan associations, because you will not come to me and pay me 7 percent and get 5 percent from them, and have it insured by the Government.

We are not making any fight whatever on the Morris Plan Banks. They are engaged in the same line of business that we are, and we think they ought to be excepted. We think, too, that we ought to be excepted, and we believe we would have been had they known about this class of business.

It is a very serious problem with us if we are forced into the Federal Reserve System unless it is mandatory on the Federal Reserve bank to make a differential in the case of savings banks of, say, 1 percent.

The Federal Reserve Bank System will be governed by the large banks throughout the country, and the small State banks; in our State we have numerous banks with $15,000 or $25,000 of capital; and if they are going to fix the uniform rate—in fact, at the present time, so far as State banks in the State of Georgia are concerned, there are 224 State banks today and they are paying 2½ percent interest, on the ruling of the Federal Reserve Bank.

We are not in the Federal Reserve System, and we are paying 3 percent; we are doing that because the Federal Deposit Insurance Corporation has not the right, under the present law, to fix the rate of interest that we pay. If we are forced into the Federal Reserve System, unless we are given a differential rate, we will be in a bad fix.

The commercial banks in Atlanta—and I suppose the same thing applies to any savings bank—do not care anything about savings deposits; they say they are a burden, and they would rather not have them. But what they really mean is that they want to get the deposits and do not want to pay for them.

Mr. Spence. What do the State banks pay?

Mr. George M. Brown. The State banks pay 3 percent—all of them not in the Federal Reserve System. Those in the Federal Reserve System are tied up with 2½ percent.

Take a town in Georgia, one of our smaller towns, where we have a national bank and we have a State bank. At the present time the national bank is in the Federal Reserve System, and they are paying 2½ percent, and the State bank is paying 3 percent. Or, to reverse the example, take a town where there is one State bank in the Federal Reserve System and another State bank not in the Federal Reserve System. The bank in the Federal Reserve System is only allowed to pay 2½ percent. We think both of them ought to be allowed to pay the same.

I am not raising any point against the bill in any way, except to call your attention to the fact that our class of business is similar to that of the building and loan associations, and as near as possible to that in the building and loan associations as the mutual-savings banks.

The main difference between a savings bank and a commercial bank is the fact that what decides it is whether your deposit is subject to check or not. Take the Federal Reserve law; if you have a savings account they have to have a reserve of 3 percent. They differentiate between commercial accounts and savings.

Mr. Spence. What interest do you pay your stockholders?

Mr. George M. Brown. To be frank with you, we have not been able to pay them anything in the last 3 or 4 years. We started on $35,000, and we gradually got up to half a million capital, and we paid in about $150,000 of that surplus, and when we paid in for the stock we raised that surplus up to $500,000 and had $120,000 of undivided profits. But when this calamity of 1929 came along we marked off $400,000 from the surplus account to profit and loss.

We had built up that surplus account over a period of 35 years, and we paid as much as 8 percent to our stockholders.

We see no reason why because it happens to a Morris Plan Bank, with banks in different States that they should be excepted and we should not. They kept them well informed about their banks but they did not know anything about us; they did not know that there were any other banks except Morris Plan Banks. Their charter and our charter and their powers and our powers are the same.

One reason why we did not want to be in the Federal Reserve System was this: We did not want to be in the shape where the Government's $5,000 guarantee to building and loan associations is confronting us with 3-percent interest because we did not see where we were going to get off. It is bad enough now with them having 5 percent and we 3 percent.

The Government is interested in building and loan associations, and is interested in our banks. That is our whole fight. We want to be included. We have the same charter powers and we have no deposits subject to check, and we want to be included. Wherever the Morris Plan Bank is excepted we want to be excepted.

I think the Federal Deposit Insurance Corporation thinks we are right and I feel sure you will think so.

Mr. Howard. Mr. Chairman, we want to express our deep gratitude to the committee for the hearing you have given us. We appreciate it.

The Chairman. We are very glad to have had you here and we thank you for your statement.

STATEMENT OF CHARLES C. MAYER, WASHINGTON, D. C.

The Chairman. Mr. Mayer, will you come around, please, sir. You may give the stenographer your name, your address, and whom you represent.

Mr. Mayer. Mr. Chairman, I undertake to speak for the 80 percent or more of our citizens who are economically and financially disfranchised through the operation of this unconstitutional system. The Supreme Court has just affirmed or confirmed the decision of the Seventy-third Congress that the banking system interfered with the—rendered ineffective the power of the Congress; and the Seventy-third Congress set out——

Mr. Ford (interposing). Mr. Chairman, I would like to know who this man is.

The Chairman. I was just about to bring out that information, and ask Mr. Mayer to make a general statement as to whom he is and whom he represents.

Mr. Mayer. I appear here also as the friend of the court, or the honorable committee, and as a spokesman for the End Poverty in Civilization Society, that was started last year in California. I claim——

Mr. Goldsborough (interposing). What is the name of your organization?

Mr. Mayer. End Poverty in Civilization Society.

Mr. Ford. Would you mind stating where you live?

Mr. Mayer. 2015 Taylor Street NE., Washington, D. C.

Mr. Ford. You live in Washington?

Mr. MAYER. And it was organized——

Mr. GIFFORD (interposing). Is that the same as the End Poverty in California? Is that the same name for the whole organization?

Mr. MAYER. Extending all over the country.

Mr. FISH. Who is the head of your organization?

Mr. MAYER. Upton Sinclair.

The question here is the sovereignty of the Government or the sovereignty of the preferred class of bankers, who have ruled economically, except for a short period that Andrew Jackson put them out of business, a period of 20 years, when the national debt was entirely eliminated and the country had so much money that it distributed some surplus among the States. Private debts were practically negligible at that time.

The Civil War came along in the sixties, and at that time we were forced into an alliance with private gold-monopoly bankers, internationally allied, under the same conditions that the Bank of England was started, through merchants in Parliament and merchants out of Parliament cooperatively giving to themselves the power to issue money under the Government; and the same system that was inaugurated under Alexander Hamilton when his friends in Congress combined with his friends, his banker friends, in New York, to give them the issuing, the power to issue, money unconstitutionally.

They chartered the First Bank of the United States, unconstitutionally.

Thomas Jefferson said that a revolution was needed every 20 years to get rid of the tyrants. That bank lasted for 20 years; and those tyrants disappeared.

In 1817 or 1818 the second bank was chartered and it lasted for 20 years, until Jackson took away their power. And for the next 20 years we had a normal Government, a democratic form of Government.

Then, in 1862, 73 years ago, the Congress violated the Constitution and gave back to the private monopolists, the gold monopolists, the power to issue money.

Money—the definition, mine—is anything agents of the people choose to issue under their sovereign fiat power to serve as a legal tender, representative, token-instrument for value created or rendered by production or services to be used for the consumation and satisfaction of our commercial transactions, trades, and transfers of property, clearances, balances, settlements, and lawful obligations and debts, regardless as to whether it is an imprinted metal coin or a paper certificate, with or without intrinsic value.

Mr. FISH. Are you in favor of the central bank?

Mr. MAYER. Under State—under control of all 48 States—yes, sir; the same as we have our Government under the control of all 48 States, its Representatives in Congress, who alone have the power to coin money, to issue a sufficient quantity to carry on the business of the country, to regulate the value of that money by naming the interest charge, the same as the Treasury and the Federal Deposit Insurance Corporation undertook, in January, a two and one-half percent basis for savings accounts, a rate that is held in abeyance, so that Congress can decide what is a fair return. The President says the Home Loan should have 5 percent and the Reconstruction Finance Corporation says 4 percent, and has loaned on that basis. That control has been turned over unconstitutionally, I repeat, for 73 years, to private promoters, who have run the Government and have dictated the economic power of the Government.

Mr. GOLDSBOROUGH. Speaking concretely, you say you are in favor of a central bank, controlled by all 48 States. Do you have in mind the bill introduced by Mr. Sweeney, the Coughlin bill?

Mr. MAYER. Yes, sir; a bill similar to the one introduced last session by Senator Cutting.

We have got to have a representative government, and the vital fundamental, all-important, all-essential, power of the Government pertains to the economies that regulate the Government, to the money issuing power and the power over the sword. That is supreme. If we are going to turn the supreme power of the Government over to the private manipulators, we have no representative government. We have had no such representative government for 73 years, until the last Congress.

And this Congress has taken back, is getting ready to take back, that control.

The Government has failed in its duty and we have had barter and trade, reversion to the cave age of mankind, in various States, because they cannot get the currency they need to do business with.

They surrendered their power to the national Government and were not permitted to issue or to coin money, with the understanding that the general Government would supply them with the—with sufficient circulation, and that has never happened.

We have had 200 billion dollars of inflation; and I would be glad to submit the figures, more or less detailed, from official records, for the information of the committee, showing just how we had 200 billion dollars of inflation, and had complete deflation.

The inflation hijacked the prices of everything in the country, and the people contracted to pay those prices, and then, when the period of deflation set in, why, nobody could meet the prices, and homes had to be foreclosed, 10,000 a week. The record showed, in the Home Loan hearings, as per page 236 of the hearings on H. R. 5531 and figures obtained by Congressman McFarlane, of Texas, 275,000 individual urban homes and 244,000 farms were wiped out in one year, because of the scuttling of humanity.

And nothing has taken the place of that 200 billion dollars. Yet we hear objection to just replacing 2 or 3 or 5 percent of that in real money. We have based everything on a few billion dollars of gold, which is not money and is worthless except as a commodity that may be used in the arts and trades, unless it has the fiat stamp of the Government on it, with enough alloy to keep it from wasting away, to make it legal tender. It is no more legal tender than our greenbacks were and greenbacks are backed up by all the energies and all the intelligence and services and productive capacity of 126 million people, which makes our money supreme. The Supreme Court was unanimous—Mr. Gifford spoke of eight members being unanimous on one point. It was unanimous.

The CHAIRMAN. It was Mr. Hollister.

Mr. MAYER. Oh, it was unanimous in saying that Congress has been or is unconstitutional. Four members, the minority, said they violated the supreme sanctity of contracts. Five said they had violated the Constitution by interfering——

The CHAIRMAN (interposing). Eight of them said——

Mr. MAYER (interposing). No; five said they interfered with the power granted to Congress or interfered with the power of Congress. I have that here somewhere.

Mr. GOLDSBOROUGH. I think all the members of the committee are familiar with the decisions of the Supreme Court.

Mr. MAYER. I would like to get that exact wording: "Interfered with the exertion of the power granted to the Congress." That was the majority. And that has been going on, as I said, for 73 years.

Mr. FISH. Mr. Chairman, can we find out whether the gentleman is advocating any specific legislation?

Mr. MAYER. I am advocating the central bank, proposed by Mr. Sweeney, with some elaborations to get rid of some of our $250,000,000,000 of debt money and in its place a little constitutional money, that will liquidate debts, and not keep the entire public in subjugation, and not destroy our democracy, and not encourage socialism, that the President, on the 12th day of this month, says must be combatted in business, in order to prevent its spread nationally. I am opposed to the promoting of communism, that the bankers' community of interest promotes.

The CHAIRMAN. You and Mr. Fish are agreed, then?

Mr. FISH. I would like to have someone liquidate my debts. I want to find out how to do it.

Mr. MAYER. I will give you that formula. I have been advocating it for years. I also found that Speaker Byrns, on the 15th day of June, in the Congressional Record, page 11836—I think that is the exact page—said that Congress had been modest in its expenditures, compared with its power to secure money. He said that we could issue $10,000,000,000 of cash legal tender, safe, constitutional money—not in those exact words—and redeem it by laying aside the revenues from alcoholic taxes. On the same basis you could issue any part of twenty-five billion to fifty billion of dollars by laying aside the excess revenues, after allowing a fair return, to the power interests, on their portion of over a billion dollars of revenue per year—take the more than 3 percent that Congress now collects—after two efforts, through Congress, the first of which was beaten in conference by Mr. Crisp of Georgia, who was kept at home because he beat it—and increase that 3 percent revenue up to 50 percent or more, if necessary, and lay that aside, $500,000,000 a year, and in time you will have enough to liquidate the twenty-five or more billions of honest legal tender cash.

A fair return—the Supreme Court's last decision is the going value of money. A previous decision was, in the *Baltimore Rate case*, 7.46 percent. The Treasury Department has been trying to fix it at 2½ percent, one-third of 7.46 percent. If the utilities are allowed to earn 2½ percent on a guaranteed basis, then all the revenues between 2½ percent and 7½ percent can be allocated for the use of the people of the United States, whose wealth it is. They produce that wealth.

Mr. FISH. How would you get the money used for relief purposes at present?

Mr. MAYER. Issue bonds to the Treasury Department instead of to the bankers, and let the Treasury Department hold those bonds for the date of redemption, and deposit them against money issued the same as the bankers do the bonds now given to them.

Mr. FISH. The banks draw interest on the bonds?

Mr. MAYER. Yes; and let the bonds draw sufficient interest to liquidate them in a given number of years, issue money against them, set aside whatever revenue from cigarette taxes, 60 percent of th consumers' purchase price, or alcoholic taxes, or gas company taxes, the gasoline and power company taxes, any taxes you need to levy on, to liquidate those bonds, and issue your honest money, not subject to inflation by the bankers, not subject to deposit as reserves and inflation 10 or 20 times, as Hamilton at first proposed, and actually operated.

Mr. FISH. What would you do with the bonds that are now outstanding?

Mr. MAYER. Gradually, very gradually, slowly, replace them with tax-redeemable bonds.

We have followed the fraudulent British system of money all through our history; and they are talking about not impairing the credit of the Government, because we have not reached the limit that the Bank of England has reached, or the English Government has reached, which is a false model to follow. We broke away from England to get away from its money controls; and immediately we lost our independence when we subjected ourselves to the same kind of money controls. We have had no democracy, such as the patriots of 1776 fought for. We have never had the opportunity to deal among ourselves on a fair and equal basis, with justice, even-handed, distributed to all. We can never have any such democracy until we are able to independently deal with one another on a settlement basis, in cash, without being tied to bondage slavery and debt.

Mr. CLARK. If you called in these bonds and replaced them by currency, you would not cancel the bonds, you would deposit them in the Treasury?

Mr. MAYER. If you called in the outstanding bonds and replaced them, you would have to issue new bonds, liquidated by tax revenue.

Mr. CLARK. You would not issue currency to pay off the present outstanding bonds?

Mr. MAYER. Not without new bonds to be liquidated through revenues accumulating from taxes.

Mr. CLARK. The original statement was that, instead of issuing bonds when the Government needed money, that it would issue bonds and deposit them merely in the Treasury instead of in the national banks.

Mr. MAYER. Yes, sir.

Mr. CLARK. Why do you not follow that method in paying the outstanding bonds that are now held in the banks?

Mr. MAYER. I would follow that and redeem them.

Mr. FISH. I am not at all worried about the so-called "distribution of wealth." I am a little bit worried about the distribution of poverty. That is what I am afraid of; and your organization is to end poverty. Cannot you tell us how you are going to end poverty?

Mr. MAYER. Yes. I am on the opposite viewpoint from you, the same as I am on the opposite viewpoint from Dr. Spahr. Yesterday he assumed that when we used money——

The CHAIRMAN (interposing). Neither one of you believes in communism, I understand.

Mr. MAYER. Yes, sir.

He is opposed to national communism and I am opposed to bankers' communism. We have had redistribution of wealth in the last 5 years. We had redistribution of wealth in 1929, 1930, 1931, and 1932, concentrated into fewer hands than before.

Seven times we had a panic, whereby—I have the figures; I have dug them out, after a great deal of trouble—$200,000,000,000, nearly, of stock market inflated values were deflated.

Mr. FISH. Distributed?

Mr. MAYER. Distributed among the bankers.

Mr. FISH. Do you not think that the rich man has had his fortune pretty well distributed in the last few years, not necessarily from the stock market crash, but from the deflation of real estate values and other values? Don't you admit that?

Mr. MAYER. I admit that he has lost a portion of his fraudulent wealth.

Mr. FISH. He has lost at least 50 percent of his wealth?

Mr. MAYER. He has lost probably 50 percent of what he fraudulently gained prior to 1929; and every panic has redistributed wealth in the hands of fewer and fewer people. Now, that has been going on 40 percent of the time, 1 year out of every 2½ years, when we have had a depression.

Mr. FISH. Now, can you tell us how you are going to end poverty?

The CHAIRMAN. Just a monent, gentlemen. I want to suggest that the committee meet in executive session at 3:30 o'clock. I hope all of the members will come. That meeting will be held in the other committee room, at 3:30 o'clock.

Now, you may proceed, Mr. Mayer, with your statement, before we quit.

Mr. MAYER. When Congress decides——

Mr. FISH (interposing). Could he tell us, briefly, how he proposes to end poverty? That is what his organization stands for and it is a very interesting proposal.

Mr. MAYER. I would end poverty by producing all the wealth we reasonably can, with all the facilities now prevailing, improved upon.

Mr. FISH. Well, then, you mean that you would abolish the A. A. A. and the N. R. A.?

Mr. MAYER. I do not believe in any of the palliative, alphabetical, soup tureen, bread-line measures.

Mr. FISH. This is treason, Mr. Chairman.

Mr. MAYER. They are all just camouflage. The big problem is how to get back to the Andrew Jackson Democracy——

The CHAIRMAN (interposing). Let me suggest to you that Mr. Fish has directed your attention to a line of questions that we would like to hear discussed.

Now, you say that you are in favor of unrestricted production?

Mr. MAYER. Yes, sir.

The CHAIRMAN. Now, will you follow up that line of discussion.

Mr. MAYER. The average income per family is under a thousand dollars. I think in 1929 it was around $800. The Brookings Institute has told us that $2,000 is the subsistence level. The President, I think, says around $1,800, and other authorities go a little higher. Take the standard of living figure of the Brookings Institute, $2,500; and if we had $2,500 a year for 25 million families or 30 million families, we would have had 75 billions of dollars, that would turn over a number of times, and it would outstrip all our present productive capacities. We could not produce goods enough to meet the demand. Never in history have goods been produced in such quantities that they could not be consumed. The reason was that there was no purchasing power. There was no means of distributing these goods. Everything in America has been tied to the banker's control, his power.

Mr. FISH. Your proposition is that we cannot overproduce goods and commodities; that there can be no such thing as overproduction?

Mr. MAYER. No such thing as overproduction, because we have never had anything but underconsumption.

The CHAIRMAN. Now, you do not mean to say that you could not overproduce? But you mean to say that we never have had overproduction.

Mr. FISH. That is what I wanted to find out, because I wanted to follow it up by the question that you could certainly in a month's time produce more shoes than the people could wear, or more toothbrushes than they could use, or hats, or anything else.

Mr. KOPPLEMAN. Just at that point. I heard you say that $2,500 would do it; but, if you took an average of $2,500, would not that be inflation which would result in that $2,500 only building up the purchase prices? What about the quantity in goods and services it would purchase?

Mr. GOLDSBOROUGH (interposing). Just a moment——

Mr. KOPPLEMAN. I would like to get that explanation. Would not you right now get back to the basis we now have? I might extend my question on the same basis and ask, if Mr. Townsend's plan for old-age pensions went through, then, if at the end of a year his $200 a month would not have dropped down to $30 in purchasing power, so that they would not be any better off by reason of the fact that they got more money?

Mr. GOLDSBOROUGH. I presume your answer to that would be that production would increase correspondingly with the increase in money, so that there would be no raise in prices, no inflation? Is that what you mean?

Mr. MAYER. Yes, sir. here would be a balanced production. It should be developed gradually.

Mr. KOPPLEMANN. That does not quite answer my question.

Mr. GOLDSBOROUGH. If you do not increase your money any faster than you increase your production, then you will not have any inflation.

Mr. KOPPLEMANN. Now, if you do not mind, let us get to that thing. If I have $18 and if I can buy for that $18 a suit of clothes; and then, next week, instead of $18 I am getting $25 and I cannot buy any more than that same suit of clothes, that cost the week before $18, but due to the fact that more money has been given to me the price of the thing has increased correspondingly—and it would increase correspondingly—therefore I would be no better off by reason of having that $25 than when I had the $18.

Mr. MAYER. On that hypothesis, yes; but if you used your $25 to liquidate your debts then you would be that much better off.

Mr. KOPPLEMANN. You are talking now about paying debts and are not answering the question asked you.

Mr. MAYER. Well, used for constructive purposes, and not used entirely for one purpose, but used in a balanced way. Say that you are going to pay—you are going to get $6,000 revenues next year instead of $3,000, and the mortgage on your house is——

Mr. KOPPLEMANN (interposing). I can readily see the wiping out of debts, that you intend to argue with me. Now, I am talking about purchasing power, underconsumption, and overproduction, and the problems they involve. Let us confine ourselves a moment to that question. I am very much interested in the value of this money for the purpose of taking up production, so as to give everybody employment, and that is the foundation of my question. I am trying to arrive at a situation where there would be enough produced to give all the people jobs.

Mr. MAYER. Only in a very gradual, slow development can that be done without disturbing our equilibrium. We cannot have a crash or an expansion suddenly without upsetting our whole national economy, which has just been upset because we had a crash from $200,000,000,000 of bankable, negotiable values that floated around in the channels of trade to nothing now. We cannot reflate $200,000,000,000 instantly without calamity. Give everybody a job at a dollar a day, if necessary, to start with, more or less, and then gradually build up the consuming power and gradually build up the productive power and not make all the shoes that people, surplus numbers, were devoted to making at one time, and include the production of every other necessity of life to balance that production.

Mr. KOPPLEMANN. Well, you based your statements on that Brookings Institute analysis of the situation, which they have just investigated, over a number of years; and in that Brookings Institute statement, the summary of it is that if you were to raise the people's income from $2,000 to $2,500, it would take care of production, so that there would not be overproduction; and you have just confirmed that, that there never was such a thing as overproduction; that it was always underconsumption.

Mr. MAYER. Yes.

Mr. KOPPLEMANN. I am inclined to go along with you on that thought. But what stops me is the question I put to you, namely, what difference will it make if they get $2,500 instead of $2,000? I want to see an increase of production, so as to provide employment.

The CHAIRMAN. Mr. Kopplemann, it would not make any difference, if there was no change in production, and you would be entirely right. It is Mr. Mayer's conception that, with the provision of an increased income, production would be immediately absorbed and that, as production was increased, distribution would take place among the people without any rise in prices.

Mr. KOPPLEMANN. Yes; that is what you have got just now. You have got——

Mr. MAYER (interposing). Yes.

The CHAIRMAN. You have got that same principle applicable, for instance, Mr. Kopplemann, in the case of wheat. Suppose you had 20 bushels of wheat. Wheat would be worth, we will say, a dollar a bushel. Now, then, if you had 40 bushels of wheat, if you doubled your production of wheat, you could bring $40 into the picture, and still your wheat would be worth only a dollar a bushel. If you increase your production, as you increase the money increase the supply, you will not raise the price level, for it does not get out of balance.

Mr. KOPPLEMANN. Do you think that the increase or the decrease of the volume of money alone would solve the problem?

The CHAIRMAN. Do I think so?

Mr. KOPPLEMANN. Yes.

The CHAIRMAN. Oh, no; I do not. I think it is one factor in the solution.

Mr. KOPPLEMANN. I was going back to Governor Eccles' theory.

Mr. MAYER. The money must not be put into circulation unless there is something to represent it.

Mr. KOPPLEMANN. That means purchasing power?

Mr. MAYER. No; it means value.

Mr. KOPPLEMANN. If the money does not represent value, you do not have the purchasing power.

Mr. MAYER. Yes, sir; and if you are going to go back to the 1929 level of true income, not $2,000, but $800. Increase up to $900 or ten hundred—you cannot do it in 1 year—and go on up to $2,000 and then stabilize your prices; not make them subject to the bankers' inflation and have everybody contract and buy on high prices and then let them call their loans, that are inflated by them 10 to 20 times based on what they call the reserve. They have no right to have the reserve of the country in the banks.

Mr. FORD. Don't you see in the bill that we are considering a very substantial step in that direction that you have in mind?

Mr. MAYER. Unquestionably. This present Congress and the last Congress have been determined to crystallize the demands of the country; and they have the genius to go ahead and put those demands in such form that people can get money more freely and liberally than they have heretofore, through this bill, with whatever improvements can be injected into it, against the opposition of the greatest force and the greatest power there is in the world, that controls the money, the international control of money, which has been set aside, slightly, now.

In 1763 the British Parliament declared all colonial acts for the issue of paper currency—legal tender—to be void. A year later the British Board of Trade went on record in opposition of any of the Colonies exercising local sovereignty to issue its own money, independent of the dictation of Great Britain.

Private "money changers" who had been in control of the money issuing monopoly manipulation privileges over credit inflation and control of wealth, demanded that only those who hoarded gold in vaults had authority to issue diluted paper money tokens, bank notes, bank debts, and credits as substitutes for a fractional amount of "intrinsic" value in gold. Private bankers for 70 years had usurped this authority in England and operated it as an exclusive racket.

American colonists had no gold or coins except a meager supply that came from England and Europe to balance trading accounts. Dominating the supply of money and trade was more potent than control by political persuasion.

Taxation measures, stamp taxes, payable only in English money, credited instant friction. Force was used to compel obedience to trade and tax measures. British soldiers were quartered in New England. Friction caused the Boston Massacre, 1770. Three years later the Boston Tea Party resulted in further restrictive measures. Two years later the skirmishes of Concord and Lexington hastened the Declaration of Independence, 14½ months following.

Fiat money issued by the Continental Congress, helped by some specie money from "prizes" captured at sea, from trade credits, and some metal money and military support supplied by France, won the War of the Revolution.

Determination to be economically free from money controls in spite of large numbers of royalist Tories, sustained by intense loyalty of devoted patriots to self-control of their economic destiny and liberty surmounted all hardships regardless of the lack of money and bare necessities.

Desperate financial conditions were indicated by the petition of soldiers presented by General MacDougall to the Continental Congress January 6, 1783. Demands for pay included these expressions: We are unable to go further—we have borne all men can bear. Our property is expended; our private resources are at an end. We beg a supply of money. We have been the sufferers by hunger and nakedness and wounds. Seven long years have made conditions wretched. They (soldiers) entreat independence of America shall not be placed on the ruin of any particular class of her citizens. Without some payment a mutiny might ensue. The Army is verging on that state which will make a wise man mad. Congress was taunted with the fact legislators always paid themselves and as regularly left unpaid the military.

On June 9, 1783, a few hundred mutinous infantrymen stacked arms before Independence Hall, threw rocks, refused to disperse. Alexander Hamilton advised Congress "think of eternity", as he did not believe they had "more than an hour to live." Pennsylvania's own militia, insubordinate, offered no protection. So Congress at night fled to Princeton and later to New York.

In 1786 Shay's rebels prevented the Massachusetts Supreme Court from sitting. They engaged in skirmishes with the State militia with a few casualties, tried to capture the arsenal, and burned a few buildings. They demanded pay for Revolutionary War services. They opposed extravagant pay of the Governor and complained of extortionate, predatory policies of lawyer legislators that burdened the poor with taxes.

After 5 years of exhausting human wastage, conditions today are much the same.

Alexander Hamilton was a radical inflationist. As early as 1780 he proposed a Bank of the United States with "a foreign loan of $200,000,000; a subscription of $200,000,000 more guaranteed by $10,000,000 of specie or a bona fide equivalent currency." That is inflation 20 times.

The half-British Hamilton, opposed by Thomas Jefferson and James Madison, evidently hoodwinked George Washington in the establishment of the First Bank of the United States in 1791, patterned after the Bank of England.

Washington had expressed his fear of fraud thus:

> The wisdom of man, in my humble opinion, cannot at this time devise a plan by which the credit of paper money can be long supported.

Through Hamilton's privately established, Government allied, privately controlled bank, the wealthy citizens whom Hamilton thought alone were fit to govern, inflated and juggled values on a thin basis of deposited specie money. That constantly increased their wealth. Hamilton's friends in Congress put through a funding operation to pay off war obligations due to Revolutionary soldiers and others. They bought up these claims for a few cents on the dollar, and cashed them, through a cooperating private bank, for 100 cents on the dollar. Government funding obligations carried 7 percent and 8 percent interest. The Government was pledged to buy $2,000,000 of the private bank stock, through notes.

Hamilton had drafts issued on European bankers for $2,000,000, had them credited on the books of the bank, transferred the credit to the account of the United States on the books of the bank, protected by Government notes, and then canceled these trumped-up drafts, which were never intended for collection. Reference: John McConaughy's Who Rules America, pages 33, 34, and 35. This operation created $2,000,000 of privately issued, intangible money. Similar methods have been pursued by the private bankers in control of the money power of the country throughout the history of the United States.

Regarding funding schemes William Pitt, British Chancellor of the Exchequer, is credited with this statement:

> Let the American people go into their debt-funding schemes and hazardous banking systems; and from that hour their boasted independence will be a mere phantom.

In regard to the Civil War inflation Abraham Lincoln said:

> If a government contracted a debt with a certain amount of money in circulation and then contracted the money volume before the money was paid, it is the most heinous crime that a government could commit against its people.

The United States Monetary Commission of 1876 made an exhaustive study of the terrible depression following the Civil War. A few of the conclusions of the Commission I outline briefly, as follows:

> Price is the relation in money units to the quantity or unit of every other thing in exchange. Under a credit system, to pay at future periods, steadiness in prices becomes all-important, and depends upon the quantitative relation between money and all other things. All contracts are based on existing prices.
>
> Generations of falling prices and ruin might come and go before relief—

if dependence were had on pure gold supplies, through the lapse of centuries, to match the relative amount and activities and services that human progress demands.

Metallic intrinsic values are based on gamblers' chances and on finding precious metals, and there is—

no scientific relation to the increase or decrease of population and commerce, which alone should govern the stock of money.

Limitation of quantities regulates the volume of money—

whether imposed by fiat yield or by nature's yield. Fiat yield is measured—

by the wisdom and justice of man. The value of money is measured by the cost of obtaining it.

A balanced supply is necessary for equity to debtors, whose contract terms must be met by submitting—

to the partial or entire confiscation of property—

when money ceases to circulate.

Money is the primary and governing force, whose functions cannot be superseded by any devices, checks, bills of exchange, clearing houses. These expedients grow out of money and could not exist without it.

Use of government fiat money is the one important advance civilization has made over barter. Credit money was impossible under the barter system and is a corrupt use or exploitation of the money system. Volume of money controls prices, not volume of credit.

Credit is the explosive element in business. There never can occur a universal fall in prices without a decrease in the volume of money.

Credit depends upon liquid cash value, which collapses when inflated credit collapses.

This explains why, since 1929, the Government has been virtually compelled to squander $500,000,000 under Hoover to help peg farm products and why thousands of millions of dollars in the past 2 years have been employed to minimize the collapse of values of all kinds, to maintain other related values.

Money alone, actual money, liquidates debts.

Credit depends upon whims and caprices, on abnormal mental conditions of the moneylender, a disease which must be treated psychologically.

Long-term stretching of debt credit money for homes, and so forth, now take the place of collapsed credit, to prevent further collapse of values.

It is notorious that most of our universities have been built with endowment from privately acquired bankers' monopolized and usurped wealth. The jobs of nearly all of the 66 so-called "economists" signing a memorandum of objections to title II of H. R. 5357 may be considered subsidized, endowed, or controlled by usurped wealth. Practically no one of the 66 signers has qualified as an independent, untrammelled, or free and unprejudiced student of the money question. Orthodox and confirmed tories, maintained in jobs because they are orthodox, because confirmed tories, cannot render disinterested opinions, except as orthodox, confirmed tories. These 66 men had as their spokesman yesterday Dr. Walter E. Spahr, of New York University, unquestionably a confirmed, orthodox disciple of predatory wealth.

The Supreme Court sustained the action of Congress in nullifying impossible contracts to save the existence of the Government, through the supreme power of Congress. Justice Stone explicitly stated that "power to regulate the currency which we now hold to be superior to the obligation of the bonds."

Prof. Walter E. Spahr, spokesman yesterday for the 66 economists, evidently considers the money decision of the Seventy-third Congress, affirmed by the Supreme Court, as a forgery—false utterance.

Dr. Spahr is correct regarding the "creating of money by borrowing—but not from bankers—and through taxation." Borrowed bankers' money is merely borrowed Government money, created and issued by the Government. Therefore, Congress would "render ineffective the power of Government" over the supply and control of money by not issuing its money direct through the Treasury Department upon the deposit of authorized, self-liquidating bonds.

Congress should borrow and create money only on the taxable, redeemable assets of all its citizens and not through the preferred privileges and powers heretofore allowed to a small class of private citizens who have controlled the congressional power "to coin money, regulate the value thereof" for many decades.

Bankers should not exist on a Government-subsidized, bond-based, dole system; but as conservators and custodians of wealth left in their protection for safekeeping and administering. Some bankers are finding it necessary to meet expenses by charging for such services, as lawyers would do. Let the depositors pay for protection from burglary. Let bankers collect for services by acting as local agents for the State authority to be set up to administer the "coin money" and regulatory powers of the National Government, not by inflating credits and manipulating values for their interest yield and confiscatory possibilities. Methods in use up to now have always caused economic crashes and bank collapses, that have constantly accelerated the concentration of wealth.

Ill fares the land, to hastening ills a prey,
Where wealth accumulates, and men decay.

New banking legislation must minimize control of the constitutional power to regulate money by private bankers, who have been sustained on a dole basis for many decades, to dominate and control the economic welfare of all the people of the United States.

The CHAIRMAN. Well, I had understood that Mr. Mayer would finish in 15 minutes. I appreciate the fact that he cannot say what he wants to say in a few minutes. I will make this suggestion, that you can extend your statement in the record by adding further expression of your views.

Mr. MAYER. I thank you, sir.

The CHAIRMAN. And I want to say to you that members of the committee appreciate your statement.

Mr. CLARK. I want to say, too, that I have a little different idea.

Mr. GOLDSBOROUGH. I would like to say that I consider Mr. Mayer's statement extremely helpful to this committee and to his country.

Mr. MAYER. I more than appreciate your courtesies.

(Thereupon the hearing was adjourned, subject to the call of the chairman.)

EXTENSION OF REMARKS, C. C. MAYER

Excerpts cited from United States Monetary Commission, United States Senate Reports, Forty-fourth Congress, appear volume 5, part I, pages 33–37.

Concerning Hamilton's Government-allied bank, "Who rules America?" reveals, page 35, "it was Hamilton's custom to borrow money from the bank when there were sufficient Government-tax funds available to meet Government requirements."

Regarding 200 billions of bankers' promoted inflation and deflation, United States Senate Hearings on Stock Exchange Practices, page 7923, part 17, lists 33 of the largest banks of America as promoters of stock-market pools and syndicate operations. These 33 top-notch banks are located in 10 cities: New York, Boston, Providence, Philadelphia, Pittsburgh, Cleveland, Chicago, Milwaukee, San Francisco, and Los Angeles. Two other greatest banking institutions, the Rockefeller Chase Bank and the J. P. Morgan partnership of 19 bankers, along with Detroit banks, had their infamous operations exposed in extended hearings that covered their notorious exploitations to the extent of hundreds of pages.

Congressman A. J. Sabath's committee currently investigating real-estate reorganizations has reported defaults upward of 8 billions. Deflation of many billions of dollars in real-estate bonds has crippled 4,000,000 of America's thriftiest investors and savers, affecting "indirectly 20,000,000 of our citizens", says the report submitted January 29, 1935.

Senator Hiram Johnson's investigation in 1931-32 of foreign-bond promotions by New York bankers revealed many billions of these bonds defaulted, with much of their value wiped out and lost to innumerable investors.

National City Bank stock values were inflated to a valuation of $3,190,000,000, at $580 per share, with promises of much higher value. More than 3 billions of this "established" stock-market value was wiped out. Similarly, the Rockefeller-Aldrich-Al Wiggins Chase Bank stock, the George Baker-Sam Reynolds First National Bank stock, Sam Insull's 2 billions of inflation, and a few other over-the-counter (or over-the-fence) cats-and-dogs approximated another 10 billions of deflation in bankers' negotiable values.

Rockefeller's Standard Oil of New Jersey was inflated to $2,160,000,000, at $84 per share, was pegged temporarily at $50 per share, and shrank to one-fourth of its boomed price. Kentucky, Indiana, and other Standard Oils were overvalued other billions. J. D. Rockefeller, Sr., and Jr., halted the first great stock crash by propagandizing through stock-exchange tickers: "Me and my son are buying safe stocks." There were no safe stocks, as demonstrated by six new, successive panic smashes, bear raids, deflations, between November 13, 1929, and July 1, 1932. Rockefellers' New Jersey and Indiana Oils were deflated 3 billions between them.

Morgan's Alleghany Corporation, United Power, Standard Brands, United States Steel were fictitiously valued, collectively more than several billions in the bankers' slaughter-house boom. United States Steel was inflated to $261 per share and has sold much below its recent $30 price. More than 2½ billions in "values" disappeared when these frauds were deflated.

The Morgan partners' General Electric was inflated to nearly 3 billions; Morgan's Electric Bond & Share and its American & Foreign Power, both stepchild brats of General Electric, were inflated above another 3 billions. These three produced a holocaust of paralyzing losses in "values" more than 5½ billion dollars. General Electric deflated 2⅝ billions, Bond & Share over 2⅓. The latter was rigged to $189 and dropped to under $5 per share for its 13,560,000 shares.

The blue-ribbon ringleaders of superlative inflations and deflations were the Morgan-Baker dominated American Telephone and the Morgan-Du Pont-Raskob General Motors. Motors was rigged to 4 billions and deflated to one-third of 1 billion, dropping 3⅔ billions.

Du Pont de Nemours stock, which holds nearly 40 percent of General Motors, was juggled to a "value" of 2⅝ billions and reduced to one-eighth billion. American Telephone was the largest culprit. Telephone subscribers were baited with this "investment" to a valuation of $4,350,000,000 which shrank to less than 1 billion. From $310 to $70 per share for 14 million shares.

Preceding the second Hoover panic of May-June 1930, stock-market jugglers employed by American Telephone's masters unloaded over one-half billion new stock on preferred subscribers with "rights" at $250 per share. Two months later, in May-June, American Telephone became deflated in value 25 million dollars average every day for a solid month, reaching a total shrinkage over 800 million in 30 days.

Anaconda ("any large snake which crushes its prey in its folds") Copper stock was rigged to $174 per share for 8,840,000 shares and sunk to $3, a drop of another 1½ billions of bankers' credit inflations.

Almost as shamefully as Anaconda was Kennecott Copper whirled about to $104 high and $5 low for 9,385,000 shares, nearly 1 billion shrinkage.

Inflation and deflation of only two railroad exploitations equalled 2⅗ billions of disappeared "values." Pennsylvania with its Penn Road monstrosity subsidiary and New York Central with its exploited pets were boosted to $110 and $256 per share, respectively, and dropped to to $6.50 and $8.75 for their 13 and 5 million share issues.

The Federal Trade Commission reveals that H. L. Doherty unloaded his Cities Service stock on the public, with the help of Nation-wide newspaper supported publicity and advertisements, to such an extent that Doherty was able to "take" for himself over $18,000,000 in cash "commissions" and profits. The Kansas State Banking Department reported 10 prior liens approximating $500,000,000 "before Cities Service common (stock) would participate * * * of questionable or worthless value." Cities Service printing presses ran off 29 million share-certificate substitutes for money to unload as high as $68 per share, and with a price deflation under $1 March 29, 1935. A drop of two-thirds of $100 per share shows worthless inflation around 2 billion dollars by H. L. Doherty.

Bankers' manipulated New York Consolidated Gas was floated as high as $183 with 11½ million shares. Current prices $15 to $20 show a shrinkage of nearly 2 billions in inflated paper stock substitutes for money, sanctioned by bankers.

Columbia Gas & Electric, United Gas Improvement, North American (electric utility), collectively inflated their printed paper money substitutes to within a few millions of 4 billion dollars. Evaporation of bank-made "values" in these three cats-and-dogs exceeds 3⅗ billions.

International Nickle and International Telephone jointly became worth 1,900 hundred million, and later less than 100 million according to "bankers' valuations" to show deflation of 1⅘ billions.

Radio Corporation of America was run up as high as $540 per share and ran down almost to the vanishing point to show 700 millions of evaporation.

Foreign bonds and real estate floated bonds were exploited over 10 billions of deflation and losses.

Over-the-counter New York bank stocks (three of them), Sam Insull's stocks, and several others show more than 10 billions inflation-deflation.

A score of New York Exchange stocks recorded above were inflated and deflated collectively more than 35 billion dollars.

Over 1,200 other New York Exchange and 800 Curb Exchange stocks aggregated more than an additional 100 billions of inflation and deflation.

Bonds and preferred stocks on the two New York Stock Exchanges alone were boomed and broken more than 20 billions in "values" by bankers.

Loans and discounts with the resources of all our banks were expanded and contracted much over 20 billions, from 60 to under 40 billions.

Urban home and farm home values were contracted 15 billions, more or less.

Defaulted debts of foreign governments exceed 10 billions deflation.

Individual unable-to-pay debts run many billions.

Authentic, official records prove the correctness of the approximations given above and show conclusively that there has been much over 200 billions of disappeared values to vitally shake the economic welfare of more than 80 percent of all our citizens. They prove the necessity of promoting "the general welfare" by restoring the well-being of our economically disfranchised citizens. Without restoration there can be no recovery.

"The epoch of the decline and fall of the Roman Empire" was due to failure "to solve the problems of the poor", says J. Blake Lowe in the February Forum, 1935. "Money got out of hand", says H. G. Wells. "Decline in the silver and gold mines of Spain and Greece" (contraction in the circulation of money tokens), says Sir Archibald Alison. The natural, early conception of money, of numerical, quantitative money used as symbols and tokens (numerata), became a thing, gold, and for a while silver, radiant and glistening—which a few learned to control—(moneta). Then it took another step toward materialism according to arbitrary weight (ponderata). When "the weights were degraded, the thing fell to barter", says A. Del Mar, a British authority, in 1886. He states the Renaissance reestablished weights first and then "pounds, shillings, and pennies, dennies, or denarii, which passed by tale." Nations have succumbed to the hypnotism of gold, the lure of spoil.

Prophetically, Del Mar observed: "Metallic money seems like one of the machines designed by illiterate mechanics for perpetual motion; it carries with it its own negation. * * * It has begun to fail from the very instant when it was first set in motion. * * * The civilization of India, of Egypt, of

Greece, and of Rome have all moved toward a vanishing point, and that is where gold and silver mining ceased to be sufficiently productive; and unless proper measures to avert it are adopted in time, it would seem that that of the modern world must move in the same direction."

History is strewn with the wrecks of governments and civilizations. The greed of money changers has ruined many.

Canada's Minister of Trade and Commerce, Harry Stevens, says "big business", made up of "unscrupulous financiers and business men, exploited Canada's consuming public, starved her producers, sweated her workmen, gouged her industries, and left her a choice of reform, dictatorship, or revolution."

Mr. Chairman, shall repressions, recessions in the circulation of currency, denials, depressions, poverty, restrictions, and destruction of our "surpluses" (undistributed) prevent a bountiful life and crush or sink our civilization?

Japan threatens our white and mixed-race population. Shall our white people survive?

Japan buys surplus crops of food, cotton, and especially scrap iron. We junk or sell as junk or destroy the natural wealth that Japan buys. Japan's commerce grows all over the world. Ours decays.

The glory that once was the United States fades. Our people grow constantly poorer, subjugated by monopouly master kings of coined boodle who control our wealth, our economic and industrial facilities. They refuse to let 100,000,000 people produce their necessities. Natural wealth is destroyed, not distributed. Prices are increased artificially. Scarcity is increased. Poverty is increased. With Japan the picture is entirely reversed. And Japan conquers the trade of the world while the "glorious" United States declines and fades out of the picture.

All American values dealt with above, Mr. Chairman, and other existing values, especially stock market quoted "values", are arbitrary values, wholly dependent upon Congress' regulatory power to stabilize valuations by limiting earnings and taxing the surplus above maximum earnings. Stock-market masters have ruthlessly ruled in juggling values. They have run wild in fictitiously fixing manipulated prices and in usurping extravagant profits.

Because the weights, values of money, and money instruments in America have been expanded and degraded over 200 billions in recent years, as summarized above, business in hundreds of communities throughout the United States "fell to barter" as during Rome's declining epoch.

Financial tyrants have monopolized the money power and economic functions of Government for the benefit of financial tyrants. An overwhelming harvest of greed, graft, and financial corruption, with wars, almost starvation, have disruption or depression 40 percent of the time, want, poverty, starvation, have resulted. To palliate poverty is no remedy. To promote democracy, money must circulate freely to liquidate debts and abolish poverty as nearly as possible.

More bondage indebtedness without adequate tax-redeeming measures means more poverty for the masses, less liberty, less economic freedom.

"Orthodox" Wall Street stock market operators consider their accumulated wealth not only legitimate but praiseworthy. They pretend to be public benefactors. They own the tax-bearing bondage bonds sucked up through Wall Street's machinery.

Andrew Mellon, John D. Rockefeller, J. P. Morgan, John J. Raskob, H. L. Doherty, the Du Ponts, and others consider themselves outstanding patriots.

This current week a large Wall Street operator (B. M. Baruch) revealed to the United States Senate Munitions Committee he has $7,000,000 in Government bonds laid aside. His constructive efforts in life have been devoted to bankers' inflations and deflations, pool operations, etc., through Wall Street. His one item of wealth in seven millions of Government interest-bearing bonds enable him to spend or squander $1,000 per day for 7,000 days. Continuously for over 22 years, omitting Sundays, he can squander dollars at the rate of a hundred $1 bills every hour for 10 hours each day, without touching any of his interest coupons or other wealth. Some consider this kind of wealth legitimate or "patriotic" wealth.

All holders of United States bonds, and amounts held, will soon be listed for Congress.

Masters of monopoly money controls have ruthlessly raided the ranks of the masses of mankind by inflation and deflation, to strip them of their earnings and accumulated savings periodically. In this way, according to incontrovertible evidence, the few have grown steadily more powerful by subjugating the masses with increasing poverty. And the poor have grown more numerous in constantly widening circles until they threaten to engulf the whole of humanity unless enlightened money policies of Congress provide a method of escape to undo the wrong policies of the past.

Constitutional control of money by Congress, replacing bankers' control, alone can halt and prevent usurped attempts at unlimited license to loot; the economically strangling usurpations such as have reddened the records of human welfare in recent decades.

Since the Seventy-third Congress renounced the unconstitutional money system that rendered "ineffective the power of government", the only course consistent to pursue is a complete return to the Constitution and its mandate to Congress to regulate the value of money.

Vital national affairs concerning control of commerce and trade, affecting all 48 States in all economic activities, must be dealt with constantly on a national basis through "coin-money" agents of all 48 States. There can be no safe turning back to any makeshift substitutes through any dominating influences that do not synchronize identically and interchangeably with the supreme power of Congress.

Human progress demands trading on a broad basis with (money) restrictions minimized. Services and products of human energies and genius must circulate freely, constantly to pass their benefits from man to man. Ancient methods of barter limit rigidly the scope of human activity. The gold-control basis of barter, inaugurated and established by the Bank of England, is only one step removed from prehistoric methods of exchange tied to any one thing, as in barter. Credit expansions and contractions based on control of any one thing—gold—have proven their destructive, annihilating effects periodically. Control of the barter—gold and credit mechanisms—have too frequently been manipulated fraudulently to confiscate the wealth and destroy the welfare of the bulk of humanity.

An adequate, honest system of barter and exchange under a uniform representative medium of value—money—is possible only through the eternal vigilance of Congress, agents of all the people, who alone can assure and protect the rights and liberties of all our citizens.

Man's ascent from barbarism demands an adequate, liberal governmentally controlled supply of money as a system of settlement for the consummation of human negotiations, deals, and trades in all their relations.

Dissolution of democracy never has been the design or purpose of any Congress. Yet there is today a Nation-wide negation of democracy by destruction of the equal rights of an overwhelming majority of citizens to life, liberty, and the pursuit of happiness. Neglect of Congress' constitutional power—abuse and effects of abuse of improper money measures for generations—are responsible.

Debt slavery and poverty have submerged preponderant numbers of citizens. Our debt-slavery era, built upon the displacement of chattel slavery, is far more malignant and cruel today than human slavery ever was in the South, in most instances. The tender care and consideration given to its human chattels, their health and welfare, necessarily selfish though it was, put to shame the ruthless cruelty practised toward tens of millions of dispossessed citizens by the debt-owning class of wealthy monopolists who are the present slave-owning masters of men.

Chattel slavery, Mr. Chairman, was beneficent philanthropy compared to today's begrudging charity and deliberate denial of the right to work and live.

England's Americanized system of debt slavery was deliberately planned to replace the chattel slavery ended by Civil War.

What amounts to an undeniable and undenied bankers' conspiracy was saddled upon the whole American people as evidenced by the British Bankers' John Hazard confidential circular of 1862, and the American Bankers James Buell circular which sought to firmly establish monopoly national banking, by bribery as suggested by Mr. Buell.

Debt slavery and monopoly money-issuing privileges have gone hand in hand as proposed, immediately following and steadily, since the adoption of policies laid down in the Hazard and Buell circulars over 70 years ago.

Debt and economic slavery drive men mad or to destruction. They foreclose families out of their homes, rob the unemployed, set whole families adrift, destroy their welfare ruthlessly.

When bankers made "ineffective the power of government" by establishing their bondage, debt-slavery system in 1862, their monopoly money policies, controlled by the usury demands of private bankers, became, and still are, a complete negation of our independence and the principles for which our Government was established through the Revolution of 1776.

Money monopolists' mighty wealth drives civilization to destruction through its heretofore irresistible force of sovereignity and power over the purse.

Mr. Chairman, greed, man's greatest curse, and money monopolies, have so completely condemned the loins and limbs of labor to a slavery existence as serfs, encumbered with idleness, irredeemable debt, and refusal to provide an adequate circulation of money, there is no escape except by revolution unless Congress reverses wrong policies.

Reversing wrong money policies of two and one-half generations, now started, must be followed by complete restitution of the rights won by the American Colonist from their British money masters. Constitutional control of the purse, regulation of the value of money, with their rightful implications, mean an entirely new rededication of our lives, liberties, and energies to the inalienable principles of equal rights, equal justice, equal opportunities, equal economic freedom.

Wrong money policies are criminally cruel.

Wrong economic (money) policies ruined Rome.

They vitiate, destroy the binding effect and control of government.

Mr. Chairman, they have destroyed many civilizations.

Wrong money policies were eternally wrong for every American caught in their meshes and economically disfranchised or fleeced for life.

Wrong money theories and practices have proven to be as cruelly criminal as autocratic, oligarchic governments that despoil, enslave, or deny the common rights of man. They have created over 250 billions of existing debt slavery in the United States and are less defensible than human slavery ever was.

Economic slavery is more intolerable than political slavery.

Untold millions of men are held in debt slavery today. They no longer get sent to prison as in another era. But they live virtually as prisoners in corporation-owned shacks and cannot hope to pay their back rents. They are held bound to their masters in bondage.

Wealth, fraudulent wealth, always has violated and exploited economic and financial laws, moral and civil, brutally with the brute force of brutes.

Exploitations of the many by the few has been the one fixed policy always used against the American people all the time, in depression periods as well as boom periods.

Exploitation more flagrant and violent than ever, has grown intolerable.

The same disruption that destroyed Rome is now happening here. Wealth was absorbed, seized, hoarded by economic autocrats.

National wealth has been siphoned into the hands of the few. Unbearable debt burdens and poverty have been saddled on the backs of the many.

The poor in Rome as here were dispossessed and pauperized.

Says H. G. Wells' Outline of History, regarding Rome: "The growing mass of the expropriated (the masses of humanity) was permeated by that vague, baffled, and hopeless sense of being bested, which is the preparatory condition for all great revolutionary movements." Rome's decline initiated a thousand years of stagnation.

"The failure of the Romans to manage the money mechanism * * * was due, in part, to the absence of paper, printing, and a convenient numerical system. * * * For a thousand years the policy of European states was vitiated by the crudest and silliest fallacies concerning the nature of money. * * * Money, like dynamite and other tools used by men, can very greatly damage, as well as very greatly serve his society", recites Norman Angell's Story of Money (pp. 107 and 151).

"Accumulated wealth was hoarded; decay ensued."—Prof. W. Cunningham.

The inevitable, drastic change in our money system, now in transition, demands an entirely new viewpoint on all legislation. Demands a recasting of our whole banking and economic set-up.

A new deal civilization must discard all the old, outworn, misdirected, and untenable theories of money.

Our few money lords must yield to the vital necessities of 126,000,000 citizens.

Men will not indefinitely suffer privation while living amid a superabundance of all they can desire to provide a full life of plenty.

To check lengthening cracks in our civilization we must have production for use on a mutually advantageous or profitable basis. Monopolized production must not supply constantly increasing tribute to redeem falsely built-up vested capital.

Purchasing power, velocity of turnover of money actually used in trade, alone promotes the public welfare.

Insufficient circulation of money compels depression and distress.

Ample circulation of money and of trade is the all-important necessity to promote the general welfare.

Only 5½ billions of pocket money are now extant in dollars, mostly hoarded in bank vaults. For every self-liquidating dollar now owned and outstanding there are nearly 50 inflationary, debt-shackling dollars in circulation. There must be several times as many self-liquidating, cash-in-the-pocket dollars as now pass in trade and actually circulate to promote the general welfare.

Taking the falsely bottomed, falsely built, falsely boomed, and repeatedly wrongly buttressed financial-industrial monopolized combines now in control, and supporting them on a status quo basis to rehabilitate or reconstruct society is a denial of all the inherent rights of mankind. There must be no continued acceptance of tribute-exacting financial tyrannies that consume, through their excessive hydra-headed interest and profits system, the substance of humanity, saddled with scores of billions of frozen debts.

There must be a reversal of the mistakenly promoted economic financial manipulations of the past 73 years, since the issuance of legal-tender dollars ceased and were succeeded by the now repudiated gold standard system of closely controlled, piratically exploited, money-token securities and measures monopolized by a few master dictators of men, their associates, and beneficiaries.

Money should have no interest or bondage value, but to be disbursed only in payment for wealth values as created or transferred.

Money should be loaned to governmental subdivisions at cost, approximating one-thirtieth of 1 percent, with a service, collection, or redemption charge added in lieu of interest, penalty, or tribute charges.

Money should be loaned to quasi-public corporations at 1 percent or less for wealth-creating, productive purposes to help reduce the cost of a high standard of living, to help reduce the cost "of liberty and the pursuit of happiness."

Money should be loaned to all real-estate owners at 1 percent or less.

Payment of the soldier certificates (bonus) should be made at once.

Proper banking legislation contemplates a redeemable, noninflationary currency, issued to all the public on their negotiable assets. Money is to be issued and loaned in the same manner the Government now issues and lends money to the Federal Reserve banks, at cost, said cost being from 30 cents to 40 cents for a thousand dollars.

Private, monopolized control and ownership of tools, of money-token and other tools, has become a basis of enslavement.

Autocracy in industry cannot exist alongside democracy in government.

The existence of luxury in the presence of poverty and destitution is contrary to good morals and sound public policy.

The present depression is one that prevents the existence of abundance to enforce the poverty of scarcity.

A small group of men have vast, overwhelming wealth while the rest of mankind have vast, overwhelming debts, subjugating and unbearable.

Proper banking legislation must mitigate, minimize existing debts.

It is contrary to common sense that men should be pauperized because they produce too much of their necessities and even of their luxuries.

Small bands of our forbears took over a vast continent on the basis that unshackled, free men were endowed with equal rights. They built great industries with continental networks of transportation and an unrivaled capacity to produce beyond the bounds of the supremest wants of many scores of millions of their fellows. Free citizens now deny that any group of men have the slightest justification to proscribe the inalienable rights of 126,000,000 people and their posterity.

Obsolete, impossible-to-bear money controls cannot be revived synthetically. A decadent system cannot survive.

With radio's freedom of speech outstripping the petty financial-enslaving propaganda of special interests, their press and their lilliputian one-track mentalities, our national strength united will inevitably be asserted to block or surmount any further financial shackling of producers to restrict purchasing power, consumption, and an abundant life. A new deal that actually gets somewhere by abolishing economic slavery or insecurity cannot be denied.

A national monetary system owned and operated by 48 States is inevitable.

America's wealth was bequeathed to all its citizens. Not merely to a small group of money-manipulating monopolists, controlling, unconstitutionally, the power "to coin money, regulate the value thereof."

Unbearable high-interest debts have nearly all been accumulated since the days of McKinley and Teddy Roosevelt. They account for the pauperization of a preponderant percentage of distressed citizens with "80 percent of our population on the border line of poverty", says Senator Borah.

Mark Hanna's gold-bug victory started our present topheavy debt-money inflation. In 1897 the total debt structure of our then existing 82 industrial combinations is reported at only $1,000,000,000. In the next 4 years a dozen more combines added 250 percent additional debt inflation, including Morgan's United States Steel.

In the 7 years ending 1929 new "securities", corporate and foreign bonds, were floated to the extent of nearly $50,000,000,000, according to the Commerce Yearbook 1929. These 7 years produced nearly 50 times as much corporate debt-money inflation as the total outstanding corporate debt structure in 1897.

Wall Street's financing of the Great War by manipulation and inflation through the privately owned and operated Federal Reserve added scores of thousands of millions (scores of billions) to our debt-money burden.

While foreign nations have mostly repudiated their debts of all kinds our nationals continue to hobble along with impossible-to-pay debts and our burden continues to increase through mistaken policies.

Private monopoly ownership of money-issuing privileges, of debt-imposing tools and instrumentalities of industry, trade, and commerce are the basis of enslavement of the people of the United States.

Monopoly and luxury flourishing in the face of poverty and destitution of an overwhelming majority belie our independence and Constitution and disrupt the general welfare.

Natural drought and famine can be tolerated. Man-made depressions, scarcity and poverty because of money stringency are intolerable.

To establish an equitable, well-balanced growth and development of the whole of the United States, all State, municipal, and local taxes should be progressively taken under control of the National Government. Money needed to carry on State, municipal, and local activities should be apportioned out of the income of the United States so as to give every part of the country prosperity under State supervision.

Mr. Chairman, most of our countrymen are in shackles and chains. Economically they are enslaved. Enslavement is eternally wrong and cannot last.

Chains and shackles that bind the limbs of productive labor—farmers, clerical workers, wage earners—must be broken.

Economic slaves must be freed.

Liberty dwells only where men are free. What crimes have been committed in the name of liberty!

"The general welfare, inalienable (equal) rights, justice, domestic tranquility, the pursuit of happiness," are all denied to the tens of millions of economically disfranchised, dispossessed, economic slaves throughout our 48 States today.

Idle men become economically disfranchised citizens and serfs. Boys without marbles or sports lose their mutuality, their cooperating activities, and languish just as men without money income must also languish.

Congress must provide money circulation. There is no equal alternative.

Congress is now obligated to adopt an honest money system by beginning to assume its sacred constitutional power "to coin money, regulate the value thereof", so as to put everybody on a work basis or a security basis.

A few billion dollars of actual gold or other cash cannot by any possibility be stretched to pay 250 billions of existing debts. In his inaugural address President Roosevelt promised to drive from the temples the "money changers" who have piled up our enormous, unbearable debts through their private control of money-issuing privileges.

Railroads, cities, corporations, and farmers have been favored with legislation by Congress to repudiate impossible-to-pay debts. Hundreds of thousands of farm and home owners have lost their homes through foreclosure of impossible-to-pay debts. Nearly a million other home owners have been saved from foreclosures by recent legislation. Fifty million povertyized citizens must have the help and humanity offered by the Lundeen bill.

Many millions of families, workers, and producers of wealth have been impoverished through no fault of their own

For 73 years Congress has allowed private brokers and bankers to control the circulation and issuance of money, an abrogated constitutional power.

For 73 years, since legal-tender dollars were demonetized and discontinued, Congress has allowed the British-Rothschild gold monopolists to gold-brick the American people in alliance with Wall Street's money masters and money conspiracies. They have gouged the Government with high interest charges for letting the Government use its own money. They have printed or ordered money printed by the Government's own printing presses. They have paid from 29 cents to 40 cents for each $1,000 of this printed money we now use as dollar bills for pocket use. They have had the exclusive right to deal in this money. They buy it cheap as the cost of paper, ink, and printing costs. They sell it dear (exchange it) for Government bonds, paying the bankers interest in the hundreds of millions of dollars annually.

For generations the Wall Street-British-Rothschild allied gold monopoly bankers have collected billions of dollars tribute from all our citizens for the bankers' unconstitutional, exclusive power to issue or deal in money. They still continue to get all the Government printed money they want, printed at their direction, at cost of printing, for their exclusive use, for them to lend back to the Government or to hire out to the public and corporations at their price and profit.

For the past 73 years all money deals and all debts have been based on a minimum supply of monopoly-controlled gold and a multiplying supply of debts. Due to the control of gold by a few money jugglers the American people have been put through the wringer and drained of their wealth periodically in nearly a dozen deliberately managed panics, depressions, and Wall Street stock market squeezes, gold corners, etc.

"Gold", said the famous Senator John J. Ingalls, "is the money of monarchs, and was in open alliance with our enemies in the Civil War."

To resume a march of orderly progress America must quickly emerge from the economic fog of past generations so as to escape the enthralling disorders of a medieval age of financial imbecilities. Imbecilities grown up and copied from those who first inaugurated, governmentally, a private bank of issue when James I was dethroned in the seventeenth century by the organizers of a banking system of human subjugation, 1694. This system developed our present age of debt slavery and exploitation under the domination of international gold-money monopolists who saddled upon America the money-governing, economic-control policies of English bankers.

Nothing less than a complete reshaping of banking and finance measures, which govern all welfare and economic measures, under a proper conception of equitable wealth of money, its functions, purposes, and reasonable relations to "the general welfare" of all the people living in a democracy, can secure "inalienable (equal) rights" and "the blessings of liberty."

Many coercive palliatives that attempt to correct and minimize the multitudinous wrongs of the past by frivolously setting aside nature's economic and deeply rooted, solidly established laws and principles of proven worth, antimonopoly and other vital law structures, have little or no constructive values. They merely undertake to regulate existing wrongs instead of removing their causes. Yet, almost unavoidably our Government has been impelled to enter into a plethora of experiments to counteract the resultant evils that have so completely disrupted our society of 126,000,000 Americans under bankers' control of Congress' constitutional power over money for generations.

Our troubles are fundamental. They are identical with and an outgrowth of the heresies and fallacies inherent in a corruptive system of banking saddled upon the United States in February 1862–63, 25 years after Andrew Jackson had eliminated banker "vipers" from national control of Congress' constitutional power over money.

All banking atrocities comprehended herein deal with the immediate present in which the Seventy-fourth Congress aims to reverse and replace the payable-in-gold banking rackets of the past seventy-odd years.

Our United States currency is a strange jumble of various kinds of money, relics of political contingencies and necessities, but tied together and interchangeable by reason of the law that gives them all equal lawful money value.

In a report of New York City bankers, in February, to the New York Chamber of Commerce, containing replies to questions by Senator Fletcher, chairman of the Committee on Banking and Currency, these two admissions are found:

"We have at the present time neither a currency system nor a banking system. By reason of the emergency legislation passed since March 1933, our former currency system has been discarded and in its place there has been substituted a currency dictatorship, which, no matter how well suited to meet the requirements of an emergency, cannot in any sense be described as a system adequate to meet the needs of moderate economic life.

"In the same way, it is necessary to point out that our present banking system is not a system but a hybrid hotchpotch of relics of various old systems upon which has been superimposed an emergency structure."

Upon such foundations have the monopoly bankers, internationally tied together, built their tinsel temples of synthetic money, their pyramided profits from debt-enslaving structures, and their gargantuan towers of bizarre holding-company and other monopoly controls.

Debt, interest-bearing obligations of all money-token instruments outstanding throughout the United States, I again state, exceed $250,000,000,000. To save our civilization, to begin to give the people of these United States the independence, liberty, equal rights, and pursuit of happiness which our forbears fought to gain and were denied, our Government must reverse its monetary policies as pursued for generations and as devoted continuously to creating debt-bearing, interest-absorbing, unearned-increment, wealth-confiscating measures controlled by private usurpers of the constitutional, exclusive Congress power "to coin money, regulate the value thereof"

Unless our debt-shackling policies of the past are entirely reversed and new policies pursued to finance all anxious workers to create wealth to be diffused among the workers and all citizens, then other nations, especially Japan, will supply the raw and finished products of commerce that we deliberately forego by destroying produced wealth in food and material crops. We not only create scarcity, poverty, high prices, and impossible debts among our own people through a private monopoly control of money; we also deliberately remove our surplus products from the world markets to favor competing nations and minimize the usefulness of our merchant marine.

Naval equality, destroyed 12 years ago, is now being restored. Merchant-marine equality must also be built up. But if we progressively impoverish and pauperize our own citizens and also destroy international trade, we are hopelessly lost.

Our civilization tends to fall apart, due to generations of misconceived monetary policies.

Denying inherent, fundamental independence and constitutional rights, pursuing any policy to further encumber with debt and with inescapable poverty most of our citizens by refusing to increase and exchange our national wealth, inevitably continue to pyramid disaster and chaos. To break the Gordian knot debt-free money must circulate freely. A plentiful supply of money must employ men who must have work. They must have tools and materials with regular, decent, or substantial income. To increase more interest-bearing bonded indebtedness means more misery and more ultimate poverty. Debt-hobbled money restricts work and prevents prosperity.

Legal tender constitutional dollars are the one form of all our various kinds of money that most completely comply with the purposes and intent of the Constitution. Legal tender greenback dollars are the one kind of money that is our most democratic and least barbarous form of money, and which has been most tenacious of life in spite of many fierce and demagogic assaults. These constitutional dollars first appeared as Civil War greenbacks, known as "Abraham Lincoln money." This money has not been encumbered by bonded debts or tributes to bankers who have dictated control of all our other money issues, money tokens, bonds, etc. It has survived all artificial changes and modifications of monetary laws.

The constitutional dollars issued for early Civil War needs to save our Union alone symbolize the independence, liberty, economic freedom, equal rights. They are free-born non-tribute-paying legal-tender dollars. Not being conceived in iniquity, they are free from debt charges of annual interest-bearing bonds. These unfettered symbols of liberty have been the constant dread of money changers and have aroused a fury of lustful antagonism among monopoly bankers who consider them mongrel money. Although unorthodox, they are more respectable than any other dollars among the brats of blue-blooded parentage, whether gilded in gold or silver, or based on bond-bedecked trappings.

Non-debt, non-gold dollars meant freedom from monopoly controls. They meant freedom from foreign entangling alliances and the autocratic domination of domestic financial despots. They meant strength and power diffused among the many, free from tryanny or domination of the few. They meant a wide-spread growth of true democracy under a truly democratic money system.

Non-debt legal-tender greenback dollars of the Constitution were set aside by the monopoly bankers. They were entirely, utterly opposed by the cupidity and rulership of the well-born, of those demanding special privileges for the few. They meant the negation and doom of domination by triumphant, irresponsible autocrats and economic oligarchs.

Non-debt dollars were dangerous to the money shavers and money changers; to those who idly live on the toil of others; to those who exact tribute, and who shackle and fetter humanity with bondage balls and chains; to those who neither sew nor spin, who never faced fire, never risked their necks, never yielded their lazy luxuries, never gave up their soft and sheltered security of life and limb, or the usurped security of their claimed sacred, bond-bloated wealth—cunning, scheming, crafty racketeers.

Men born free should not be chained to bondholders. Bondage bonds should not be forced by government. Free men and their free institutions should not yield to autocrats of any kind, foreign or domestic. Freedom cannot flourish when bound to bondage. Free-born men cannot attain freedom when chained to any form of consecrated economic wealth or autocracy, or to any system based on the divine right of kings or their kind.

Men cannot live in liberty outside the pale of poverty when burdened with the bonds of money masters. Pursuit of life, liberty, and happiness becomes impossible under the whiplash of economic tyrants. Instead, failure, despair, death fiddle their alternate tunes.

Debt-free legal-tender money is dangerous to socialism. To socialism such as President Roosevelt fears may develop to counteract the socialism he spoke of in March as already developed by private, preferred business monopolists preempting exclusive privileges. Debt-free dollars are as dangerous to Fascism and Communism as they are to monopoly, to autocracy, and socialism.

The supreme menace of legal-tender, nondebt dollars is implied in the modest measure of social justice they can render to more than 10 million economically disfranchised unemployed and their 30-odd million dependents, to 4 million World War heroes with over 10 million dependents, and to 2 million superannuated old folks needing pensions.

Too much democracy may be wrapped up with and would spread through use of debt-free dollars. They would result in independence, equal rights, the establishment of justice, an equal voice in government, equal privileges, and abolition of most restrictive economic influences that cause crimes.

The rights of man are paramount. All men are superior to a small controlling class of tax-exempt bondholders or tax-dodging banketeers and financiers. Tax-free dollars will necessarily spread wealth to "promote the general welfare" by tapping our unlimited reservoirs of national riches belonging to all our citizens, high and low, haughty and humble, wealthy and few, smart and dumb. There will then be money enough for all who can honestly earn it, meted out with even-handed justice when Congress coins legal-tender dollars to comply with the Constitution, and regulates the value thereof.

Since our Constitution was adopted the most important legislation in five generations abrogated the use of gold as money. The Supreme Court affirmed this vital overthrow of a wrongly built-up money system. The pending institution of a valid constitutional money system affects the fundamental concept of our society as a free people entitled to self-government rather than a subject people controlled by a few money masters. It contains the most vital principle ever involved in any legislation—control of the power over money, social justice, and economic liberty.

Discarding the use of gold as having a fixed, intrinsic property value, and its barbarous power as an enslaving, subjugating measure of wealth accelerating the decline and threatening as it did the extinguishment of our 300 years of American civilization, now makes possible the rehabilitation and restoration of the independence and general welfare of 50 to 100 million of our citizens.

The reaffirmed money power of Congress is a mandate for a new (money) Bill of Rights to promptly institute a safe and sane currency system to replace the untenable system that has chained and shackled humanity by piling up hundreds of billions of debt-bearing burdens surreptitiously according to authenticated, acknowledged records.

The legal tender constitutional dollars of Civil War days, the nondebt dollars, became sidetracked. They were followed by "payable in gold" bonds (interest and principal), the gold being controlled and monopolized by International-Wall Street bankers. As a result our total debts have reached a collapsible condition. They have become an insuperable and almost insurmountable burden upon our civilization in competition with Japan and other nations, especially those that repudiated their internal and external debts.

Blundering on and off the vicious, illusive, enslaving, tyrannous gold system of money control, as England has done, is unworthy of a great democracy that assumed 160 years ago to cast asunder from the British system of financial gold control and domination— a domination that has clutched America's throat and dictated our destiny most of the time since 1776. England's monarchical, imperialistic problems and policies are no criterion or model for the United States, especially the falsely built-up gold-controlled, consols debts dictated by the bosses of the privately owned Bank of England, based on economic imperialism.

"Reconstruction and control of finances in both countries is most essential", said Lloyd George recently. Here they transcend any attempt of emergency experiments to further tax and hobble employment with makeshift insurance measures, and through new swarms of bureaucratic leaches, before there is a solid approach of national stability in employment.

"America is prodigiously wealthy. Its riches are to (should) be utilized to ensure a higher standard of life and greater security for its workers", says Lloyd George. But only by assuring work for all idle willing workers through operation of a constitutional money system legally directed by Congress, not by crippling production or export power or purchasing power under direction of hordes of bureaucrats to further muddle our present almost insoluble distress. But by nation-wide employment and generous circulation of debt-free money in reach of all workers.

The Treasury Department, in March 1935, ended the 72-year-old racket of money-issuing privileges by national banks, coining their own imprinted currency upon hundreds of millions of legal-tender greenbacks, printing-press paper money. The absurdity of this racket was indefensible.

A sovereign government's supreme constitutional power to issue money, to make its legislation effective by directing control of its national wealth and economic destiny was surrendered during the Civil War period, to the guidance and control of international bankers through their development of privately monopolized and usurped privileges to issue money, to inflate money, to deflate money, or the equivalent money tokens and money substitutes.

America's ablest authorities have all sensed the dangers to our Republic by a denial or repudiation of democracy in monetary matters. Abe Lincoln foresaw "a crisis * * * the money power * * * prolong its reign * * * until the wealth is aggregated in a few hands, and the Republic is destroyed." Lawyer Salmon P. Chase, made Treasury Secretary and influenced through his New York banker friends, confessed "the national banking act was the mistake of my life * * * has built up a monopoly * * * should be repealed * * * the people will be arrayed on one side and the banks on the other in a contest such as we have never seen in this country."

Thomas Jefferson condemned "government subserviency to private interests" and warned, 75 years ahead of Lincoln's warning, similarly, "allow private banks to control the issue of their currency first by inflation and then by deflation, the banks and corporations that will grow up around them will deprive the people of all property until their children will wake up homeless on the continent their father conquered." Henry Clay opposed any concentrated power over the "purse and the sword." He opposed the "anti-American, * * * British institution" of banking. Webster decried "allowing a banking corporation to issue a substitute for money as one of the greatest political evils, * * * a contrivance for cheating * * * mankind." Senator Randolph of Virginia, said, "Charter a bank * * * learn its power, * * * find, if you can, means to bell the cat. It will * * * laugh at your laws."

"Of all aristocracies, none more completely enslave a people than that of money; no system was ever better devised * * * they (banks) form a precarious standard by which all the property of the country—homes, lands, debts, and credits—are valued, * * * prescribing every man who dares to expose their unlawful practices", declared a New York legislative committee in 1818.

Said William Pitt: "Let the American people go into their debt-funding schemes and hazardous banking systems, and from that hour their boasted independence will be a mere phantom." "National debts paying interest are simply the purchase by the rich of the power to tax the poor", said John Ruskin.

James Madison's framed message George Washington intended using to veto the British-patterned, debt-funding, private money-issuing bank charter which Alexander Hamilton unconstitutionally sought for participating Members of Congress and his New York banker friends, was set aside under influences of the privileged few. Hamilton, with Isaac Roosevelt and 10 others, had set up a similar, State-chartered "wild-cat" bank in New York City, 1784.

Andrew Jackson termed bankers "vipers" and "swore by the eternals" he would hang Nick Biddle "as high as Haman." Honest John Tyler vetoed a proposed reincarnation of the British-Rothschild banking scheme ninety-odd years ago.

The British-Rothschild allied gold monopoly bankers of Wall and State Streets brought to bear the influence in the rich man's Senate, as elected then by State legislatures, to completely emasculate the legal-tender values of the law so overwhelmingly passed by the House of Representatives February 6, 1862.

Senate amendments, forced upon the House in conference under urgency and pressure of war necessities, nullified the constitutional value of legal-tender money as not receivable "for interest on bonds and notes, which shall be paid in coin"; also authorized the Treasury Secretary to sell United States bonds "at the market value thereof, for coin or Treasury notes" (outstanding 7.3 percent notes convertible from existing 20-year 6-percent bonds); also provided that coin interest payments on the debt of the United States and coin for a sinking fund should be accumulated from "duties on imported goods and proceeds of the sale of public bonds." Exempting this legal-tender money as not payable for "duties on imports, and interest on the public debt" was a powerful weapon to the gold monopolists. Importers had to bid high for metal money.

The Rothschilds and their New York-British banker allies actually controlled nearly every dollar of gold in the United States. They kept it scarce and manipulated gold in the "gold room" adjoining the New York Stock Exchange to charge enormous premiums for compliance with the specie gold payments the gold monopolists had dictated.

Government bonds and notes were sacrificed as low as 50 cents on the dollar; legal-tender dollars as low as 35 cents, all to the extent of many hundreds of millions of dollars.

Gold monopolists collected tremendous tribute on every Government financial requirement for war purposes. The Army and Navy soldiers and sailors who suffered, bled, or died to win the war, and other creditors, all received depreciated money in disfranchised paper dollars while the "wild-cat banker gold inflationists" took their toll on nearly every dollar that circulated. They dictated ruthlessly to and traded on the necessities of a financially dominated Government. They piled up inconceivable blood-money fortunes in all finance and Wall Street manipulations. And laid impregnable foundations to establish and develop their claims to, and their conquest of, the national wealth and the economic control of these United States.

Customs import duties of $910,000,000 in 4 years of war were levied upon by the gold monopolists to yield stupendous tribute to enable the Government to collect the juggled gold needed to meet dictated payments continuously required by and to the same gold-juggling monopolists.

The first issue of limited legal-tender money authorized $150,000,000 in notes on the credit of the United States February 25, 1862. Acts of July 1862, March 1863, and June 1864 authorized added issues of $450,000,000. There are still outstanding $346,000,000 of these notes. Some of the original notes were made payable with interest at 5 percent. It is calculated the Civil War legal-tender greenbacks which became a noninterest, nondebt bearing circulation has saved the Government 12 thousand million dollars of accumulated charges (12 billions), figured on a 5-percent basis.

In the 2 years, 1865 and 1866, the Government put out new and refunded obligations of $1,800,000,000. Total interest payments, not compounded, on those 2 years of war financing have amounted to more than the existing outstanding public debt. Yet those 2 years of war financing and refunding are less than half of our current annual financing. With the use of constitutional legal-tender dollars there would be no existing public debt.

The gold-monopoly money powers dictated the act of Congress July 14, 1870, refunding the public debt so as to make its payment in metal money beyond question.

James G. Blaine's Twenty Years of Congress, page 606, quotes John J. Ingalls: "Gold is the money of monarchs, and was in open alliance with our enemies in the Civil War."

In President Grant's inaugural address, 1869, he alluded to "the sacredness of the public faith", and "let it be understood that no repudiator of one farthing of our public debt will be trusted in place."

Hon. William Mungen, of Ohio, made a powerful presentation of Civil War financing in the House of Representatives, 1869. He detailed how the Government was being bled on a double usury basis and echoed repudiation.

In 10 years' time the Rothschild-American allied gold monopolistis had made a profit above 1,500 million dollars upon the outlay of juggling of ony 500 millions of jointly manipulated bank bookkeeping credits and a minimum of gold. At 50 cents on the dollar in actual gold they bought 1,000 million of Government obligations with an initial profit of 500 million dollars. Compounded interest, 7 percent or more, on the full face value quickly exceeded 1,000 millions. From a single 500 millions of bank credits and gold combined over a score of thousands of millions (over 20 billions) of tribute have since been drained from the people of the United States, allowing 15 years for each doubling of the first 1,500 millions of profit.

Since a subservient Congress yielded to the gold-monopoly dictators 73 years ago there has been a succession of laws consistently and progressively favoring and granting special privileges to private banking interests, until at last the country is completely under control of a powerful money group, who levy annually an enormous tribute upon industry for the privilege of doing business. Operating unconstitutionally for 73 years under the aegis and auspices of Government agencies.

Those controlling money and finance have controlled our country. They are our present-day masters. The interests of the public have been persistently disregarded, until at last we find ourselves in our present almost inextricable economic predicament. As Lincoln and others had forecast, "wealth is aggregated in a few hands"; people are enslaved economically; inflation and deflation have despoiled society; foreclosed millions have lost their homes; independence is "a phantom" for most citizens.

Because our money masters so completely overplayed their game as to crash the economic stability or povertyize a large majority of all our citizens, many expressions are heard, "they have dug their own grave."

President Roosevelt had no choice but to abandon the gold-monopoly system of money.

The Supreme Court has sustained the debunking of the "intrinsic value" theory of gold, because gold is merely a commodity. So is any other money substance. The Court recognizes only legal-tender constitutional dollars issued under the supreme, sovereign power of Congress, irrestrictible and illimitable. Gold money (clauses—any rigid monetary measures) "cannot fetter the constitutional authority of the Congress." They vitiate Congress' power, "interfere with * * * the power granted to the Congress" (majority, pp. 15, 21). The Court upheld and confirmed the findings of the Seventy-third Congress, which declared "no currency system, whether based upon gold or upon any other foundation" (upon bondage debts or other irrational conceptions), cannot interfere with a Congress' policy or "render ineffective the power of the Government to create a currency and determine the value thereof" (referred to p. 18, majority opinion).

When the guns of the Southern Confederacy began firing on Fort Sumter and the cohorts of secession inflamed the South to arms, immediately gold and silver ceased to circulate. Like two cowards, they hid away in secret vaults or fled from the country, as was the case in all wars in recent centuries.

International bankers, as always, dictated the price of gold and lashed the necessitous government most unmercifully. Men there were in plenty, eager patriots in thousands, tens of thousands, hundreds of thousands, that answered Lincoln's calls to yield their happy homes, their fortunes, their lives to prevent dissolution of their Government. But money and capital, left by Government in control of private banker manipulators, waited, delayed, refused to serve except for dictated profits, profits, profits in the "holy name of gain." Delay helped the enemy organize, recruit, drill. Also business alliances were developed with British-Rothschild gold-monopoly agents and promoters of war, lust, greed, to harass shipping, and for other financing.

To replenish a depleted Treasury, to stimulate action, constitutional "greenback" dollars were issued without regard to gold-monopoly traditions and with no promise of gold or silver redemption. They were issued as full legal tender for the payment of all Government obligations and private debts within the jurisdiction of the United States.

America's Money Tragedy, by former Senator Henry C. Hansbrough, relates most dramatically the opening Civil War monetary crisis. With permission from B. G. Labore, publisher, we submit 2 pages of Mr. Hansbrough's story:

"In 1861 the United States became the mecca of the international banking group * * * with a view to be sure of the usual war-time harvest. In the realm of high finance, blood and boodle are synonymous, interchangeable on a * * * usury basis.

"John Hazard, of London, representing the Rothschilds, became active to involve America in the European banking system—for fabulous profits to foreign capitalists.

"In behalf of the big bankers of Europe, Mr. Hazard seductively framed a secret circular that shocked the American conscience, * * * for in the final analysis it spelled a voluntary contribution to the usurer who skins the borrower, and the sheriff who knocks him down on the auction block. Addressing the international bankers of this country in 1862, Mr. Hazard wrote:

"'Slavery is likely to be abolished by the war power, and chattel slavery destroyed. This I and my friends are in favor of, for slavery is but the owning of labor, and carries with it the care of the laborer; while the European plan, led on by England, is capital's control of labor by controlling wages. This can be done by controlling the money. * * * We are now waiting to get the Secretary of the Treasury [United States] to make this recommendation to Congress.'

"First Usurer (laying a sheet of blue boolscap in front of the Secretary and indicating with his thick finger). A memoranda contract, sir. You are to sign on the dotted line.

"Out of sad but understanding eyes the Secretary looks hopelessly at another of the conspirators.

"Second Usurer. Sign!

"Third Usurer. Sign! Why hesitate? The country is at war.

"Fourth Usurer. Sign! It is the the law, be sure of that.

"The Secretary signs, but with mental reservations. Rises, and with a sigh throws himself on a lounge, covering his face with his hands.

"The man was right; it was according to the law, but recently enacted—on July 17, 1861, to be exact—said at that time to be one of the blackest pages in the history of America. Other Secretaries perhaps, and at least three Presidents, because of the exigencies of war, have put their signature to corrupting measures: Lincoln to this gold-purchase bill, McKinley to the Philippine Enabling Act, under pressure by the sugar interests, and Wilson, if not his signature, found it necessary to give consent to not a few outrageous war contracts.

"The historian having the hardihood to question the actual cause of the Civil War would have been guilty of treasonable utterance toward society's golden god. Suffice it to say that slavery was only the capsule. Within the glutinous shell were the almighty dollar and the usurer's substitute for the money of the Constitution. Mr. Jefferson would have freed his own slaves rather than embroil his country in bloody strife, while Mr. Lincoln incurred the bitter opposition of the Northern politicians because, man of justice and equity that he was, he proposed to buy the slaves' liberty and assess the cost upon those who professed their love for the black man.

"So that in the midst of war predicated upon a background of greed, Secretary Chase, the conspirators having sneaked off, made his way to the White House. Said he to the President: 'I have agreed to borrow $250,000,000 gold and to issue coupon bonds, or registered bonds, or Treasury notes, as I "may deem advisable" (the insinuating letter of the law).

"The President. At your option, I understand?

"The Secretary. At my option; yes.

"The President. I have complete faith in your judgment.

"The Secretary. But they are a pack of scoundrels, and in all likelihood will again have their way with Congress."

"And so it came to pass. For on August 5, 1861, a supplementary act was put through the legislative hopper directing the administration to issue 6-percent 20-year bonds exchangeable for Treasury notes, bearing $7\frac{3}{10}$ percent interest. From this vantage point the money power was enabled to manipulate the public finances at will. All potent, also conscienceless, it moved corruptly from one stage to another throughout the war.

"It debased or overvalued money and securities as suited its purpose; it discredited the greenbacks, bought them up at less than half their face value, and exchanged them at par for gold bonds; it cornered more of the world's gold; it demonitized silver; it established the gold standard and national banks of issue." (Insurmountable mountains of debt are the result of private bankers' gold-monopoly and money-issuing controls of money. For nearly 25 years after Andrew Jackson abolished private-bank frauds, the United States was not only free of debt but distributed surplus money among some States. Private debts were negligible.)

"It was in the Senate that the legal tender act received its quietus; not alone the act itself but the constitutional money of the people as well, for it was here that the public debt was made payable not in the dollar of the Constitution but in coin, the first godchild of plutocracy." This contention is sustained by the Supreme Court's recent decision.

The Lower House of Congress, February 6, 1862, passed the law which created for the first time a scientific money, by a vote of 93 to 59. Eight days later the legal tender act passed the Senate, greatly altered by amendments, that completely changed the course of America's economic history to result in our present jam by diverting the power of the purse into the control of the gold-monopoly bankers of Europe. Thaddeus Stevens, the grand "Old Commoner", is described by Congressman Judge Kelly as returning to the House with hat in hand and cane on arm after the final conference, shedding bitter tears over the result: "Yes", said he, "we had to yield; the Senate was stubborn. We did not yield until we found that the country must be lost or the banks gratified, and we have sought to save the country in spite of the cupidity of its wealthier citizens."

To comply with its constitutional obligations, to accede to its conventional, bounden duty by accepting the Supreme Court's mandate of February 18, 1935, the Seventy-fourth Congress undoubtedly will initiate far-reaching measures of financial reform consistent with, and mandatory to, a truly democratic form of government. To halt encroaching communistic conceptions of government is one of many important reasons. Also to comprehend President Roosevelt's attitude that "destruction of private socialism is utterly essential to avoid governmental socialism", expressed March 12.

Should it dare to act, Congress undoubtedly has the genius to devise a simple, noncommodity, non-interest-bearing, value-determining legal-tender medium of exchange that will enable the public everywhere to exchange goods for goods, raw materials for finished products, mental services for physical toil, and all the vast products of human invention and energy for other products of human endeavor and accomplishment in endless profusion—all by means of such legalized medium of exchange issued in an adjusted volume so as to bring about a balanced condition of approximately unchanged average prices.

Such a consummation would allow progress and civilization to complete their conquests over the materials and forces of nature. Then freedom, liberty, peace, and prosperity could reign untrammeled among men.

Legal-tender money should not enslave humanity by entailing endless debt-bearing bonds issued to and for other than Government agencies and redeemable progressively by taxes. And issued solely for services that "promote the general welfare", produce wealth, and discharge debts.

Legal-tender money should be based on the energies, brains, labor, wealth, resources, and constructive power of 126,000,000 citizens. It must be representative of value with no commodity value within itself and with no pretensions of being anything but sovereign fiat money. And it must be limited in issue to the careful engineering-ascertained needs of commerce and industry, but issued in sufficient amounts to meet all national requirements on a conservative, safe, and sound valuation basis so as to secure the approving loyal support of all citizens in every class and walk of life.

Hotchpotch blending palliatives would then be promptly displaced by modern monetary reforms that must inevitably promote peace and prosperity under intelligent, mutual understandings of helpfulness to enable humanity to discard the dreams of visionary high-brow well-wishers of mankind so as to actually achieve the brotherhood of man by establishing the rights of man under the supreme rule of reason. The gaining of these rights will automatically abolish crimes and treasons against the social justice of economic liberty.

Justice long delayed has been justice long denied.

Mankind must now emerge from the thralldom of generations of monetary inhumanity, slavery, and injustice.

127297—35——52

BANKING ACT OF 1935

TUESDAY, APRIL 2, 1935

IN THE HOUSE OF REPRESENTATIVES,
COMMITTEE ON BANKING AND CURRENCY,
Washington, D. C.

The committee met at 10:30 a. m., Hon. Henry B. Steagall (chairman) presiding.

The CHAIRMAN. Gentlemen, we have Mr. Franklin W. Fort, former Congressman from New Jersey. I am sure that the members of the committee know him. He has come to discuss this bill. We are glad to have you do so, Mr. Fort, and you may proceed in your own way, without interruption, until such time as you desire to be interrogated.

STATEMENT OF FRANKLIN W. FORT, FORMER REPRESENTATIVE IN CONGRESS FROM NEW JERSEY, AND FORMER CHAIRMAN OF THE FEDERAL HOME LOAN BANK BOARD

Mr. FORT. Gentlemen, I have tried to analyze this bill from the standpoint of a practical banker, which is one of my occupations. As a banker, I have had some practical experience which may be of some value to you. The bank of which I am president, for instance, advertised, in 1932, our willingness to lend money; and if necessary, to borrow it for the purpose of relending, and did borrow to relend, right through the depression, and showed the borrowings in our statement without detriment to our standing with our depositors.

Then in December 1934, we reduced the rate of interest on all types of loans, mortgages, collateral loans, and discounts so that no loan pays over 5 percent, where the borrower has recognized his honorable obligation during the depression even though unable to make substantial payments. I mention these things because I shall refer to the results of both of these policies later.

Mr. REILLY. What is the name of your bank?

Mr. FORT. The Lincoln National Bank at Newark, N. J.

There are 2 or 3 phases of this bill, gentlemen, on which I do want to comment—2 or 3 major phases, and some minor ones.

In the first place, my service on the Federal Home Loan Bank Board, of which I had the privilege of being chairman at its inception, substantially modified my views as to what constituted sound mortgage lending.

I have always believed, and still do believe that mortgages are probably the safest form of long-term investment of money. I have grave doubts, however, as to the wisdom of a straight mortgage under any circumstances by any type of lender. Indeed, since the depression, I am convinced that nothing but amortization mortgages should be made by any lender, unless it is distinctly upon the understanding that the mortgage is to be paid off in full at an early maturity, if it is a straight mortgage.

Then I do not believe that liberal mortgage loans are in the interest of either the borrower or the lender. There are few communities in the United States today where the tax rate is as low as $3 on the hundred.

Let us take the provision of this bill, and for the moment overlook the 75 percent provision that you may loan 60 percent of the value of the property. A tax rate as low as $3 on the hundred constitutes a fixed charge for the owner to meet of 5 percent on the mortgage. Nowhere can he get a mortgage at less than 5 percent interest; and in many of the communities where the interest is rate is 12 percent.

Consequently, the minimum fixed charge between taxes and interest on 60 percent of the value of the mortgage is 10 percent on the mortgage—5 percent on the mortgage for taxes and 5 percent for interest; and in many of the communities where the interest is higher and taxes are higher, it can run up practically to 20 percent of the mortgage without difficulty.

There is no property in the United States which can stand that fixed charge, unless it is a speculative proposition which is chiefly unimproved real estate, and you are not dealing with that type of loan here.

Now, in the second place, the depression has shown, as I have said before, absolutely, that there must be amortization of mortgages.

Your bill contemplates, in its 75-percent provisions, a maximum of 20 years for the amortization, which is 5 percent of the mortgage as an annual amortization charge.

If you add that 5-percent amortization to the 5-percent tax minimum and 5-percent interest minimum—if you are going to lend 60 percent of the value of the property, you are putting 15 percent of that mortgage, or 9 percent of the property value, as an annual charge against the borrower before maintenance and upkeep charges, and there are mighty few properties in the United States which can stand that charge these days. I do not believe it is in the interest of borrowers to encourage that type of lending.

We have recently had a survey in New Jersey by the building and loan associations of the whole problem of mortgage lending, in which they have recommended, in spite of their old policies, a limitation on the amount of loans for building and loan associations to a maximum of 60 percent, even on their method of amortization, which allows a share in the profits back to the borrower.

Mr. FORD. What is that method like; how long does it run?

Mr. FORT. About 12 years, with a share of the profits back, in our State, rather than the direct-reduction mortgage method, although they have recommended changing to the direct-reduction method rather than profit-sharing.

They have further recommended another requirement: That the owner must have a substantial equity. In other words, they have looked ahead to the point of opposing first-mortgage loans where the owner has a substantial second mortgage, because the depression has taught them convincingly that it is not in the interest of either the borrower or lender to make too liberal mortgage loans and to cut into the equity of the borrower too greatly.

Now, let us take the situation, if you start even with the 60-percent-loan provision, a man can budget the 60-percent loan for its first year or two; that is to say, he can figure that, at the end of a year, if he holds his job and holds his health, he is going to be able to meet the requirements of that mortgage for a year, or possibly he can see 2 years ahead, but that is the limit that he can possibly foresee.

Now, let us suppose that he loses his job, or is ill, or for any other reason gets behind the first year. As I pointed out, the minimum fixed charge for taxes and interest is 10 percent of the mortgage. You have increased the mortgage in a little over 1 year of bad luck from a 60-percent mortgage to a 70-percent mortgage; and at 70 percent a conservative lender must foreclose, because the auction-sale value of real estate is very rarely over 70 percent of its normal value.

Consequently, if you start at 60 percent, you are definitely letting your borrower put his neck in the noose.

I think you should start at 50 percent, as the present law is. We all know that banks have had trouble enough in this depression with frozen loans on real estate. I think you should start at the 50-percent rate, but I would favor a provision that permitted the banks to recast their loans upward as far as 60 percent, to save foreclosure.

That is to say, a man that starts at 50 percent may lose his job, he may get in bad health, and the lender must foreclose, if he is behind 1 year. I would like to see a provision that a bank might, at the end of a year, turn in and lend him more money, or increase that mortgage up to 60 percent, and then carry him, give him a chance to come back, not foreclose on him, and not force additional costs on him. But you cannot do this on top of a loan which starts on the 60-percent basis, because that makes your loan too high.

In other words, your lending limit ought never to be at a point beyond which you cannot go in order to save foreclosure; but, if you start at 60 percent, you are rendering foreclosure compulsory in many cases.

I want to emphasize again that what I am urging is in the distinct interest of the borrower, because the lender will still be paid if he forecloses when the loan reaches the 70-percent stage; and the lender must foreclose when it reaches the 70-percent stage, if he has any conception of trusteeship to the depositors in his institution.

Now, so far as the lender's end of this thing is concerned, as I said a moment ago, we have seen plenty of banks close in this depression through 50-percent mortgage loans; that is, supposed 50-percent loans.

May I say in that connection that, of course, the valuation of real estate is the least accurate of the sciences, if it can be termed "a science." You can take any committee in any bank and send them out to appraise a parcel of property, and there is never a chance that three men will agree on that value. They may compromise to reach an agreement, but no one of the three, acting alone, will put the identical value on it the other two did.

Consequently, you should have in here, from the lender's angle, protection against appraisal error, which is involved in a certain percentage of the loans. That is the chief consideration, I think, from the standpoint of the lender. And this means you should retain the 50-percent basis of the present law.

Now, about the length of mortgages—3 years is either too long or too short. A man can see ahead a year, sometimes 2 years, with reasonable accuracy; but a loan made in 1929, maturing in 1932, was a 3-year loan. It could have been refinanced in 1930 or possibly in 1931. You could, if you had made it in 1929, have gotten new money in 1930 or 1931, some way or other, possibly at a high premium, but you could have refinanced it. Three years is a term that you can not reasonable foresee. My own feeling is that a mortgage should be made of only two types. A straight mortgage should not run over 2 years without renewal requirement, because that far ahead a man can reasonably foresee and have a reasonable chance to refinance it if it is called for payment. If it is for a time longer than that, it ought to be on an amortization basis, and a high amortization basis.

I said to the Pennsylvania State Bankers Association 2 years ago that, in my judgment, no commercial bank ought to make a straight loan, unless to a business enterprise, with the understanding that that mortgage was to be paid at maturity, without renewal, and only when the money was needed for new capital. But generally mortgages, if they are to be held at all by commercial banks, should be on an amortization basis for two reasons: First, for the borrower, because, if he is on an amortization basis, his fixed charges are brought down annually, and his ability to recast the loan, in case of necessity, is simplified.

Second, from the standpoint of the lender, because neighborhoods change in cities with almost lightning rapidity. A loan that is good as a 60-percent loan today may be bad as a 50-percent loan in 2 years. In the country, for instance, out in Kansas lately, with dust storms or something of that sort, what was an excellent loan a year or two ago may not be worth anything today. The lender must have the security of justifying his original appraisal that is brought about by a definite and substantial reduction of the loan.

I have a theory, personally, that mortgage loans should be amortized contrary to the usual practice. The usual practice is to amortize mortgage loans at a fixed annual rate, the same rate every year from the inception of the loan. I think that mortgage loans should be more heavily amortized in the earlier years and then allowed to tail off in amortization to a moderate annual charge.

Certainly, if they are to be as heavy as 60-percent loans, in the first instance, they should be brought down to a maximum of 50 percent within the first 2 years, which the borrower can reasonably foresee. Thereafter the amortization might be slower, after the loan has been rendered secure for the lender and rendered recastable for the borrower, by early substantial reductions. Once reduced to the point of absolute safety there is no objection to slow amortization from the borrower. I would see no objection on a conservative 50-percent loan to reducing the annual amortization thereafter, so that it ran 25 years—2 percent of the property value a year on the balance. But I do see serious objection to starting at 60 percent and then applying 2 percent or 3 percent a year as amortization, because the mortgage is still above the danger mark for 4 or 5 years, if it starts on that basis.

Now, one other thing on the mortgage provisions of this act which I feel very strongly on is this: I believe it is a serious mistake to make it possible to borrow a mortgage at the Federal Reserve bank. In setting up the Federal home-loan-bank system, the first board deliberately—and so stated publicly—fixed the situs of the 12 Federal home-loan banks in different cities from the Federal Reserve cities, for this reason: We believed that the administration of long-term credit, which real-estate credit is, was a distinct and separate thing from the administration of short-term credit. There are lots of times when short-term credits should be tightened and long-term credits eased; and the reverse is also true.

If you are putting the rediscounting of mortgages into the Federal Reserve System, you are merging in the one institution control both of long- and short-term credit, and the policies, under the language of this act, will have to be identical, because the same rediscount rate will cover both types of rediscount.

I believe that, having the Federal home-loan-bank system, you should make mortgages rediscountable only with it, if the commercial banks are to carry them at all.

The present provisions extend membership in the Federal home-loan-bank system to building and loan associations, savings banks, and insurance companies, which are the chief mortgage holders. The rediscount privileges of the home-loan-bank system should be extended to cover mortgage loans of commercial banks, both in order that the handling of long-term credit might be kept separate and apart from the handling and control of short-term credit, and in order that the policies of credit administration on mortgage loans should not differ between the two institutions. If you have two institutions loaning on or rediscounting mortgages, you will have no uniformity of mortgage policy.

Now, a large part of the real-estate difficulties of this depression came from too great extension of mortgage credit, due to easy money.

In the long-range working of the home-loan-bank system its most useful public service, in my judgment, will come from a sound administration of the problem of real-estate credit, the prevention of booms in real estate, the prevention of too great an extension of building operations, and of speculative operations; the prevention of those extensions of credit which lead chiefly to the eventual collapse of real estate and which did lead to the collapse of real estate in this depression. But it can happen often—as it has often happened—that at the very time that there should be a tightening of credit on real estate, there should be an extension and loosening and relaxation of credit to the ordinary commercial banks against commercial transactions. But if you put the two functions into one institution, you render impossible the separation of credit control, which, I think the depression has taught us, is essential.

The psychology of the short-term lender is not the psychology of the long-term lender, and should not be. The view is not the same; the controlling background is not the same.

Now, you have a home-loan-bank system—and may I say, parenthetically, that while I believe it is being run splendidly by a very fine board of men—you should not give them control of any other problem or divide their authority over their problem.

Someone asked me how I would finance it. That is perfectly simple. Any study of the Home Loan Banking Act will convince anyone who is familiar with financing that the debenture provisions of that act will enable that system to expand as its financial requirements necessitate it. For all these reasons, gentlemen, the idea of putting the rediscounting of mortgages into the Federal Reserve System is a very serious mistake in this proposed legislation.

While we are talking of mortgages, it is my opinion that there should be one change in the banking act, whether you are going to pass this bill to expand the mortgage-lending powers of the banks or not. The banking act prohibits any bank from holding real estate, acquired as a result of foreclosure, or in any other way, except for its banking house, for longer than 5 years. Under existing conditions, that promises a slaughtering of the real-estate market sometime in the next 5 years. The banks have had to acquire enormous holdings of real estate. They should not have them, of course, but I think you should put in the law the same provision that is in the insurance laws of most States. Insurance companies—in which I also happen to be interested—are prohibited, in my State, for instance, and in New York State, from holding real estate longer than 5 years, but there is a saving clause, "except with the consent of the superintendent of insurance." There is no such saving clause in the National Banking Act.

I can give you a specific example of the way this works out. We have been compelled, in my bank, to take over a piece of vacant real estate in satisfaction of a debt. The only thing we can do with that property today is to make a long-term lease, and we cannot do that, because, under the law, we cannot hold it more than 5 years, and we have already had it for a year. We could lease it for an oil station if we could make a 5-year lease. Consequently, we have either got to slaughter the value of that asset, hold it without income, or write, as we did, to the Comptroller and get a noncommittal answer that the law says we can hold it but 5 years, but maybe we will not go to jail if we do.

Mr. Brown of Michigan. I think that is an excellent suggestion. Is there anything in the bill, at all, to cover that?

Mr. Fort. No, sir. Now, there are two or three other minor things that I want to speak briefly upon, and then one major question.

Under the provisions in here, gentlemen——

Mr. Hollister. Just a moment. Before we leave the mortgages, would you care to comment—or if you believe in more strictness in the taking of mortgages, would you care to comment on the existing mortgages which the banks already hold, where there might be some more liberal provision, so they will not be forced to liquidate, because of the fact that the margin has been reached?

Mr. Fort. I think you can perfectly properly put in a provision that any mortgage may be renewed, provided, at its original inception, it was within the statutory limit. I think that is an essential provision, if you are going to avoid foreclosures.

Mr. Ford. Did not Mr. Eccles suggest they be given authority to handle that by regulation, in his talks to us?

Mr. Fort. If the statute is going to be on the mandatory basis, I do not think you ought to leave that to the regulations—if Congress' policy is going to be that there shall be a certain percent as the maximum; but as I said earlier, the recasting of loans to prevent foreclosure should be permitted and also the renewal of mortgages ought to be permitted, without regard to the present-day appraised values unless the mortgage is hopelessly bad. There is no reason for forcing the banks into foreclosure, if you can avoid it. I think you should permit renewals, providing the loan was proper in its inception.

The CHAIRMAN. Of course, there are two things about that, Mr. Fort, that were contemplated. One, of course, being to afford an opportunity for State nonmember banks, who enjoy more liberal privileges as to loans on real estate, to join the Federal Reserve System; and at the same time, to prevent foreclosure in the case of member banks where the loans have run up beyond the present limitation.

Mr. FORT. Well, of course, I have not studied this act as you gentlemen have, but, unless I am very much mistaken, you have a provision in here which provides that any State nonmember bank, joining the System, can carry the assets that were legal under its State law, under regulations to be prescribed by the Federal Reserve Board and the Comptroller. There is such a provision in here, I am quite sure, because I noticed it, as I had some difficulty with the Comptroller, myself, as to marking off some assets we took over when we took over a State bank. I noticed it and wished it had applied before.

But I think it is in here. I think there is in here some provision that covers your nonmember banks exactly. If there is not there should be. There should be a provision that gives banks coming into the System, or those that merge with national banks, to have a sufficient time in which to meet the normal requirements as to assets.

Mr. FORD. On three different occasions, when Mr. Eccles was talking, he suggested he would supply an amendment that would give the Board wide latitude in letting those banks in.

Mr. FORT. I think you have got to do that, gentlemen. You have got to do a lot of things today, that we would not have done when we were investigating chain, group, and branch banking here 5 years ago, Mr. Chairman.

Mr. GIFFORD. Mr. Fort, might I ask you about your home-loan bank, because you were interested in it, and its inception. Shall we put into this act the denial of the home-loan people of deficient mortgages?

Mr. FORT. I do not know what you mean, Mr. Gifford.

Mr. GIFFORD. The Government will now own a great many properties; we have given them $8,000,000,000 to buy in loans and——

Mr. FORT. You mean waive the deficiency judgment provision?

Mr. GIFFORD. Yes.

Mr. FORT. I think that should be done universally. I think mortgage lending should be put on the basis of the mortgage and not on the bond or note. I do not believe in deficiency judgments anywhere, at any time.

Mr. REILLY. What about second mortgages?

Mr. FORT. I think we would be better off if we had none. I mean this: A lender makes a mistake, from his own angle, if he has only a shoestring in the property. Second mortgages are chiefly, in our section, the device of speculators and not of the permanent owner of the property.

Mr. FORD. Is it not a device of the speculator in all cases?

Mr. FORT. No; there are cases where second mortgages are taken by home owners who want to acquire a house and cannot get a mortgage for the full amount they need, except often largely on a second mortgage.

Mr. CAVICCHIA. That has been the cause of a great deal of trouble, has it not?

Mr. FORT. Yes, sir.

Mr. REILLY. You ought to outlaw them.

Mr. FORT. Well, I hardly think you can outlaw them, because there are cases of utility. For example, a man has a moderate first mortgage, say, reduced by amortization down to 35 or 40 percent. He needs a little additional money, and he has a real equity there. He prefers to take a second mortgage to pay off, not as a permanent addition to his original mortgage. Things of that sort I think are legitimate; and we all know we bankers occasionally need a second mortgage as security for some bad loan we have gotten caught with.

Mr. DIRKSEN. To abolish the deficiency judgments will mean that they will exercise a little more caution in their appraisals?

Mr. FORT. Yes, absolutely; the deficiency judgment certainly should be impossible after the property has changed hands. I have developed a theory that I have not followed out completely, that there should be in every mortgage a provision eliminating the obligation on the bond after the first change of ownership, but giving the mortgagee the privilege of calling the bond at the time of the change of ownership. In other words, when a man makes a loan to you, because he thinks you would keep up your payments, he might make a little more liberal loan than he would make to somebody else, but if he did, he should have the option of calling the loan, if you sell the property to somebody else that he does not like so well. But a provision that permits a deficiency judgment against the man who may have sold that property 20 years ago, when it has passed through 15 hands since is a vicious practice——

Mr. DIRKSEN. That would make it a personal mortgage, rather than a mortgage against definite security?

Mr. FORT. No; I say if you are going to have a deficiency judgment, at all, that is the way it should be limited.

Mr. DRISCOLL. If you foreclose the first mortgage, that wipes out the second mortgage, does it not?

Mr. FORT. Yes.

Mr. GIFFORD. I want to say this to this committee, and to you, Mr. Fort, that, seemingly, at present, the volume of foreclosures where there are deficiency judgments has assumed very great and important proportions.

I had a letter from a prominent lawyer last week, and I have written him several letters, in which he stated to me that they really loan on character of the person, and simply take mortgages as security, and he was representing a cooperative institution, a cooperative bank; and your viewpoint is extremely different, extremely important, and I want to say to you that it would absolutely frighten you to think that, in the county where you summer, I have two cases of properties of $7,000 mortgages, valued at $12,000 to $15,000, and assessed for $10,000 or $12,000, sold and bid in at $2,000.

Mr. FORT. Yes; we have had that everywhere.

Mr. GIFFORD. And they are being sued for the balance.

Mr. FORT. That is all wrong. That is legal under the old forms, but I think it should be abolished.

Mr. REILLY. Why should not the law provide that it should be discretionary——

Mr. FORT. That is true under the old bond. We passed a statute—I speak of New Jersey—but our courts held it was unconstitutional as to the old bonds; but as to the new mortgages, I think the deficiency judgment should disappear.

I think they are anachronisms from the old days, when real estate was not so often transferred from hand to hand. I do not think they belong in the law any more.

Gentlemen, I am going to have to try to get away on the 12 o'clock train, and if you will permit me, there are 2 or 3 minor matters I would like to speak of—1 major and 1 minor.

You have a provision in here on page 59, which requires the directors to carry one-tenth of the bank's net profits to surplus before paying dividends. I thoroughly approve of the purpose of that, but I say it is not going to work out in its present language. As drawn, a big bank, we will say, will have a surplus of $10,000,000 1 year and the next year it will have $10,000,750.42. I think you should revamp that section so that there will be a round sum contributable to surplus; and also so that a bank may, if it desires, anticipate the contributions to surplus in round sums.

If my bank wants to throw $50,000 over into surplus this year out of undivided profits, we should be able to continue to pay dividends until we have exhausted that $50,000 surplus contribution. I think a section can be drawn rather easily, so that we can have a definite figure, a round figure, in practically every bank in the United States.

Mr. BROWN of Michigan. You cannot put less than that amount you fix into surplus?

Mr. FORT. Yes; then you have to remember the other provision of law under which each bank must buy Federal Reserve bank stock to the extent of 6 percent of each accretion to surplus, under the new provision of the law. Then a bank's lending limit is 10 percent to any one borrower of its capital and surplus. I think the round-sum contribution to surplus would be a sounder thing, as an accounting practice.

Mr. RUSSELL. Have you made any comments that a bank could take it beyond that?

Mr. FORT. There are going to be a lot of banks whose one-tenth is going to be about 50 cents for some years to come.

The second minor thing——

Mr. GOLDSBOROUGH. What do you recommend, then, Mr. Fort?

Mr. FORT. That some language—if you like, I will prepare it in the form of a suggested amendment—some form of round sum, or some language that makes a round-sum contribution easier to handle.

Mr. HOLLISTER. Nearest a thousand dollars?

Mr. FORT. The nearest thousand dollars, or something of that kind.

Another minor thing, gentlemen, you have in here a provision for one-twelfth of 1 percent contribution for the Federal Deposit Insurance Corporation on all deposits. Postal Savings deposits have been largely turned back by commercial banks to the Government because they are unwilling to pay 2½ percent, under existing conditions as to the possibility of investment, with the result that the Postal Savings System is now chiefly backed by Government bonds. I am going to speak on that feature in a moment.

But if you put an additional one-twelfth of 1 percent a year charge on top of that 2½ percent, you are going to have almost all the rest of those Postal Savings handed back to you. The margin in them is very, very slim now to the bank that has them.

Mr. CAVICCHIA. Was it not the purpose of the Banking Act, the past year or two ago, to practically eliminate the Postal Savings?

Mr. FORT. I do not know. It has not worked that way. The purposes of Congress are beyond an ex-Member.

The CHAIRMAN. What we attempted to do was terminate the checking accounts in the Postal Savings, as you say it has not worked out. I hesitate to say why, but I think it should be made to work.

Mr. FORT. My thought on that is that the Postal Savings accounts ought not to pay one-twelfth of 1 percent, when they are secured by Government, State, or municipal bonds, in the first instance, deposited with the Treasury, since they are not on the same basis as other deposits and are not subject to guarantee, because they are usually away in excess of the $5,000 insurance provision.

The CHAIRMAN. Let me ask you a question there, Mr. Fort. Do you think, if we are going to have anything approaching an adequate system of bank-deposit insurance, we should differentiate between the classes of deposits, and permit one depositor to enjoy full protection, independent of the insurance system, and thereby have discrimination between the classes?

Mr. FORT. In the long run, Mr. Chairman, I think it will work out to accomplish what you have in mind, because I think the tendency will be to split the deposits. In the long run, if trouble begins to develop in banking in the United States again, particularly if it happens to hit a large institution, from then on, the large depositors would not keep all of their money in one bank. They would spread their deposits down to small units, so as to get the benefits of the guarantee. I do not think there is any doubt about that.

Mr. WOLCOTT. It cannot be applied to municipal deposits and—

Mr. FORT. No.

Mr. WOLCOTT. How do you take care of municipals that a bank buys, when it is compelled to hold Government bonds? Would you exempt that altogether?

Mr. FORT. No; I do not think I would. I do not think you can go beyond secured deposits.

Mr. WOLCOTT. That is what I mean.

Mr. FORT. If you specify the type of investment that a bank must buy and put up to secure its deposits, it is a low-yield security, necessarily. The limitation on the type of security you may give is such that it becomes a low-yield security. Now, to put on top of the fact that you must invest funds in that low-yield security, the additional charge of one-twelfth of 1 percent for those deposits is going to mean the turning back of a lot of them.

I am told, and I do not know whether this is correct or not, that $600,000,000 of Postal Savings were turned back to the Postal Savings fund by the banks in the United States last year, because they were unwilling to pay the 2½ percent.

Mr. GOLDSBOROUGH. As long as we send them Government bonds, they are going ahead on it without one bit of risk in the world, after we have made a present to them to the extent of $13,000,000,000, as we have done, and that is going to continue.

Mr. FORT. That is a matter of opinion, Mr. Goldsborough, that I have not the time to go into in detail, but I just mentioned that, since I think it is minor——

Mr. GOLDSBOROUGH. I do not think it is minor, at all.

Mr. FORT. What I have said about one-twelfth of 1 percent is relatively minor. I am coming to the major question of the Government bonds now. Of course, everybody recognizes that Government bonds are the premier security, but it still is a fact that realization on Government bonds for cash has to be accomplished in the market, and it certainly is a fact that, twice in less than 15 years, Government bonds have sold at 80, or below, in the market.

The possibility of the policy that this act contemplates—I speak now of the declarations of policy in regard to it made by the Governor of the Federal Reserve Board, and the general understanding of it—namely, that its fundamental design, in part, is to increase the amount of holdings of Government bonds by commercial banks and the Federal Reserve Bank System. Today, gentlemen, Postal Savings funds are chiefly in Government bonds. Federal Deposit Insurance Corporation assets are almost entirely in Government bonds. Forty percent of the bank assets, or more, are in Government bonds. You now propose in this bill to still further increase the holdings of Government bonds by the Federal Reserve System. In other words, the first line of deposit protection, namely, the Postal Savings fund, and the commercial banks, after the exhaustion of the present surplus reserves, which are temporarily the first protection of deposits, has got to be financed by selling Government bonds. Now you are planning here to put the entire Reserve System into Government bonds. The Federal Deposit Insurance Corporation already is.

The net result is that if any kind of serious trouble develops any of these intangible, unreachable waves of public sentiment which result in the withdrawal of a substantial volume of bank deposits for any reason—war, further disturbance of financial conditions, the collapse of foreign central banks, as happened to us when the Bank of England went in 1931, the disturbance of confidence through some crookedness on the part of some individual bankers, the fear of inflation on the part of conservative holders of large deposits, and whatnot—anything that happens to produce a substantial withdrawal of deposited money from the banks of the United States or the Postal Savings Fund System, must be followed by the immediate liquidation in large volume of United States Government bonds.

Mr. GOLDSBOROUGH. All that means, Mr. Fort, is this: That whenever, from time to time, the public finds out that there is only a very small amount of real money in existence—and as a matter of fact, this whole money process has been created by the banks—they are going to the banks after their money.

Mr. FORT. Well, that may be the thing that will do it, Mr. Goldsborough. I am not going to say. I have said that of a number of things, and there is any number of things that may produce it; but I say that what you are doing in this type of legislation, particularly when you put your Federal Deposit Insurance Corporation into Government bonds, on top of the Reserve banks, as long as you have your present banking system and your present monetary system, Mr. Goldsborough—I am not going to argue that phase of it with you—you are making it absolutely certain that at the moment the demand comes for money, for any reason, from the depositors of the United States, you are going to force liquidation in Government securities with no buyers.

Mr. GOLDSBOROUGH. And no ability on the part of the Government to issue its own money on the faith and credit of the whole people, and all of their assets to absorb Government bonds?

Mr. FORT. What you are doing here, gentlemen, really is making a forced levy on the thrift of America, as represented by the bank deposits, to buy Government bonds.

Mr. WOLCOTT. Of course, we have the potential stabilization fund of $6,000,000,000.

Mr. FORT. Well, $6,000,000,000 sounds like a lot of money, but if Government bonds once start being liquidated you will need it.

Mr. FORD. What other type of security would you have them put their reserves in?

Mr. FORT. The Federal Reserve banks' should be in more liquid securities, not dependent on the bond market.

Mr. FORD. Where are you going to get them?

Mr. FORT. I am not talking, gentlemen, a partisan proposition, but this business of putting the Federal Reserve banks in Government bonds has been going on too long.

Mr. FORD. But you are going on the assumption that this bill is being enacted for the specific purpose of putting it in form, are you not?

Mr. FORT. Yes.

Mr. FORD. What warrant have you for that assumption?

Mr. FORT. The statements of the Governor of the Federal Reserve Board.

Mr. FORD. I have heard nothing in any statement he made——

Mr. FORT. The statement was reported in the newspapers.

Mr. FORD. There was nothing he said here before this committee——

Mr. FORT. He is reported in the newspapers as saying that if the banks would not buy Government bonds, then this would compel it.

Mr. GOLDSBOROUGH. No, no; what he said was this: He very clearly indicated, although he did not want to say so outright, that he had no more sympathy with this largess we are handing over to the banks in the shape of Government bonds than some of the rest of us have; and he indicated that if the banks should take the position that they would not take the bonds, the Government could exercise its sovereign powers and relieve the banks of the necessity of issuing money by issuing it itself.

Mr. WOLCOTT. The act provides specifically that the policy adopted by the Open-Market Committee should be followed by the banks; and I remember very distinctly I asked Mr. Eccles the purpose of that, and the answer that I got from him, as I gathered it—as I gathered from him, his answer was this: That the purpose of it was to compel the banks to take the Government securities, just as Mr. Fort said.

Mr. HOLLISTER. He said if the time came when the Government felt that bonds should be acquired, and the banks thought otherwise, either the banks would have to take them or the Government would take over the banks.

Mr. FORT. Something of that sort is what I have reference to having seen.

Mr. GOLDSBOROUGH. I understood what he meant was that, if the banks were to cease to absorb these Government bonds, then the Government was not dependent upon the banks for its financing; it could issue its own money instead of having these banks do it, instead of having this money created by the necromancy of a bank clerk. That is what he said.

Mr. FORT. Well, you have stopped any issue of currency by banks through the call of the circulation bonds; that is, the Government has.

The point I want to make is this: My own bank, like most others, has 40 percent of its assets in Government bonds, and that is too much.

Mr. GOLDSBOROUGH. It is too much, but you are going to hold onto them, until you get better investments, and that is what you ought to do, of course.

Mr. FORT. It is too much facing the fact that you may have to liquidate them some day, presumably, either for the purpose of loaning for other purposes or for the purpose of meeting your deposit liability.

Mr. FORD. Is there not sufficient reserve at the present, so that the banks could actually lend up to 20 billion?

Mr. FORT. They can loan, but they cannot meet the deposits out of that 20 billion.

Mr. FORD. I understand that. Therefore, you would gradually get your assets into other kinds of loans?

Mr. REILLY. Mr. Fort, if the insurance-deposit loans work, there will be no more scares or withdrawals of money from the banks, will there?

Mr. FORT. Up to $5,000, you are right, but your big trouble is in the big withdrawals that come in through the exchanges, rather than the small withdrawals.

Mr. REILLY. What do they do with that money? Is it not a fact that runs on the banks have already been started by 96 percent or 98 percent of the depositors, who are now protected?

Mr. FORT. The runs at the windows, yes; but the 96 percent relates to the number of depositors, not to the amount of deposits.

Mr. REILLY. Those are the people who start the runs on the banks.

Mr. FORT. It is also true that the bank holidays in many States were forced largely by large deposits that were drawn through the exchanges and not the withdrawal of small deposits at the window.

Mr. GIFFORD. Mr. Fort, I have made this expression once or twice, and it seems to have very little value, but a very prominent member from New England said once "The more money you loan to the Government the less you have to loan to people."

Mr. FORT. That is true; but it is also true that the public is not borrowing today. I want to say, in defense of the banking fraternity, that despite the fact that we advertised in 1932 our readiness to loan money in our bank, when everyone said it was impossible to borrow, and cut our rate of interest by public announcement in 1934, we have found that there is no demand from business for money and there has been none for 3 years.

Mr. GIFFORD. Do you realize how out of date you are when the Governor of the Federal Reserve Board does not worry about $40,000,000 today or 5 years' balancing of the Budget. Why do you come here and try to argue with us?

Mr. FORT. I am not arguing with you, but I might argue with him.

Mr. CROSS. Mr. Fort, I noticed the other day in the bank clearings in New York, in 19 banking institutions, the demand deposits were in excess of $7,500,000,000.

Mr. FORT. Yes.

Mr. CROSS. They have had to do a lot of loaning in order to give that much credit. Of course, that is more money than we have, literally, because that is in excess of $2,000,000,000 that there is in the entire country. So that money is bound to be simply bank credit, check money.

Mr. FORT. It is on Government bonds, chiefly.

Mr. CROSS. So there must have been loans or must have been a lot of loans, in order to have that much deposit money, and that is demand deposits.

Mr. FORT. We have increased our Government debt $14,000,000,000 in 5 years, that is what has produced most of it.

Mr. CROSS. Do you count those deposits by the Government in that?

Mr. FORT. Yes; and the expenditure of Government funds.

Mr. CROSS. I notice the deposits are in excess of $500,000,000 and some odd——

Mr. FORT (interposing). Where, in New York commercial banks?

Mr. CROSS. In the banks that belong to the Clearing House Association.

Mr. FORT. I want to bring to your attention another suggestion. You have a provision in here on page 6, section 4, for no-par stock for the Federal Deposit Insurance Corporation. I have had a theory for 3 or 4 years that we should establish no-par capital stock for the banks, and I will tell you why. It is no secret in this room, of course, that there are a great many banks in the United States whose only existing capital today is preferred stock from the R. F. C. There is no secret about the fact that there is a vast number of banks which have still to take heavy write-offs. It would make a far straighter and simpler capital structure if those banks were allowed to restate their capital structure, transfer to surplus, and use for their write-offs a large part of what they now carry in their capital accounts, with the permission, of course, of the Comptroller of the Currency and the Federal Reserve Board.

I happened to have a hand in opening or keeping open some 32 banks since 1932, and, therefore, have seen the intimate, inside figures of a good many small and medium-sized banks. Mergers are the only salvation of a large number of these banks.

Now, to work under the existing statute with a minimum par value per share, you have got to have stockholder meetings on notice, and you will have to tell the stockholders in a weak bank what they are going to get; and when you tell some of them what they are going to get in terms of dollars they are going to close the bank by withdrawals before you can hold your meeting. If you had the ability to issue no-par stock, you could offer the stockholders of a weak institution some shares of stock of no-par value without too great a public disclosure of the whole picture, and thus eliminate by merger a whole lot of these weak institutions which are going to be a source of trouble in the future if they are not eliminated.

But no strong bank could afford to take over some of those banks and give them the stock which they would have to give if they had to adopt a definite capital value in dollars. To do so would make a demand on the surplus of the strong bank and weaken it.

But it seems to me, gentlemen, that while you are at it in reconstruction of banks you should insert a no-par provision in the law.

Mr. FORT. There is a picture in American banks, gentlemen, where something of that sort is going to be necessary. Now, the original objection of the Comptroller's Office to it 2 or 3 years ago was the disturbance to the assessment-liability feature on national-bank stock. But, of course, if this is necessary to be taken care of it could be done through using the same assessment liability, if you please, fixing it at whatever was the old par value. But unless you do something of this sort, a lot of these weak banks are going to be laboring and struggling along as individual units that can never make a dollar.

Not only that, but they are not going to be able to take the write-offs that would enable them to make an honest statement for 5 to 10 or more years.

If you let them restate their capital—if, for instance, they have $300,000 capital and have only $100,000 capital assets—the bank can send a letter to their stockholders saying, "We want to change our stock from 12,000 shares of $25 par to 12,000 shares no par." It can then restate its capital at $100,000, and take $100,000 into surplus and $100,000 into undivided profits, and use it for write-offs. If you will let it do that you will get their capital structure straight.

The important part of that is that the thing that has closed more banks, in my judgment, than anything else, has been the loss of nerve by the banker, as he saw his surplus vanishing and his capital getting a deep cut, and realized that he never was going to be able to pay dividends to his stockholders again for many years.

Mr. HOLLISTER. Did you not have a great deal to do with the preferred-stock idea in banks?

Mr. FORT. I believe so. I advanced that suggestion back in 1931 or early 1932. I now think that a really complete recapitalization proposal is what many banks need. Of course, there are a lot of banks that do not need it, but there is a mass of them—particularly among the small banks, gentlemen, in the small communities in this country—there is a mass of those banks that cannot begin to pay a dividend to their shareholders for 20 years, under the provisions of the existing law—10 years, anyhow.

Mr. FORD. What brought that condition about, Mr. Fort?

Mr. FORT. What brought it about is this: I would say a combination of different causes: Bad faith and dishonor in the management of a good many institutions, of course, but not in nearly as many as the loss of confidence in honestly run banks, due to the stories of dishonesty in others.

I think the story was something like this: There were in the country, in the State nonmember-banking system, entirely too many States which allowed banks to start with very low capital. I recall one State in which something like 68 banks closed in one day, where the total capital of the 68 banks, if my memory is correct, was under $1,000,000. They had in that State, I think, a $5,000 minimum capital limit. Now, that story of 68 banks closing got into the newspapers and the average person, in the average town, thought of those banks as he thought of the banks around his neighborhood; a bank was a bank; and they were not aware of the fact that these so-called "banks" that had gone under in large blocks really had been insolvent as soon as they paid the janitor his first month's wages—their capital was so small and they had no surplus. That kind of story scared the average bank depositor elsewhere and caused the spreading of those small-bank failures, particularly in the country districts, and may I say parenthetically, largely because of frozen-mortgage loans.

The continuance of stories of banks of this type closing produced a psychology in the country that the banks were insolvent as a group, and that produced hoarding, and that produced fear in the minds of the bankers.

There is no way in the world to make it more certain that people are going to be afraid of you, that they are going to distrust you, than to show that you are afraid of your own position. And the bankers got afraid to make loans for fear of withdrawals; and the moment they were afraid to make loans everybody in the community got suspicious of them, because they thought they must be tied up.

If you add on to that the requirement of publicity of the loans from the R. F. C., that just finished the picture, because the people began to think that any bank who borrowed money from the R. F. C. was busted.

Mr. DRISCOLL. Was that not pretty good proof—a bank borrowing money from the Reconstruction Finance Corporation was pretty good proof that the bank was in pretty good shape, because my banker friends tell me it was hard to get money from the R. F. C.

Mr. FORT. The trouble with that was that the R. F. C. took the best assets. There were some banks that were closed with all of the good assets in the R. F. C., and there were $3,000,000 or $4,000,000 or $5,000,000 of deposits left unsecured, or secured only with the bad assets, or slow assets, such as the banking house and things of that kind. But, of course, there are all kinds of excuses.

I have always thought that one psychological thing, along with the failure of the small banks, that at least in the East did a great deal of harm was the suspension of gold payments by the Bank of England. The old phrase "As safe as the Bank of England" had been a byword for strength for a hundred years, and when the Bank of England had to quit gold, I think that produced a psychological effect throughout the eastern half of the country, at least. I do not know what it did elsewhere. From all these things, it finally became like a snowball, and there was no stopping it.

But nothing hurt worse than lost nerve by bankers.

When a banker lost his nerve about making new loans, when a man came in to borrow money and the banker said he could not loan him, that man went out at once convinced that the bank was in trouble; and I think that contributed in a very large degree to the trouble, myself.

Mr. DIRKSEN. You said a moment ago there was no demand for loans; would you care to make the distinction that there was no attempt to secure loans by people who had sufficient collateral to satisfy the bank examiners?

Mr. FORT. Well, when you say "bank examiners", yes; it is impossible to satisfy the bank examiners.

Mr. DIRKSEN. Well, satisfy the bankers, then?

Mr. FORT. I can say this: We advertised in 1932 for 3 months—big ads—our readiness to loan money, and we did not have two applications from business men. And we cut our maximum interest rate in December and announced it publicly, and since then our loans have gone down rapidly. The repayment of the old loans have exceeded our new applications, although we have made it known that we cut the rate on mortgage loans and on everything else.

The only demand there has been for money has been on real estate in our community, things like building and loan associations and mortgage money.

The business men are in one of two classes: They either have all of the liquid capital they need for their present operations and are unwilling to start any more operations, because of some feeling of uncertainty on their minds of one thing or another—the N. R. A. in one man's case, inflation in another man's case, the A. A. A., or what not—some one thing, some another—something that strikes a man's mind as a reason why he is not ready to go ahead and do something—or if they are not in that shape, if they haven't all the money they need, they are in shape where their business is in such shape that you cannot loan them anything.

You do not get any applications from men who are merchants that you could do business with, or manufacturers. We are in a big manufacturing community, the city of Newark, and we just had one new manufacturer's loan this year in my bank, and we made it, and it was one the R. F. C. had turned down.

Mr. BROWN of Michigan. Governor Fort, I would like to interrupt. Do I understand, Mr. Chairman, that you are going on this afternoon?

The CHAIRMAN. Gentlemen, I guess Mr. Fort has finished as far as he desires to proceed without interruption.

Mr. FORT. I have only one other thing, gentlemen. I do not know whether you want to touch on this in the bill or not, but you have a reference in here about offsets, somewhere——

The CHAIRMAN. Just a moment, Mr. Fort. What did you start to say, Mr. Brown?

Mr. BROWN of Michigan. If we are going to decide this question of the location of the committee, I would like to be here, and I would like to see it laid over until 3 o'clock, when we meet again.

The CHAIRMAN. Will that suit all of you, gentlemen? Suppose we say we will come back at a quarter of 3? Well, say, 3 o'clock.

Mr. FORT. It will only take me a very short time, gentlemen, to finish.

The only other thing I have to say is this, gentlemen: It occurred to me in reading the bill that you have a reference in here that the insurance on deposits means that the guaranty applies to such part of the money due to any depositor for deposits in insured banks, "after deducting the offsets."

If you are going into a general reformation of banks, I have never seen any justification for allowing a borrower an offset against his deposits as a preference over a nonborrower in a bank. A depositor in a bank puts his money in and gets nothing but service. The borrower gets the use of the other man's money on the payment of interest.

The present system throughout the United States, State and National, results in the condition where, when a bank closes through bad loans or for other reasons, any borrower who has a deposit in a bank gets 100 percent of that deposit credited against what he owes, before the nonborrowing depositor gets any credit, and thereby reduces the net assets, so the borrower gets a larger dividend on his deposit than the nonborrower gets, because he gets full credit for his loan and then gets the same percentage of what is left that the nonborrowing depositor gets on his deposit.

Now, that is a survival of the old idea that, when you have cross transactions, you can offset one against the other, but I do not think that idea should properly be applied to modern banking, because a bank is dealing chiefly with other people's money when it loans. The deposits are other people's money, and not the bank's money; and the whole theory that permits a borrower preference in his dividend from the bank seems to be unfair and an improper custom.

In addition to that, it has worked out very badly in depressions, for this reason: It has been ruled that if a bank has rediscounted my note with the Federal Reserve Bank or the R. F. C., or whatnot, then the offset feature does not work; it can only work if the loan is still in the possession of the bank.

The result is that one borrower gets the credit of his deposits and another borrower does not get the credit of his deposits. That caused the failure of some banks during this depression, because borrowers who were wise to that situation went to the banks and demanded to see their note, to make sure they had not been borrowed against, so the bankers did not dare to borrow.

In some cases, wise men who did not want to draw their deposits out because they wanted to maintain their credit with the bank for the future, if the bank lasted through the depression, went in and borrowed money on collateral, or otherwise, equal to their entire deposit, and took it and put it in some other bank, with the result that when the bank closed they got 100 percent of their deposits as an offset to the notes, yet they had actually drawn their deposits out.

The whole system of offsets is a survival of the days of private banking, when, to a large extent, credit was an interlocking thing—

that is, the banker was loaning his own money—but today a banker is loaning 10 times, usually, of his depositor's money to what he is loaning of his own; and no borrower should get a complete offset, in my judgment, for the amount of his deposit.

Mr. GIFFORD. Mr. Fort, cannot banks force you to keep a deposit, if you get your loan there?

Mr. FORT. There may be a proper exception, Congressman Gifford, such as to say that any deposit which is contractually maintained should be offset. But, generally speaking, the practice is not a fair practice to all depositors and results only in the reduction of dividends to depositors.

Mr. REILLY. In giving those fellows a preference?

Mr. FORT. Yes, sir; a borrower is a preferred depositor in that bank.

Mr. WOLCOTT. Is not that largely a matter of State jurisdiction, the theory being that the bank could sue, in the State courts, the borrower on any paper he has in the bank?

Mr. FORT. Yes, sir.

Mr. WOLCOTT. And the State law allows him to offset the liability to the bank?

Mr. FORT. It is largely a matter of State law, but I have always taken the view that you can do about what you please—Congress can do what it pleases with the State banking system, if it wants to use its power, and you are pretty nearly doing that in this bill.

Mr. WOLCOTT. I agree with you there.

Mr. FORT. Now, you are deliberately here perpetuating the offset, however, in the F. D. I. C. provision; you are deliberately enacting that into a Federal statute.

Mr. WOLCOTT. If we assume jurisdiction for that purpose, we can also assume jurisdiction for other things.

Mr. FORT. Yes; and it has never seemed to me sound, under modern banking practices, where you are loaning other people's money and not your own to differentiate between two depositors.

The CHAIRMAN. Well, Mr. Fort, we thank you very much.

Mr. FORD. May I make one observation?

The CHAIRMAN. Yes.

Mr. FORD. Mr. Fort, you said that real estate is good security, if the loan is conservatively made. Real estate is a good security if conservatively made, but it is a bad risk, under all circumstances, for the borrower; is not that your psychology?

Mr. FORT. No; if it is too high a loan, it is a bad risk for the borrower.

Mr. FORD. Well, as a matter of fact, since a man has to pay taxes on real estate and keep it up and pay insurance, and all of the rest of it, and pay interest on the loan, it would always be a very heavy charge for the real estate as used as security for a loan?

Mr. FORT. Yes; but it may not be, if you hold the principal of your loan down to the point where the combined fixed charges and proper amortization do not exceed the fair rental value of the property—whether you are renting it or living in it—if it does not exceed what you would have to pay elsewhere for rent, or substantially exceed it, it may be a very wise investment for a man's savings. Then it is undoubtedly desirable, socially, to induce people to own their own homes; but it is unwise, sociologically, to induce them to buy their own homes on terms they cannot maintain with absolute assurance.

Mr. FORD. Then there is another phase: A man has a piece of business property in a very good part of a city, that is inadequately improved, but by reason of the tremendous value of the lot he is able to make a loan; is that kind of loan justified, at any time by a bank?

Mr. FORT. Rarely ever.

Mr. REILLY. It would depend on the rent, would it not?

Mr. FORT. It would depend on that somewhat. For example, if a man had a store business—a man who was a bank's customer had a store, and his business had expanded to the point where he needed a bigger store, and rather than use his working capital that he needed in his business to swing the building of the bigger store——

Mr. FORD. That is different.

Mr. FORT. The bank might very properly go in there to improve that property and develop that property as a business enterprise.

Mr. FORD. Assuming he was going to develop the property, but just take the value of a piece of property as consideration for the loan—that is not justifiable, is it?

Mr. FORT. You mean take the land alone?

Mr. FORD. Yes.

Mr. FORT. No; I do not think banks ought to make land loans.

Mr. FORD. There is no building on it, and therefore——

Mr. FORT. When I say "land loans", I mean where the big value is in the land.

Mr. REILLY. What do you think about the adequacy of one-twelfth of 1 percent for the insurance fund.

Mr. FORT. Assuming that the Government bond market should hold for 3 years, if you are going to put all of the money in Government bonds, that should be adequate. If Government bonds break in 3 years and all of the assets of your bank system and the Federal Deposit Insurance Corporation are in Government bonds, you cannot make it adequate.

Mr. HOLLISTER. And that figure would not be adequate?

Mr. FORT. No.

The CHAIRMAN. We will meet tomorrow morning at 10:30, and everybody be here.

(Thereupon, the hearing was recessed until 10:30 a. m., Wednesday, Apr. 3, 1935.)

BANKING ACT OF 1935

MONDAY, APRIL 8, 1935

House of Representatives
Committee on Banking and Currency,
Washington, D. C.

The committee met at 10:30 a. m., Hon. Henry B. Steagall (chairman) presiding.

The Chairman. The committee will come to order. We have with us this morning Mr. Frank A. Vanderlip.

Gentlemen, I am sure it is unnecessary to introduce Mr. Vanderlip to this committee. You all know who he is, and I am sure we will be delighted to have him discuss this bill which we are considering, H. R. 5357.

I assume Mr. Vanderlip desires to address himself to title II of the bill. Mr. Vanderlip, you may be governed by your own pleasure as to whether you will proceed first without interruption, indicate when you would like to submit to inquiries.

You may proceed.

STATEMENT OF FRANK A. VANDERLIP, NEW YORK, N. Y.

Mr. Vanderlip. Mr. Chairman, I do not mind being interrupted, if anything I say is not clear, or if you want to challenge it.

I am profoundly impressed with the importance of what is before you. You are going to give a mandate for the management of the currency of the country.

Mr. Cross. Mr. Chairman, I do not know whether the new members of the committee know Mr. Vanderlip's background, and I think it would be desirable for him to give that to us.

The Chairman. Will you state that for the record, Mr. Vanderlip? Of course, some of us know what it is, but some of the new members may not know.

Mr. Vanderlip. I do not want to give you an autobiography. I was Assistant Secretary of the Treasury under McKinley. I had a good deal to do with the formulation of the Federal Reserve Act.

After leaving the Treasury I went into the National City Bank of New York, and in a short time became president of that bank. I was president down to 1919. I have since retired from active banking, but have been extremely active in contemplating banking from a public aspect.

As I was saying, Mr. Chairman and gentlemen, you are, in my opinion, dealing with one of the most fundamentally important matters that has ever come before Congress. The Constitution lays on you an obligation; it says the Congress "shall" coin money and regulate the value thereof, and you are now proceeding, really for the first time in our history, to regulate the value of money.

For a century and a half, in common with a fallacy held by all the world, we thought we were regulating the value of money by attaching it to a given weight of gold. We supposed that an ounce of gold was a stable measure of value. We have found in recent years that it is not a stable measure of value at all. It is about as stable as it would be to use an accordion for a yardstick. The yardstick has to change when an ounce of gold brought three times as much in 1900 as it did in 1920. In the 4 years, from 1930 to 1933, inclusive, gold so changed in value that it bought twice as much as it did in the beginning.

It is like having a yardstick that is 3 feet long sometimes and 1 foot long at another time. It is not a measure of value to set up a weight of gold as your standard.

Now you are proposing a managed currency, because that is really the essence of this bill, and I believe it is a most proper objective step. But the bill does not really state the objective.

You give great powers, and properly, to a committee to manage the currency, but you do not state what their objectives shall be in its management.

Now, I understand that in the testimony of Mr. Eccles he has proposed a statement of the mandate. I only have it from a letter which I have, which he wrote. You are all familiar with it, I suppose.

Mr. GOLDSBOROUGH. If you have it there you might read it.

Mr. VANDERLIP. It says that "it shall be the duty of the Federal Reserve Board to exercise such powers as it possesses in such manner as to promote conditions conducive to business stability, and to mitigate by its influence unstabilizing fluctuations in the general level of production, trade, prices, and employment, so far as may be possible within the scope of monetary action and credit administration."

I do not think that that is a clear enough statement under which Congress should transfer its obligation to regulate the currency. Whatever action that board took could be fitted to some interpretation of this statement, it seems to me.

I was told last evening that the statement had been lifted bodily, but with a slight change, from the Canadian banking act. Well, Canadian banking has obviously been better than American banking, but still I do not agree that that is a proper form of the mandate which you should give to the managers of our currency system. There is the very heart and essence of your action.

To what purpose is the currency to be regulated?

Mr. GOLDSBOROUGH. Do you not think it is clearly the duty of the Congress, under the Constitution, to declare a mandate?

Mr. VANDERLIP. Absolutely; it has the obligation under the Constitution. The Constitution says so.

Mr. CROSS. May I ask for your reaction on this amendment, which I propose to offer in that connection: It shall be the duty of the Federal Reserve Board, with the use of the powers herein granted, continually to maintain, as near as possible, the wholesale commodity price level comparable with the wholesale commodity price level covering the period from January 1, 1921, to December 31, 1929, thereby stabilizing the purchasing power of the dollar and make it an honest dollar by making it dependable as a measure of value.

Mr. VANDERLIP. I should agree with that whole-heartedly.

Mr. GIFFORD. Would you withdraw all credit for those who produce and stop overproduction?

Mr. VANDERLIP. I would limit the total volume of bank credit. You have a section in this bill in reference to the cash reserves that must be held back of deposits, which gives you control of the total volume of bank credit. I believe that is necessary to a managed currency in a country where bank credit forms such a large proportion of the purchasing medium, as with us.

For example, if you set up such an objective as you mention there, a price index, and prices were raised to that level, there might then come a wave of optimism both on the part of borrowers and the bankers, and with the huge surplus reserves that there are, you could have an expansion of bank credit which would carry prices to some enormous height, in spite of almost anything you could do with the currency itself.

I would object most deeply to Government functionaries having to do with individual bank credits what some call the "nationalization" or "socialization" of the banks. But I do believe that in the management of the currency the managers should have a control over the total volume of bank credit and should be able to put a brake upon too rapid an expansion, so that prices could not be inflated and carried away beyond their currency control.

Mr. GIFFORD. Pressing my question further, overproduction causes an immediate crash in prices. Can you carry your money control so far as to control production to that degree?

Mr. VANDERLIP. Certainly you could control production if you controlled the total volume of bank credit.

Mr. GIFFORD. Could you carry that to that particular commodity that is overproduced?

Mr. VANDERLIP. No; a particular commodity might be overproduced.

Mr. GIFFORD. And it may be done in such large proportions as to affect many other commodities of a similar kind?

Mr. VANDERLIP. That is conceivable. But people look for some one thing of great significance that might go wrong under such a system to prove that everything goes wrong under such a system as we have had. To come to a currency that was managed, to use the language of the President, "so as to give the same purchasing and debt-paying power throughout a generation", would be one of the most beneficent acts Congress ever passed. We could afford to have incurred all the indebtedness—the billions of indebtedness—we have in this depression to get such an act.

There is an objection raised to setting up a price index as an objective. I was talking with a very distinguished member of the Government last night. His objection was this: "How do you know if you got back to the price level which you would have named, that you would have full employment—or perhaps we ought not to go that high—that we would have full employment then? You want to leave that to the discretion of the managers."

A stable currency which I want to see, a currency that will have, throughout a generation, the same command over goods, the same purchasing power and debt-paying power, is not a cure-all for every evil. Our currency difficulty has been the root evil, but a sound currency bill will not make hair grow on a bare head; it will not prevent technological unemployment; it will not completely cure the agricultural situation, although it will profoundly help it. If you do not ask too much of a currency bill nor expect a vast amount, you will get it if your bill is sound.

The CHAIRMAN. If I understand you correctly, the objective outlined in the amendments proposed by the Governor of the Federal Reserve Board are all desirable?

Mr. VANDERLIP. Yes, sir; that is, at least, those that apply to the management are desirable.

The CHAIRMAN. And the ends set forth to be sought by those amendments you regard as to be desired, do you not?

Mr. VANDERLIP. In the statement of objectives?

The CHAIRMAN. Yes.

Mr. VANDERLIP. They are too obscure to me to be able to analyze.

The CHAIRMAN. He says, "conducive to business stability." That is desirable, is it not?

Mr. GOLDSBOROUGH. That is a generalization.

Mr. VANDERLIP. That is a generalization.

The CHAIRMAN. To overcome, if it is necessary, unstabilizing fluctuations in the general level of production.

Mr. VANDERLIP. What are unstabilizing fluctuations in the general level of production?

The CHAIRMAN. I think you pretty well outlined that briefly already. That is what we want to get away from. If I understand you, you agree that that is desirable, but you think those ends can best be accomplished by reaching a desired price level and trust that to accomplish other desirable results and let that be our guide.

Mr. VANDERLIP. If Congress chooses a price level and it becomes obviously a wrong standard, Congress has the power to change it; but it ought not to delegate that power to the wisdom of a small group of men.

You have the obligation to state the objective of a managed currency when you are adopting a managed currency.

The CHAIRMAN. Let me ask you this question in that connection. If I understood you correctly a moment ago, you said that conditions might develop which would cause a rise in price levels far beyond that laid down as a guide, and that that was to be desired?

Mr. VANDERLIP. Oh, no.

The CHAIRMAN. Then perhaps I misunderstood you.

Mr. VANDERLIP. I said that with the management of currency alone you might get a rise in the price level above your stated objective.

The CHAIRMAN. That is what I understood you to say.

Mr. VANDERLIP. Let me go on. Because price is a function of the total purchasing medium, and the total purchasing medium is made up of the currency and bank deposits, therefore the control is both by currency and the total volume of bank deposits. You must have that power. You have it in the bill, perfectly stated.

There is much of this bill that I approve.

The CHAIRMAN. If I understand you, you approve the machinery established and you approve the powers granted, but you do think that there should be a specific direction rather than a declaration of general policies.

Mr. VANDERLIP. Above all else, I believe that there should be a general and specific direction. I do not want to give quite as sweeping approval as you made me give in your question.

Mr. REILLY. In other words, you think because Congress has this power it should tell this authority just what to do?

Mr. VANDERLIP. Yes, sir.

The CHAIRMAN. Let me ask you one other question. I think now I understand that, as you view the matter, it might be possible that, although we outline a specific price level as a guide, conditions might develop that would lift us beyond the level desired.

Mr. VANDERLIP. No; they would not lift you beyond that desired level with the control of the ratio of reserves to deposits which the bill gives you. You can prevent that.

The CHAIRMAN. You think that with that power, properly exercised, that cannot happen?

Mr. VANDERLIP. Absolutely.

The CHAIRMAN. Then I want to ask you this question: How far, in your judgment, do the activities of other governments, and conditions throughout the world, enter into our efforts, and the results?

Mr. VANDERLIP. There is no reason whatever why we should not do this independently. England is doing it independently, and most successfully, today. England is managing her currency, detached from gold, against a price level, holding her domestic price level within narrow fluctuations.

The CHAIRMAN. How long has she done that?

Mr. VANDERLIP. Since she went off gold, since the Ottawa Conference.

The CHAIRMAN. That was only a few months ago.

Mr. VANDERLIP. No; it was since she went off gold.

The CHAIRMAN. The Ottawa conference was last year, was it not?

Mr. VANDERLIP. No; the Ottawa conference was in the summer of 1932, I believe. But they did it back of that.

The CHAIRMAN. What I was going to ask you was this. Our trouble seems to arise only upon occasion. Some of our friends say it comes in cycles, and all that sort of thing, which I do not believe. But that has been periodic.

But I will ask you to address yourself to this inquiry, whether or not the practices that have been employed in Great Britain have been tested out long enough to assure us that they will protect against periodic developments such as we have experienced under the old order.

Mr. VANDERLIP. They have been tested out only for 3 years; nevertheless, in that time, in days of great depression with us, they have given England a measure of prosperity almost equal to what she had in the peak days of 1928 and 1929.

Mr. GIFFORD. Right there, let me ask you this question: You do not think for a minute that this country would stand for those harsh measures that England has adopted, do you? Suppose labor had even an inkling of what might happen to it if our currency was managed in the way that England managed hers in the last 3 years, what do you think would happen?

You have read, have you not, about the criticism they made of us for allowing labor to get the prices that they get in this country, when they have said they would never have allowed any such condition over there?

Do you think for a moment that such harsh treatment, in connection with what we are trying to do in raising prices, as compared with what they are trying to do in holding them down there, would be endured in this country for a moment?

Mr. VANDERLIP. I have observed with my own eyes a comparison of labor conditions there and labor conditions here. Take, for instance, the building industry over there. England, in the last 3 years, has constructed more houses than all the other countries on the continent of Europe together, and, I guess, plus what America has done. Compare that with our own situation, where 80 percent of the building-trade industry is idle.

Mr. GIFFORD. But compare the prices paid there, the wages of labor in building operations, with the prices paid here; do you think for 1 minute that our people would stand for that?

Mr. VANDERLIP. I have read their criticisms of the payments we make to our labor here.

Mr. GIFFORD. Do you agree with me that the wages paid to their labor in building operations are extremely small, as compared to the wages we pay to our men, organized into unions?

Mr. VANDERLIP. I think this takes us off the point.

I think one of the causes of our depression has been that labor has not received enough of the fruits of industry to enable them to purchase the products of industry.

Mr. GIFFORD. When they band themselves together and will not work for less than $12 or $15 a day, will managed currency cure that as it has cured it in England?

Mr. VANDERLIP. I do not think it was that that cured it in England. Of course, managed currency will not do a lot of things.

Mr. GIFFORD. Do not let us boast about what England has done by her managed currency, with the harsh treatment she has accorded her people, and then ask us to endure that for a minute.

Mr. HOLLISTER. As I understand it, Mr. Vanderlip, you are speaking particularly with respect to title II. You said that there are a great many things in title II that you are very much in favor of, but chiefly you thought it did not state specifically enough the object to be attained.

Is there any other provision in title II that you do not like? Take, for instance, the make-up of the controlling Board itself; is not that highly important?

Mr. VANDERLIP. It is highly important. I think there should be no ex-officio members of that Board. They are appointed by the President, and capable of being, perhaps, not removed, but diplomatically put out of the picture as members of a Board on which the Secretary of the Treasury is known to voice the President's opinion, as must always be the case; and you will find that the Secretary of the Treasury can outvote a majority of the Board; that is, the Board will conform. I think it is wrong to have ex-officio members of the executive family on this Board.

Mr. HOLLISTER. How do you feel about having a governor who could be removed at the will of the President as the chief man on the board, as he always has been?

Mr. VANDERLIP. I would not choose to do it that way, but I would like to do it in a different way. To my mind, if Congress will specifically state this mandate, the character of the people who are carrying it out becomes far less important. If you will specifically set up a mandate as to the price level, and make it mandatory when current prices are below that level to raise it, then they must inflate; then they must use one of the half-dozen levers, or all of them, to raise prices.

The CHAIRMAN. You desire a control of law as far as we can, and leave as little to varying judgment of men as we can?

Mr. VANDERLIP. Yes, sir.

Mr. HOLLISTER. You visualize the board as a body with little discretion, but merely following the distinct purposes set up in the law, and the provisions here, which are so easy to be handled that the discretion of the individual is rather unimportant?

Mr. VANDERLIP. I would compare it to the Supreme Court of the United States. A judge of the Supreme Court does not say whether he thinks the law is good or bad law; he says, "Does it come within the meaning of the provisions of the Constitution?" I want this governing body not to say, "Well, I think personally we ought to inflate," or "I think personally we ought to deflate." Their job is cut out for them. You said this price level must be attained, and they must inflate or deflate when current prices are above or below that level. They have a large measure of judgment, and it should be a body of trained men, because you put into their hands six different levers to work.

Mr. GOLDSBOROUGH. You might state what those levers are.

Mr. HOLLISTER. Let me follow my point for a moment. You believe that as far as it is possible they should be removed from political control, and that to that extent it would be better.

Mr. VANDERLIP. That would be better.

Mr. HOLLISTER. And probably they could be removed.

Mr. VANDERLIP. Yes. I am not afraid to have that amount of political control over a board as the Federal Reserve Board now stands, appointed for 12 years. They are long appointments. But I would rather have a board insulated from both business and political pressure.

Mr. HOLLISTER. Or banking pressure?

Mr. VANDERLIP. That is business pressure.

The CHAIRMAN. Let me ask you this question in that connection: Suppose we should adopt your view and undertake to lay down a specific guide for the Federal Reserve Board, and we set up that Board with a tenure of 12 years, and release them with those powers. They do not have to run for election——

Mr. VANDERLIP. No.

The CHAIRMAN. Like the Representatives, who make the law. They are responsible to nobody after this power has been placed in their hands unless they recognize the right of removal, about which there may be some question.

What would you do in such a situation if the Board, in such a situation, was unsympathetic, and for reasons satisfactory to themselves but no satisfactory to the country, said they could not do it and that the ends desired could not be attained?

Mr. VANDERLIP. I know how easy it would be to do that under this mandate that is proposed, which is not clear to anybody. It is not specific. Make your mandate specific.

The CHAIRMAN. I am assuming that our mandate would be such as you consider desirable. What would we do, if under such a mandate, they gave some reason that they found satisfactory to themselves for not carrying out the mandate of Congress, and they were in office for 12 years, and had those powers, without the right to recall them?

Mr. VANDERLIP. You could impeach them, of course. If you set up a price level, they will have to inflate or deflate if the prices are above or below. The price level will be known; your stated price level would be known, and their action would be direct.

The CHAIRMAN. If I understand you correctly, you would give those broad powers to the Board and recognize it as a body analagous to the Supreme Court?

Mr. VANDERLIP. Yes, sir.

The CHAIRMAN. And the Supreme Court judges could not be impeached for an unwise exercise of judicial discretion by the Supreme Court, could they?

Mr. VANDERLIP. I am not a lawyer, and I do not know.

Mr. CROSS. I do not think there is any discretion here. You have a wholesale commodity price level that is a fixed thing.

The CHAIRMAN. I am wondering about this. We can find in the case of the Federal Reserve Board itself where the law specifically set up definite machinery, but we did not create the office of Chairman of the Federal Reserve Board. They did that without provision of law.

Mr. HANCOCK. Will you not tell us what you would do today to accomplish the maintenance of the price level if you were a member of the Board and had the powers or levers at your command?

Mr. VANDERLIP. I would have to know what the mandate was.

Mr. GOLDSBOROUGH. Raising the price level to that of 1926.

Mr. VANDERLIP. If that is the mandate, there is one thing more. There should be no attachment of this currency to gold. That may shock some of you.

Mr. GOLDSBOROUGH. There are a lot of us whose feelings it does not hurt.

Mr. VANDERLIP. You should have a broad, proper gold market in which anybody can trade, as in the wheat or cotton market, and do what they would with the gold.

There is one thing that Congress has not the power to do, and that is to stabilize the foreign exchanges and at the same time stabilize prices. You cannot do those two things; you have to choose which you are going to do.

The CHAIRMAN. Right there you have reached the discussion that I sought to invite your attention to a little while ago.

You say they cannot do both.

Mr. VANDERLIP. No, sir.

The CHAIRMAN. Can they do one permanently without the other?

Mr. VANDERLIP. Yes, sir.

The CHAIRMAN. I will be glad to have you discuss that.

Mr. VANDERLIP. They did it permanently. They established the stability of foreign exchanges. The whole world has always been ready to take gold as a final payment in making money settlement of trade balances.

When Congress attached our dollar to a given weight of gold they gave to the whole world a put-and-call option to either sell gold at a fixed price or to buy gold at a fixed price. Anybody with gold anywhere in the world could bring it here and demand its value at 23.22 grains to the dollar. Anybody with free credit anywhere in the world, with free capital, could, through the stabilized exchanges, buy a New York bank account and draw against that in currency and demand gold, and get it, up to the time we went off the gold standard.

The whole theory of the gold standard was that if a country exported less than it imported, that balance had to be settled in gold, and then it was a beautiful regulator of foreign trade.

The gold went up and interest rates were raised as a result, because it affected your currency about 10 times, that withdrawing of gold. That made interest rates higher, it restricted credit, and it lowered prices. The very heart of the theory was that if the stabilized foreign exchange fluctuated your prices you could then go out and have a good market to buy it and a bad market to sell in, and you could correct your unbalanced foreign trade.

That answers your question, can you do one without the other. You have done one, and you can do the other. You can have a stable price level, but you will have a flucutating foreign exchange.

Our domestic business is 95 percent and our foreign business is 5 percent of our business. It seems to me, however, that you should begin to stabilize domestic prices and not foreign exchange.

The evil of the gold standard was that it led to a breaking down of foreign trade, in this way: Every nation needed to protect its gold stock. Therefore, they set up embargoes and quotas, every obstacle to importing goods into a country because that importation might take gold out of the country. Happily, now all but three nations are off the gold standard, and I think we will get an improvement when they are all off, that is, an improvement in our foreign trade, because I think some of these obstacles to foreign trade which were erected to protect gold stocks will be removed.

Mr. GOLDSBOROUGH. If it is agreeable to you at this time, Mr. Vanderlip, I think it would be illuminating to the committee if you would state those six levers you referred to.

Mr. VANDERLIP. I would have all currency issued by this body, call it a monetary authority, if you choose, as we have. But let us drop that and call it the Federal Reserve Board. That currency should be the exclusive currency of the country. I do not want the Federal Reserve banks to issue it. It must be done by the Government.

Mr. GOLDSBOROUGH. It must be society itself.

Mr. VANDERLIP. It should be done by the Government of the United States, as far as the Treasury is the Government, or have some entity, we will call it the Federal Reserve Board if that is more agreeable. But have an entity that is absolutely and wholly an arm of the Government.

They would take over all the gold that the Government has and all the silver, paying for the gold, presumably at the present price of $35 per ounce, and they would issue their circulating notes against that.

I would have taken away the currency privilege from the Federal Reserve banks. I do not believe that the issuing of currency is a proper banking function; it is a function of the Government, and all profit which lies in it should go to the Government.

But having taken that away, and wanting to maintain the Federal Reserve System for what it was organized to do—to be a central reservoir of reserves, a place where banks could rediscount—we would have to give them a certain outlet so they could rediscount.

So I would have it mandatory upon this body that they would always rediscount the rediscounts of the Federal Reserve regional banks, and any Federal Reserve bank, in turn, could come to this body with its rediscounts, and this body would be under obligation to rediscount them. So the Federal Reserve regional banks could always get currency, just as they can get it now. But it would only be the one kind of currency.

Then I would permit this body to buy and sell short-term Government obligations. I should prefer that they had not over a year to run. It should also be permitted to buy foreign exchange and bankers' acceptances. The balance sheet of this body you could write on a visiting card.

On the liability side there could never be but one item, circulating notes outstanding. This is not a bank. It never receives deposits, and it never could owe anything except its circulating notes outstanding.

It could not get out a note except for these items on the other side, which would consist of gold and silver, rediscounts of the Federal Reserve banks, United States short-term obligations, foreign exchange, and bankers' acceptances. There is your whole story.

They will control the interest rate in a measure by being able to name the rate at which they will rediscount the rediscounts of the Federal Reserve banks.

They can vary the amount of gold that there is under a dollar, because they will buy and sell gold in a free gold market, just as the Bank of England does it itself at the direction of the British Government.

Under the old compensated-dollar plan, people thought of changing the gold content of the dollar from day to day. That would have been a very difficult thing, and was not far-reaching enough to control the price level. But here you change the price of gold in dollars—or the gold equivalent of the dollar—every day, if necessary, only you do it in an open market for gold.

The gold value of the pound sterling is changed daily as the open market for gold fluctuates, but nobody has any objection to that. The fact that the pound buys the same amount of goods all the time is the satisfactory feature.

The CHAIRMAN. The important thing in this country is to get a dollar that will pay debts.

Mr. GOLDSBOROUGH. Will you please complete your statement?

Mr. VANDERLIP. What kind of a dollar will the debts of the United States be paid in if we do not look out? You are going to the poor people today with a baby bond and saying to them, "Give us $75 and we will pay you $100 in 10 years." Have you the slightest idea what the value of the dollar they get back will be? Will they have earned interest on their money or will they have lost some of their principal when the bond is paid? Unless you stabilize your dollar to a purchasing value——

Mr. GOLDSBOROUGH. Will you proceed and tell us about your levers, if you do not object?

Mr. VANDERLIP. The thing is so simple—I have given them all to you.

Mr. GOLDSBOROUGH. All right.

Mr. VANDERLIP. This body would have the choice of using some of those levers or throwing on all of them. They play the piano, but you set the tune. They must inflate if current prices are below your stated price level. But what is so much more important, they must deflate if prices get above the price level, and we are saved from a runaway inflation. We will know that in a generation the dollar will have the same purchasing and paying power. We will know that when we buy an insurance policy or an annuity, or when we borrow some money, we will be paid or we can pay back with the same kind of a dollar that we started with.

Mr. GOLDSBOROUGH. Mr. Hancock asked you what you would do at this time in a period of deflation. I would like to supplement that by suggesting that it is probably more difficult to cure deflation than to restrict inflation.

Mr. VANDERLIP. You can pull on a string, but you cannot push a string.

Mr. WOLCOTT. How would you inflate to get the price level back?

Mr. VANDERLIP. It is perfectly simple. Probably the important thing would be the purchase of short-term Government obligations, and the putting out of currency.

Mr. WOLCOTT. It is a very important matter, but this committee is in somewhat of a quandary as to what the economists believe in that respect.

Mr. VANDERLIP. Do not believe any of them.

Mr. WOLCOTT. Last year we had hearings on the bill providing for a Federal monetary authority, and you came down and gave us your advice. As I recall, many of the economists were of the opinion that the volume of money had little relation to the commodity price index.

Mr. VANDERLIP. I am not an economist, but I think that is a perfectly silly proposition, with the experience that the world has had with inflation.

Mr. WOLCOTT. Of course, we are taught to believe that the volume of currency has a decided influence on the commodity price index, and I recall very distinctly that there were about as many opinions on that question as there were economists who appeared before us, all the way from Pearson up to Fisher, or vice versa. So I will say very frankly I have not decided; I have kept my mind open in the hope that the economists would eventually get together and decide for us whether the volume of the currency had a relationship to the commodity price index that we have always been given to believe it did.

They tell us that the volume has little or no relationship to it, but that velocity controls it. In the Federal monetary authority bill, you suggest the only brake which we have on the velocity of cash currency and deposit currency and on bank credit is the open market operations of the Federal Reserve open market committee, or whatever body is set up for this purpose.

If it should develop that the theory of these economists who claim that velocity controls and volume does not control is correct, then have we provided anything in any of these bills for the control of inflation, or, the reverse, for the control of deflation?

Mr. GOLDSBOROUGH. Let me say this right there. These economists who claim that the volume of money does not control the price level undertook to base their statements, on what they said was a fact, and it is a fact, that the banks now have tremendous reserves which they are not using.

Mr. WOLCOTT. I may say that the theory under which the administration is proceeding today, in following the advice of Professor Warren, who spoke to us through Professor Pearson last year, is—and he believes, honestly and sincerely believes—that velocity has no connection with the price level, and that volume has no connection with the price level, but that the price level is tied to the value of gold, and he would control the commodity price level by fluctuations in the price of gold. That is the theory the administration is following today, and I do not know, and I do not believe the majority of the members of the committee know, which theory to follow. That is what causes the confusion.

Mr. VANDERLIP. Under the power conferred in this bill to fluctuate the ratio of reserves to bank deposits you would have the power to go up to a hundred percent, if you wanted to. You can absolutely control, with that power.

Price is a function of the total purchasing medium, and that is why you have to take in this control the total volume of bank deposits, because bank deposits as well as currency are purchasing media.

Mr. WOLCOTT. My point was simply this. Assuming I have a deposit of $500 to my account. The checks I issue against that, to all intents and purposes, are currency, and the number of times I turn that account over, they tell us, controls the commodity price index, and it is the turn-over of these things that the control or authority has no jurisdiction over, that might control the commodity price index.

Can this authority tell me how many checks I will draw against the $500? I might draw 1 check, or I might draw 200 checks.

Mr. GOLDSBOROUGH. I might overdraw my account.

Mr. WOLCOTT. Those 200 checks go through that many hands, and the velocity increases in proportion. I am asking for information.

What curb have we, or what regulation have we, governing the number of checks that a person shall issue, which are the same as currency issued from the Treasury through the Federal Reserve banks?

Mr. VANDERLIP. It is perfectly true that velocity has an effect on prices, as well as the volume of currency, and that by controlling the volume you can compensate for a change in the velocity. If your velocity increases you can decrease your volume, and you can keep your price level.

Mr. WOLCOTT. We have been told that the velocity of bank currency or credit currency depends largely upon the ability of the people to borrow from the banks, and I assume that could be regulated somewhat by regulation by the authority of loans made by the banks.

But is there not the danger that when this authority starts to tell the banks that they shall not make loans—and they have tried to regulate it, of course, heretofore by raising the rediscount rates—is there not a danger of people beginning to fear that the same thing will happen that happened in 1929, and then proceed to draw out their deposits, thinking that the banks are unsafe?

Mr. VANDERLIP. I think there is none of that danger.

Mr. CROSS. Would it not have a different psychological effect when you put the price level as a standard, that business and everyone else practically would feel that it would go there, and people would buy and have faith in prices going to that point?

Mr. VANDERLIP. It would be a breath of confidence which we so terribly lack now.

Mr. GIFFORD. I am rather new on this committee, Mr. Vanderlip, and I must be taught a good deal.

In connection with this wholesale price level, you seem to take it for granted that it is determined by a large number of commodities, and you have it in your mind all the time, I presume, that the dollar shall be stable, so far as concerns the man who is trying to live in this country and pay his debts.

But you do not have in mind the farmer, whose wheat or cotton may go way down in price, and who may look at you and say, "My wheat and corn are way down, but this other fellow has held the dollar up to just the same value." You do not care about the wheat farmer or the corn farmer or anybody who produces.

Mr. VANDERLIP. I care profoundly about him.

Mr. GIFFORD. It does not look that way.

Mr. VANDERLIP. Let us analyze that.

Mr. GIFFORD. There is an army of all sorts of productive interests in this country, but you pay no attention to them. Their products are all down, but the dollar is up.

Mr. VANDERLIP. I am paying the most acute attention to them.

Mr. GIFFORD. I am interested in them, and I want to be shown.

Mr. VANDERLIP. The price of cotton and the price of wheat are world prices, are they not? We cannot maintain our cotton values by storing it or burning it.

Mr. GIFFORD. Your remarks a while ago would indicate that we were going to pay no attention to world prices, but that we were going to take care of the 95 percent of our own market.

Mr. VANDERLIP. The world price of cotton, with every country off the gold basis, will be translatable from one currency to another by their respective prices of gold. There will really be a price for cotton in terms of gold that can be translated into each currency at whatever that currency's relation is to gold, or by naming the price of cotton in the currency of that country.

Mr. GIFFORD. Not when there is an embargo on cotton going to another country.

Mr. VANDERLIP. If the price of gold advances, the dollar price of the commodity will advance. We saw that to be so, and saw it to be so with rather remarkable accuracy in the repeated deflation of the dollar in gold.

This act, instead of being harmful to the farmer, will be a strong influence to bring about an equalization and to get over this disequilibrium between agricultural prices and other prices.

Mr. GIFFORD. Granting that, what are we going to do in the case of Japan, when she prefers to and will buy cotton of India? How will that help us in any way to keep up the price of cotton insofar as Japan is concerned?

Mr. VANDERLIP. We have lost our predominant place in the world's cotton market.

Mr. GIFFORD. How does that apply to that cotton?

Mr. VANDERLIP. We are not going to keep Japan and Russia out of war with a currency bill.

Mr. GIFFORD. Then your currency scheme cannot cure that, and your credit scheme would not cure that at all.

Mr. VANDERLIP. All right.

Mr. GOLDSBOROUGH. Following Mr. Gifford's questions, you do not mean to say that a sound currency scheme in this country which would obviously be reflected in the currency plans of other countries would not tend to create an economic condition which would tend to prevent war, do you?

Mr. VANDERLIP. Well, I do not want to prescribe a currency bill for all of the patent-medicine addicts!

Mr. GOLDSBOROUGH. I understand that; but is it not a fact that wars are largely the creation of disjointed economic conditions, and would not proper currency measures tend to help economic conditions, which, in turn, would tend to prevent war; is not that true?

Mr. VANDERLIP. I should hope so, but I would not feel insured against future wars by having even the most perfect currency.

Mr. GOLDSBOROUGH. I have not made such a suggestion.

I would like to have your opinion, because I think one of the things which a proper currency system would do would be to very strongly tend to disestablish national animosities.

Mr. VANDERLIP. I quite agree with that.

Mr. CROSS. The point I would like to discuss with you for a moment is this. I will take cotton, because I produce a good deal of cotton. Mexico is not so far below me.

When you buy cotton in this country, that is to say, when England, for instance, buys cotton in this country there has got to be first a translation of the pound into the dollar in order to pay me my 11 cents a pound for cotton.

When you translate the pound into American dollars, instead of getting par, the pound, with the new dollar, is worth $8.24. I am looking at the exchange table.

Mr. VANDERLIP. I do not understand that figure.

Mr. CROSS. Just listen to me for a moment. The exchange value of the pound now is $4.80.

Mr. VANDERLIP. Yes.

Mr. CROSS. So, when they buy my American cotton they have got to buy American dollars to pay me, and the exchange value of the pound is only $4.80 instead of $8.24.

Mr. VANDERLIP. When did they ever get $8.24?

Mr. CROSS. That is the sterling par value of the pound, with the new dollar, $8.24. The demand value is $4.80.

If they translate that into American dollars they pay me 22 cents for my cotton in English money, but they go to Mexico—and they are doing this in Mexico paying 34 cents a pound for Mexican cotton, in pesos. And the peso is way below par, too.

So they pay the Mexicans 34 cents a pound for their cotton, and that peso pays as much debts down there, and just as much taxes, and helps those people just as much in paying their domestic debts and taxes, and when they pay it in English money they only pay 17 cents, because the English penny or cent will buy 2 cents worth down there. But when you come here it will buy half as much worth.

So when they pay me 11 cents a pound for my cotton in English money they are paying 22 cents. So they go to Mexico and pay 34 cents.

In India their money is attached to sterling and they swap it penny for penny. If you pay 17 cents in Indian money, which is the rupee, they pay the same thing in English money; that is, 17 cents. They pay the cotton producers there 17 cents. So it would be foolish to come to America and pay me 22 cents when the English money can be translated into the same number of units in India.

Mr. VANDERLIP. All those things refer back to what each currency will exchange for in gold dollars, and the gold price in each currency will come out just about the same. The net prices are the same when they are referred back to a common point.

Mr. WOLCOTT. Is not that all dependent upon all of the gold nations, establishing the same value for an ounce of gold?

Mr. VANDERLIP. The same value in what, in their currencies?

Mr. WOLCOTT. The same as the exchange value at the present time, whether it is in their currency or not, as long as there is a stabilization of the gold value that is recognized by all of the countries.

We pay $35 an ounce for gold, and England, in the equivalent of their money, pays perhaps $30. France might pay $28 or $37.

Mr. VANDERLIP. But England does not pay dollars; it pays pounds.

Mr. WOLCOTT. I mean in terms of dollars; reduced to dollars.

Mr. VANDERLIP. Wait a minute. If you do that, you have to assume stabilization between the dollar and the pound.

Mr. WOLCOTT. Yes.

Mr. VANDERLIP. There is no such stabilization.

Mr. WOLCOTT. Do you not tie this dollar to the value of an ounce of gold?

Mr. VANDERLIP. I tie the dollar to the 1926 value for an ounce of gold in each currency.

Mr. WOLCOTT. If the value of an ounce of gold is the same in England, in India, in the United States, and in Mexico, following the illustration used by Mr. Cross, then when you reduce these other moneys into terms of dollars we are all on an equality, and

I predicated my question upon that. Does not this scheme depend largely o nall nations, establishing an international value of gold?

Mr. VANDERLIP. Not in the slightest. You just said that the price of gold is the same in England, Mexico, India, and the United States. What do you mean by that; the price of gold measured in what?

Mr. WOLCOTT. In that example we are talking in terms of a bale of cotton.

Mr. VANDERLIP. The value of gold—its purchasing power—will be the same in India, Mexico, and the United States. If you translate the relative differences of their currencies, you are measuring in the currencies of those countries. You could take Mexican money to buy gold, or you could take Mexican money to buy United States money, and then buy gold, and the result would be the same. That is, the value of gold is the same in the three places. But you are obscure as to how you measure the value of the gold dollar. You measure it by different measuring sticks.

Mr. WOLCOTT. I think that is the whole point. Assuming, for instance, that you take 70 pesos to buy an ounce of gold, the relation between the peso and the dollar would be 2 to 1, and the value of the peso would be 50 cents.

So, if a pound of cotton sold in America at 22 cents, it would sell in Mexico for 44 cents, and in England, in reducing its pound to pesos or dollars, it would have the same relative value.

Is not that all dependent, is not the value of the peso and the purchasing power of the peso and the dollar, dependent upon the world value of gold?

(Thereupon the committee took a recess until 2:30 p. m.)

AFTERNOON SESSION

The committee reconvened at 2 p. m., at the expiration oi recess.

Mr. REILLY. Gentlemen, please come to order.

Mr. WOLCOTT. I think that I had a question that I asked Mr. Va derlip that he wanted to answer before we go any further.

Mr. REILLY. All right, Mr. Vanderlip.

Mr. WOLCOTT. The proposition was that Mr. Cross had raised a question that we remove the disparity between the currencies of the different countries of the world so that the price of cotton would be the same in England and Mexico and the United States, and so on. We were discussing the reason for that, and it was asserted that it was all tied up to the international value of gold. I think that was the line on which we were progressing.

Mr. VANDERLIP. That is the case. Cotton sells substantially in every market of the world for the same number of grains of gold. The prices differ in the currencies of those countries in just the same proportion that those currencies bear to gold.

But if you would raise the price of gold in this country, you would raise the price of cotton in dollars, because the price of cotton would remain the same, reckoned in gold, and the dollar has a new relation to gold—not so valuable.

In thinking of values, you have got to think in terms of relativity. The value is the exchangeable quality of the commodity for other commodities of commerce, and a definite weight of gold is not a measure of value, because its exchangeability for other commodities fluctuates.

Mr. WOLCOTT. That was my point that, because of the relative value of an ounce of gold fluctuates, it causes a fluctuation on international exchange which is not overcome by the stability of the currency of one particular country, without agreement among the countries that an ounce of gold would have a stable value for all international purposes.

Mr. VANDERLIP. The point of reference of all of these currencies is to an ounce of gold, and currencies will—it will take as much currency to buy, in one country, an international product as it will take in another, if you translate those currencies into their exchangeability for gold.

Mr. FORD. May I ask one question?

Mr. REILLY. Proceed.

Mr. FORD. Mr. Vanderlip, there is one thing I would like to ask you, and that is this: You say that we are speaking of deflation and inflation, if we put a direction in this bill that says to the Federal Reserve Board they should bring on a stabilization of our dollar on the basis of the 1920 to 1929 average price level, which is supposed to be some place around the price level of 1926; and if, in the course of 6 months, we will say, there was a tendency for prices to rise beyond that level, could the Federal Reserve Board, by utilizing its existing levers—for instance, it could raise the reserve rate, it could order the open-market operations, or it could fix a new rediscount rate—would that, in your judgment, operate to keep things stable?

Mr. VANDERLIP. You say they could change the exchange rate? They cannot change the exchange rate; they can change the price of gold. If you detach yourself from gold, with the others powers—and all of them that are now in the bill—you can absolutely stop the inflation above the stated level that you authorize.

Mr. FORD. That is your reasoned judgment?

Mr. VANDERLIP. Yes.

Mr. WILLIAMS. Now, Mr. Vanderlip, I understood you to say this morning—and I did not understand that you had finished the argument you had with someone who represented the Government with reference to your objective, or the objective that you think should be put in this bill, and that is the commodity price level, the general commodity level of 1926, or from 1921 to 1929—if that was raised, or if you should stabilize that price level, and if there is still left a large army of unemployed, what would be the result of that? Or would the fact that the price level was raised to that point necessarily carry with it business revival and revival of employment?

Mr. VANDERLIP. Not to full employment, necessarily. During that period in which we had that price level, we did not have full employment. The question of technological unemployment is a very serious question, and I believe we have to have social legislation to cope with that problem; you cannot insure complete employment by a currency bill. I do not pretend it would do that.

Mr. FORD. Is not there an element of unemployables in the country?

Mr. VANDERLIP. Certainly, probably 2,000,000, or more.

Mr. WILLIAMS. Would there not also be an army of 12,000,000 or 13,000,000 unemployed?

Mr. VANDERLIP. There will not be if you reestablish the price level of 1921 to 1929.

Mr. WILLIAMS. Well, now, what assurance have we that we will get back employment? It seems to me that it would not be desirable to stabilize this price level, unless it brought with it a full measure—I will not say a complete measure—of employment; but if we still had a large army of unemployed, it seems to me we have not gone anywhere.

Mr. VANDERLIP. You have not got your price level high enough, or the change of the price level does not do any good. Which alternative is there?

Mr. WILLIAMS. Well, it is just a question of whether one will produce the other or not; whether an increase of your price level, say, to the 1926 level, will bring back into employment this large army of men.

Mr. VANDERLIP. That must be a matter of opinion. My opinion is, it will bring back into employment a great proportion of the unemployed.

Mr. WILLIAMS. As I remember the chart that was submitted to us by the Federal Reserve authorities when they appeared before this committee, it showed that England, during the last 5 years, had been able to stabilize the price level——

Mr. VANDERLIP. Fairly well.

Mr. WILLIAMS. Fairly well?

Mr. VANDERLIP. Yes.

Mr. WILLIAMS. But that it had not had any appreciable effect over the unemployment question, because that is a question that had varied very, very greatly.

Mr. CAVICCHIA. May I correct you there, Congressman?

Mr. WILLIAMS. Yes.

Mr. CAVICCHIA. I remember studying that chart, and it shows that the peak was at 3,000,000 unemployed, and in the past year and a half, or in less than 2 years, that had gradually gone down and stopped at 2,000,000 unemployed, but the price level during that time had remained absolutely constant.

Mr. WILLIAMS. Yes; there was a variation of four times as much, relatively so, in the unemployment as there was in the price level.

Mr. CAVICCHIA. Yes; and I remember asking Governor Eccles this question: That the price level necessarily has no relation to unemployment, according to the English chart? And he said that was true.

Excuse me for interrupting.

Mr. WILLIAMS. If that is true, then you get back to a question that is bothering me considerably; that by raising and stabilizing this price level, the question in my mind is, have we not made conditions worse, instead of better, to the large army of unemployed?

Mr. VANDERLIP. No; in my opinion, it is the reverse.

Mr. CROSS. May I ask a question there?

Mr. WILLIAMS. Yes.

Mr. CROSS. Mr. Vanderlip, profits depend upon prices, do they not—adequate prices?

Mr. VANDERLIP. Not necessarily.

Mr. CROSS. I mean adequate prices. You have got to have adequate prices before you can have profits. With adequate profits resulting in employment—I mean with adequate prices resulting in profits, and profits mean employment and expanding and putting on labor, does it not?

Mr. VANDERLIP. It depends somewhat on where the profits go. If a fair share of the profits go to wages, so that goods are consumed, it does.

Mr. CROSS. So that as your prices go up, profits come into existence, employment develops; and as employment is increased, the purchasing power, as the result of labor and people getting money—the purchasing power develops and increases.

Now, does it not all hinge right back on having a price level that is adequate and that will bring about—and we do know we did have profits and lots of activities when we had such a price level, whether in 1926 or from 1921 to 1929.

Mr. VANDERLIP. There are many situations that hinge on the necessity of having a higher price level, or going into bankruptcy. When you have debts incurred on the higher price level, and people cannot pay them on the present price level, there is insolvency.

Mr. CAVICCHIA. Mr. Chairman, may I ask through you whether Mr. Vanderlip has finished expressing to this committee his views on the monetary question; because there are some other parts of this bill that some of us would like to ask a question or two about.

Mr. VANDERLIP. I have been handed, during the recess, the recommendations of the American Bankers' Association; and in the main, they are favorable to the bill. As you know, they want some alterations of it.

Mr. WOLCOTT. Are they favorable to title II of the bill?

Mr. VANDERLIP. Title II, in the main; yes. They want some changes in the bill, but in the main they are favorable to title II.

Now, in my opinion, they do not go far enough. They say something about the mandate that you are going to give as the objective in managing the currency. I regard that as of the most vital importance. In fact, I doubt—I am not a lawyer and so my doubt is of little consequence, but I doubt the constitutionality of the bill as it is drawn here without any mandate, at all. You are delegating the policy you are advocating, and I do not believe you have got the constitutional authority to do that.

The CHAIRMAN. Let me ask you this question: Are we not in reality finding a different way for the exercise of the authority that has already been conferred upon the Federal Reserve System?

Mr. VANDERLIP. Yes; I think you are, in some measure, and in a large measure, but——

The CHAIRMAN. I do not know whether the question you are asked has ever been passed upon, or not——

Mr. CROSS. It has never been attacked before the Supreme Court.

Mr. SPENCE. They are pretty close to it in the "hot oil" case.

Mr. CAVICCHIA. Mr. Vanderlip, had you finished?

Mr. VANDERLIP. Just a moment. That, I think, is an essential thing, that you define the mandate and set up the objective of regulating the currency. I do not believe you can delegate that.

Then I feel very deeply that you should do another thing:

You say we are on the gold basis now. Well, we are attached to it by the most tenuous thread. You are on the gold basis now, to this extent, only—that gold can be obtained for shipment to another country that is on the gold basis when the trade balance demands a remittance and the remittance cannot be obtained through exchanges except at a cost above $35 an ounce. You cannot ship gold to England, for example; you have got to do it surreptitiously by shipping it to France. There is no redemption of money. You are simply not on a gold basis at all; and if the gold bloc further fades, as I believe it will, you will not be on the gold basis at all, under the law as it is now written.

I think you should detach your currency from gold. You should not have a call upon the Government for dollars by anybody who has the gold to deposit, nor should you have a call on the Government for gold by anybody who has dollars and offers them for redemption.

Mr. WOLCOTT. Mr. Vanderlip, in that connection, what would you suggest that we substitute for gold as a measure of value in our international exchange?

Mr. VANDERLIP. I do not recommend any substitution. Gold is the final means of settling balances, because gold is acceptable to all countries.

Mr. WOLCOTT. We will assume that France goes off the gold standard, and all of the major nations of the world are off of the gold standard, and the only demand for gold is for the fine arts——

Mr. VANDERLIP. No; no.

Mr. WOLCOTT. Where is the other demand for gold? Then if it is not used for a monetary base, all the currencies will be——

Mr. VANDERLIP. All the currencies will be offered back for the international settlement and——

Mr. WOLCOTT. They are predicated upon the demand for gold in that country which makes a market for gold, and they would rather take gold than any other commodity because of its rarity and worth; but if we create a situation where this gold is of no value whatsoever as a monetary base, then the only purpose that people use gold for is in the fine arts, except in one or two instances. Then how can we settle our trade balances if there is no demand on the part of France, which has an advantage because of the trade balance in her favor? Then surely, if there is no demand for gold in any country, either as a monetary base or for any other reason, they will not want gold, will they?

Mr. VANDERLIP. Oh, yes; they will want it quite as certainly as they have always wanted it, because it is a means of settling trade balances.

Mr. WOLCOTT. It is now; but assuming that all of the nations go off of the gold standard and we get above our 80 percent of gold, and the other nations say, "All right, you have got all of the gold—you have got all of what we use for our currency; therefore, we will go on a commodity basis; we will average the prices of commodities as we have here in some instances"—taking 784 commodities in the Bureau of Labor Statistics—and we will create a commodity dollar. We don't want your gold, except as it may be a commodity, one of the 784 commodities behind our dollar." There is no demand for that gold, and we will then be unable to settle our trade balances with gold. That is my fear.

Mr. VANDERLIP. I can imagine your fearing that, but I cannot imagine that ocurring in a thousand years, because from the dawn of civilization it has been ingrained in the human mind that gold is the most desirable of all things.

Mr. WOLCOTT. Is not that because of its rarity, that it has been used as the base for the currencies of the world?

Mr. VANDERLIP. Yes; and the world is accustomed to it and will continue to use gold to pay international balances.

Mr. WOLCOTT. We are assuming a condition where there is no further demand for gold among the nations of the world as a monetary base.

Mr. VANDERLIP. That will be a long time before it comes, so long that none of us will ever see it.

Now, there is objection raised to fixing the price level under a mandate, on the theory that we could not raise the price of gold, under such an arrangement as I propose; that the only way you could raise the price of gold would be by buying more, and we have already got too much. You remove the embargo on holding gold, so that it is no longer a criminal offense to hold gold, so you can hold it as freely as you could hold cotton or wheat, and you will find that there will be such a demand for gold that the price of gold would rise markedly, without any operations of the Federal Reserve Board.

Mr. CAVICCHIA. Would that have any adverse effect upon our commerce, if we pay for all of our goods with gold?

Mr. VANDERLIP. Well, if you speak of our domestic demand they cannot take all of our gold without giving us something in the place of it.

Mr. CAVICCHIA. And that would be gold?

Mr. WOLCOTT. Wait a minute. It might be goods or—

Mr. VANDERLIP. We will not take the goods.

Mr. WOLCOTT. Or perfumes or other commodities, but you see we cannot use perfumes as a commodity behind our monetary unit. We can exchange our gold for wheat, and so on.

Mr. VANDERLIP. No; we have been taking gold in enormous quantities, because we sold goods and would take no goods in return. We will eventually drain the world of gold, if we go on in this way.

Mr. FORD. Our trade balance this year is $421,000,000.

Mr. CROSS. A country that has a trade balance constantly—if gold is used to settle the international balances only, and if a country constantly has a trade balance in their favor, does that not, of necessity, draw the gold into that country?

Mr. VANDERLIP. Certainly; so long as there is any gold to draw. If you take goods and you cannot sell goods, what else is there left? But foreign trade must, in the end, be the exchange of goods for goods. That is how you have got to balance the foreign trade in the end. If we do not want to take any goods, we must not want to sell goods.

Mr. CROSS. Suppose our exports amounted to $3,500,000,000 and our imports amounted to $3,000,000,000; we have purchased $3,000,000,000 worth of foreign goods, and we have sold $3,500,000,000 of foreign goods, which leaves us a trade balance of $500,000,000. Now, how are you going then to settle that $500,000,000 unless you settle it in gold?

Mr. VANDERLIP. There is no other way, except credit. There are only three ways you can settle a trade balance—that is, with goods, with credit, or with gold—and if we have exhausted, in the end, all of the gold there is, we will not sell more goods than we buy.

Mr. HOLLISTER. And credit or debit them?

Mr. VANDERLIP. That is all.

Mr. CROSS. In credit we simply, for instance, buy their bonds?

Mr. VANDERLIP. Yes.

Mr. REILLY. Now, if all of the nations of the world abandoned the gold standard, would gold go up in price?

Mr. VANDERLIP. In my opinion.

Mr. REILLY. Why should it?

Mr. VANDERLIP. When you say "go up in price"——

Mr. REILLY. Right on that point, let me make this statement: The silver advocates argue that way, because silver has gone down in price; and by demonetizing it, why should it go down?

Mr. VANDERLIP. Let us see what that means. Gold goes up in price—in what price? In the price made in dollars. Another way of putting it is this: Would the dollar depreciate? Yes; measured in gold. It is just like the ends of the teeter; if gold goes up in this country, then the value of any particular thing depreciates as against gold.

Mr. REILLY. Why has it not worked with silver?

Mr. VANDERLIP. Because silver is not a commodity of international universal acceptance.

Mr. REILLY. It is the money of the greater part of the world.

Mr. VANDERLIP. In population, perhaps. If you want to count China—well, I doubt it; but I am not a silver expert.

Mr. REILLY. As I see it, it is rather inconsistent; I do not know. It may be true. The argument has always been that we should have more money, because so many nations are using gold for money that there is not enough to go around. Your argument is, then, that when all of the nations abandon gold, it becomes more valuable?

Mr. VANDERLIP. It will become more valuable—in their currencies. You can put it the other way, that the currencies of all of the world will depreciate.

Mr. REILLY. If you controlled our currency to the right level, our dollars would have the same purchasing power?

Mr. VANDERLIP. Not in gold.

Mr. REILLY. If gold is not used, what good is it? It is simply like iron, or copper, or any other commodity.

Mr. VANDERLIP. It is universally acceptable.

Mr. REILLY. But it would be of no use for exchange—international exchange—would it?

Mr. VANDERLIP. There is use for it now.

Mr. REILLY. We use it as a backing for money. France uses it as a backing for their circulation. It has been used in three nations, at least.

There is another question, Mr. Vanderlip. What you wanted us to write into this bill is the specific direction to this monetary authority to proceed immediately to raise the price level to 1926, and keep it there?

Mr. VANDERLIP. If that is what you want to do; yes.

Mr. REILLY. Is not that what you want?

Mr. VANDERLIP. I want you to state specifically what is the objective of managing the currency.

Mr. REILLY. That is your objective—the 1926 price level?

Mr. VANDERLIP. My advice is a price level. The 1926 level is not sacrosanct in my mind, at all. I am inclined to think it is of justice to the creditor, but you are not putting the 1926 price level into effect. In respect to the debtor, it would be a disastrous thing to the debtor to stabilize at the present price level; but the point at which you put the price level has nothing to do with the philosophy of managing the currency.

Mr. REILLY. Well, I put 1926 because that seems to be the price level that people who claim we have not enough money, want.

Mr. WILLIAMS. Do you think that would be any advantage to the Government, itself, or the Federal Reserve System?

Mr. VANDERLIP. I think the Federal Reserve System should be the bankers' banks—that it should be run by bankers—but I think it should have taken away from it the currency-issuing privilege. The currency-issuing privilege should not be given to banks that are operated for profit, but it should be in the hands of the Government itself.

I would also take away from the Federal Reserve System open-market operations. They should be conducted by the Federal Reserve Board, if you are putting this authority into the hands of the Federal Reserve Board. I would clothe that Board with all of the powers for the management of the currency, but I would not have it exercise powers over individual credits, which should not get into socialized banking.

I should leave the Federal Reserve Board to be the bank of bankers, and run by bankers, but I would take these privileges away. I would take these privileges away from them that I do not believe they should have.

Mr. WILLIAMS. Do you not think the System could be run just as economically and efficiently under Government ownership as it could under private ownership?

Mr. VANDERLIP. No, sir.

Mr. WILLIAMS. You do not think that could be done?

Mr. VANDERLIP. No, sir.

Mr. WILLIAMS. There would be a saving to the Government if that could be done.

Mr. VANDERLIP. Why?

Mr. WILLIAMS. In the interest that is paid to the member banks.

Mr. VANDERLIP. They would get all of that profit in the operation of the Federal Reserve Board in their currency management.

Mr. CAVICCHIA. As I understood you this morning, Mr. Vanderlip, you did say that the profit that heretofore has gone to the Federal Reserve Board, or the Federal Reserve banks, would go to the Government?

Mr. VANDERLIP. Certainly. The Government, through this body, would put out notes and would take over the gold and silver, which would not pay any income. But it would have the Federal Reserve regional banks' rediscounts, and the interest from short-term Government obligations, and bankers' acceptances, and all of those pay profits. There would be huge profits, very considerable profits to the Government from this authority that would manage the currency.

Mr. WILLIAMS. I do not understand you to mean that the member banks should retain their stock in the System, and still not receive anything in the way of dividends?

Mr. VANDERLIP. No, no; the member banks should retain their stock in the System, and should receive 6 percent, possibly, with the present level of interest, which is pretty liberal.

But the note issuing woud be by the Government, and the Government would hold the assets back of the note issues, the interest-bearing obligations, the earnings of the Federal Reserve Board, as reconstituted, the rediscounts and bankers' acceptances—all that profit would go to the Government.

Mr. WILLIAMS. They would not pay the banks any interest on their own securities?

Mr. VANDERLIP. No, sir.

Mr. CAVICCHIA. They would be receiving the interest, as I understand, on the stock; but at the same time, if the banks got their 6-percent interest, what, after all, would be the difference, as far as the money difference, to the Government is concerned?

Mr. VANDERLIP. The money difference would be in the profits of not more than 6 percent.

Mr. CAVICCHIA. The banks do not get that, anyway, do they?

Mr. VANDERLIP. No, sir; it is not paid over to them, but it is accumulated as surplus.

Mr. CAVICCHIA. They never have received any of that, have they?

Mr. VANDERLIP. No, sir.

The CHAIRMAN. Excepting 6 percent.

Mr. FORD. The balance went to surplus?

Mr. VANDERLIP. Yes.

Mr. WILLIAMS. Who got it?

Mr. VANDERLIP. It is there.

Mr. CROSS. Up until 1933 it was to go into the Treasury?

Mr. VANDERLIP. Yes.

Mr. CROSS. In 1933 we passed an act that it was, after that, to go into surplus; and then if, at any time, the Federal Reserve Banking System was dissolved, all that would come into the Treasury?

Mr. VANDERLIP. That is correct.

Mr. WILLIAMS. After all, it will not go to the banks?

Mr. VANDERLIP. Nor does it now come into the Government, but it would on the dissolution of the banks.

The CHAIRMAN. In other words, all of the profits of the Federal Reserve System have been coming to the Government of the United States, or the Government can take it any time it wants to and dissolve the system?

Mr. CROSS. That is why I am saying I do not see very much difference in it.

Mr. WOLCOTT. It has gone into subscriptions to the shares of stock of the Federal Deposit Insurance Corporation.

Mr. CAVICCHIA. And the Home Owners' Loan Bank.

Mr. VANDERLIP. And to buy Government bonds.

Mr. FORD. Let me see if I understand what I think Mr. Vanderlip is advocating, which is this: That the present Federal Reserve banks still do remain bankers' banks; is that right?

Mr. VANDERLIP. Yes.

Mr. FORD. But that the Federal Reserve Board would be the bank of discount for the Federal Reserve banks, with the Board reserving to itself the right of currency issue?

Mr. VANDERLIP. Yes.

Mr. FORD. Does that express your idea?

Mr. VANDERLIP. Yes; the Government would issue the currency just as it now issues the Federal Reserve currency, but it would go to the Board and not to the Federal Reserve banks.

Mr. FORD. But the Federal Reserve Board would be the only authority in the United States to issue currency?

Mr. VANDERLIP. Absolutely.

Mr. FORD. Then it would be the bank of final discount—not the Federal Reserve bank—for the member banks, the 12 banks, in the event that they wanted to rediscount any of their paper?

Mr. VANDERLIP. Yes.

Mr. FORD. In other words, you would set up a genuine monetary authority in the Federal Reserve Board, with all right of currency issue in their hands?

Mr. VANDERLIP. Yes.

Mr. FORD. Independent of any Federal Reserve bank or Federal Reserve member bank?

Mr. VANDERLIP. Yes, sir.

Mr. HOLLISTER. And also independent of administrative control?

Mr. VANDERLIP. Certainly. As to that——

Mr. HOLLISTER. Let me emphasize that. I want to make that perfectly clear. Mr. Vanderlip, as I understand it, wants the issuing power just as far from administrative control as he does even from the bankers' control.

Mr. VANDERLIP. Yes.

Mr. FORD. In that connection, let me make this observation: Since the Federal Reserve Board would be appointed by the President, as it is now, how could it be absolutely independent?

Mr. VANDERLIP. I do not think it can be absolutely independent. But may I just enlarge on that a little bit? As a council of perfection, it ought to be absolutely independent. However, if you will set up your mandate and say that the price level is the objective, it does not make any difference, but the Federal Reserve Board must expand the currency when your current prices are below that level, and they must contract the currency when the prices are above it, so you have safety against runaway inflation.

Mr. WOLCOTT. Would this enable the Federal Reserve Board, under the domination of the Executive, to use the issuing of currency for the purpose of stabilizing Government bonds, or the Government bond market?

Mr. VANDERLIP. No, sir; that is exactly what they would not do, and that is exactly what the bill you have before you does do.

Mr. WOLCOTT. My point in bringing that up is the criticism which we hear, to the effect that the authority which is set up, due to the fact that history tells us that, when we affiliate our currency with our national credit, there is chaos and destruction of the national credit and the country, itself.

Mr. VANDERLIP. You have got that written in the present bill.

Mr. CAVICCHIA. Is that why this bill has been labeled by some as the "political backed" bill, that particular provision?

Mr. VANDERLIP. Well, I never labeled it that, and so I do not know why it has been labeled that.

Mr. CAVICCHIA. Let me put it another way: If that were elminated and what you advocate were written into the bill, there would not be able to be any charge made against this bill as being a politically backed bill?

Mr. VANDERLIP. No, sir.

Mr. FORD. Is it not true that in 1912 or 1913, when this act was written—is not true that, at that time, the charge was made that the Federal Reserve Board would be a political board?

Mr. VANDERLIP. Yes.

Mr. FORD. The bankers that oppose it made that charge at that time, did they not?

Mr. VANDERLIP. Yes; and now it is proposed to give it the power to compel the member Federal Reserve banks to follow the dictates of the Board in respect to their open-market operations, and that means that they can be compelled to buy Government bonds.

Mr. CAVICCHIA. Mr. Vanderlip, would you care to tell this committee what your ideas are concerning that part of the bill which goes to the real-estate loans? As it was written originally, it called for lending on real-estate mortgages up to 75 percent of the appraised value, and the suggestion has been made, or will be made, by Governor Eccles to cut it down to 60 percent. Do you think that commercial banks ought to engage in the private mortgage field, whether on short-term mortgages or amortize mortgages?

Mr. CROSS. Let us get that correct. They were not to be rediscounted, but they could put them up as collateral and borrow on them from the Federal Reserve bank.

Mr. CAVICCHIA. Yes.

Mr. VANDERLIP. It gives permission to banks to take real-estate mortgages and, in turn, to rediscount them; and, in turn, to put them under note issues as collateral by the Federal Reserve.

If I know anything about banking at all, I know that neither demand deposits nor short-term deposits—and all term deposits are short-term deposits—should be frozen up in long-time capital uses.

Now, it is highly desirable that you should do something for the real-estate mortgage situation. That is frozen, I suspect, beyond your conception. But you cannot relieve the mortgage situation and keep the money that goes into it perfectly liquid. That is not in the nature of the thing.

Mr. Eccles has testified that there is no more objection to real-estate mortgages than to corporation bonds and foreign bonds. I would debate that a little.

A real-estate mortgage has a very narrow limit. Very few people can know what the value of it is; and therefore there can be but a narrow market for it; whereas a bond issue has the wider acquaintance of financial people, of investors, and therefore a wider market.

But neither of them should be in a bank against demand or short-term deposits. We have tried to give liquidity altogether too much and that is not in that range, and you cannot do it.

We need, the worst way, a proper mortgage bank or banking system, but the money that goes into it would not be liquid, it cannot be liquid, in the very nature of things. But we need it.

Of course, this takes me into the banking question. I believe the banks of this country have tried to do a department-store business, do everything, and they have tied up their deposits in capital purposes that are not liquid, and that was very largely the cause of our trouble.

This is getting into the banking situation, and again it is a council of perfection, but I would segregate the banks by functions.

There should be commercial banks that receive demand deposits, that pay no interest on them, and that make only self-liquidating commercial loans.

There should be investment banks, that receive deposits, upon which generous interest is paid, and their deposits are not absolutely liquid—that can be no more liquid than the purpose to which those deposits are put.

If you put them into bonds, or if you put them into stocks and bonds, the only liquidity is in finding another investor for those stocks and bonds. There is no self-liquidation quality in that loan. So the money that goes into it ought to be paid for at an interest rate that is higher, or the interest rate of the people who borrow on them ought to be higher. Loans on stocks and bonds have been at the lowest rate of all, but it is the commercial loans that ought to be at the lowest; and the loan for capital purposes, which is being loaned on stocks or bonds or the thing that has no self-liquidating quality—that loan ought to carry a higher rate of interest than a commercial loan.

Mr. Cross. Mr. Vanderlip, as I understand you, you believe in the separation of commercial and investment banking business. What disturbs me most is this: What are we going to do with what I conceive to be thousands of communities in this country, as a practical proposition, where it seems that they cannot maintain two banking systems of any kind, in the small communities?

Mr. Vanderlip. If you do this, you are going to do something that you are objecting to: You are going to permit branch banking within a restricted territory—not a Nation-wide branch banking. I never would think of that. But branch banks can run more cheaply and, on the whole, probably be better run than the small bank, that is, the banks of $10,000 and $25,000 capital. They cannot be properly run.

Mr. Cross. You mean, then, that you think the time has come when they will have to get out of business entirely?

Mr. Vanderlip. Yes.

Mr. Cross. For instance, there are 8,500—they are not all of the little kind—but there are 8,500 of them now out of the Federal Reserve System; and their day is past?

Mr. Vanderlip. In the decade following 1920, in a period of great prosperity, thousands of banks failed regularly.

Mr. Cross. Yes; and there are half as many now as there were in 1921.

Mr. Vanderlip. That was because we had a bad banking system. In some measure it was because of bad bank management, but on the whole it was the system and not the bankers.

Mr. CROSS. Do you not think we have corrected that now?

Mr. VANDERLIP. No, sir.

Mr. CROSS. You still think the system is wrong?

Mr. VANDERLIP. It will be wrong until we segregate those functions of banking and do not tie up the demand deposits in long-term capital purposes.

Mr. CROSS. What disturbs me the most is the fact that we have thousands of communities in this country that, in my judgment—that is, where that cannot possibly be done now, in my opinion.

Mr. CAVICCHIA. One more question on that line, Mr. Chairman, if you do not mind, and I will be finished. Would you say it would be feasible if we took away the right from the commercial banks to make mortgage loans and put it in some other agency, say, the Federal Home Loan Banks?

Mr. VANDERLIP. I have not given study to the mortgage-banking structure so that I am prepared to offer you a suggestion of what should be done along that line. I know in Europe there are mortgage banks that have gone through all of this depression perfectly solvent, operating and offering loans right along.

One difficulty with the mortgage situation at the present moment is that I know of no way of appraising a piece of real estate. What is appraisal value? Is it what you can sell it for? If it is, the price you sell those things for today has no relation to their worth. How can we appraise a piece of real estate with any degree of dependence is beyond me.

Mr. CAVICCHIA. One more question, and this will interest Mr. Williams, I think. In going back to that English chart as to unemployment and the price level. Is it not a fact that during this depression the price level in England has not dropped appreciably compared to the drop that we have had in this country? They cannot explain why that chart shows there was a diminution of unemployment in England with not much rise in market value. I would like to get your views and see whether I am right in that respect or not.

Mr. VANDERLIP. I think you are right.

Mr. REILLY. Mr. Vanderlip, assuming that our law insuring bank deposits should work, would not that permit passage from solvency—from liquidity to solvency—as to the condition of the bank?

Mr. VANDERLIP. Just what do you mean?

Mr. REILLY. Now, the Comptroller or the bank examiner comes into the bank and he looks at it from the liquidity standpoint. Assuming now, if the banking insurance law works, there will be no more runs on banks. Now, we are not going to have any more runs on banks and people are going to be assured as 98 percent of them now are assured, that their deposits are secured, why cannot the ban kexaminer use the solvency test and not the liquidity test?

Mr. VANDERLIP. He should, and never has——

Mr. REILLY. Well, they are coming to that. They are doing more of that now, and if we had had this insurance proposition at the time of the panic, if we had accomplished what we should have from the time the Federal Reserve Bank Law was written, we would not have had those bank failures and there would not have been that scare and a shrinkage of values.

The CHAIRMAN. This act recognizes that principle, fundamentally, that solvency is the thing about which we are chiefly concerned.

Mr. VANDERLIP. Yes.

The CHAIRMAN. And that we should not have such a run on a bank that is solvent and such a thing as a state of fear in the public's mind toward the institutions that are solvent simply because the machinery is not properly geared up to enable them to function.

Mr. VANDERLIP. How is an examiner, however, going to say whether a bank is solvent or insolvent when a considerable portion of that bank's assets are invested in real estate, which may have no market at all but have great worth?

Mr. CROSS. May I interject right there, Mr. Vanderlip, if we drew this bill as you have suggested, that we put the price level when the commodities were much higher than they are now, that would, of course, mean that the real-estate values would be much higher, and they would function in a satisfactory way, would that not then be the way to determine the value of real estate?

Mr. VANDERLIP. That would undoubtedly improve the value of real estate and improve the solvency of the banks that are not too solvent now.

Mr. SPENCE. Mr. Vanderlip, how valuable a privilege is the note-issuing privilege to banks? It has been said that many of the banks that had the right to issue currency did not issue it, did not avail themselves of that privilege.

Mr. VANDERLIP. That is true, because the national banks that had the right to issue currency had to take the chance of losing on Government bonds. The national-bank currency issue operated in just the wrong way. When there was little demand for more currency was the time it was more profitable to issue it, because they could invest in Government bonds and get a good return on Government bonds, and if they could keep their currency out, they would get interest on it, too. They do not get as much currency as they had to put into Government bonds, however. When there was more demand for currency it was unprofitable to do that. The national-bank currency operated in exactly the opposite way from what it should.

Mr. REILLY. It gave us too much money when we did not want it and not enough when we needed it?

Mr. VANDERLIP. Yes.

Mr. FORD. In discussing the mortgage situation, do you not think that the amortization principle applied to long-term mortgages somewhat alters the situation for this reason: That as long as a man is paying his interest and his amortization on that loan no bank examiner or anybody else can say that that loan is other than a solvent, sound loan, can they?

Mr. VANDERLIP. It does not mean that. I will tell you so you can see why it is not a satisfactory loan. If a depositor wants his money, it has got to come out of that kind of asset. It may be sound, but it is slow.

Mr. REILLY. They can take it down and rediscount it at the Federal Reserve bank; they could get the money for it.

Mr. FORD. If there is an emergency, it is privileged to take a group of these mortgages to the Federal Reserve Bank and discount them for 30, 60, or 90 days, or some other term, to meet the emergency, and the bank can get money on them.

Mr. VANDERLIP. Yes.

Mr. FORD. And at the end of 90 days things might go on just the same. Do you not think that adds a feature of safety to it?

Mr. VANDERLIP. I am certainly willing to testify that amortization, began the right way, adds strength to a mortgage.

Mr. FORD. Well, now, when you are figuring on a bank's capacity to pay—assuming that here is a bank with $1,000,000 in deposits, and it has got $200,000 or $300,000 or $400,000 in that kind of mortgages, and it is coming in at a rate, we will say, of 5 percent a month, plus interest, does not that put the bank in a fairly good cash position at all times with reference to those so-called "slow" loans?

Mr. VANDERLIP. Of course, it is nothing like as bad as it would have been in the past, and was in the past, for them to take such mortgages.

Mr. FORD. Do you not think this: That if in 1932, when the demand for withdrawals was in effect, if the banks had been able to take those mortgages to the Federal Reserve bank and get a reasonable amount of money on them, they could have met their demands promptly; would not the payment of cash stop the demand for money and have given the people confidence in their banking institutions that they otherwise would not have?

Mr. VANDERLIP. It undoubtedly would have tended to do that and would have saved some of those destructive things that did happen.

Mr. FORD. Then this feature that we have in there, this amortization feature, by and large you could not say it was destructive or dangerous, could you?

Mr. VANDERLIP. It is nothing compared to what I have been talking about and——

Mr. FORD. What do you think about the 100-percent reserve attitude? We have had a great many people advocate 100-percent reserve for demand deposits; what is your view of that?

Mr. VANDERLIP. I think it is silly. How is a bank going to expand its loans? It cannot do it.

Mr. REILLY. How is it going to stay in business?

Mr. VANDERLIP. Yes; it is just silly.

Mr. FORD. If I had $500,000, would it not be beter for me to go out and loan it without putting myself under the banking laws rather than to take the money and put it in a bank, and have to put up——

Mr. VANDERLIP. Yes.

Mr. FORD. $1 for every $1 I have got?

Mr. VANDERLIP. I think it would. We have got many people who are completely under the misapprehension that we could give complete liquidity to anything on earth, and you cannot do it.

Mr. FORD. We do not demand 100-percent reserves on our insurance policies, do we?

Mr. VANDERLIP. No; nor get it.

Mr. FORD. Just one more question on that reserve matter: You said that, assuming that a wild period of expansion started, you would feel, however, that the Federal Reserve Board would be justified in using the reserve principle to check a thing of that kind, would you not?

Mr. VANDERLIP. That is not just my language. If you would set up the proper mandate, that moment that the current prices went above that price level, then the Reserve Board, political or not, must begin to deflate.

Mr. FORD. And one of the ways of deflating is to demand increased reserves on the part of the banks?

Mr. VANDERLIP. That would be one of the ways, but the first way would be to sell the Government bonds they had, and to sell bankers' acceptances.

Mr. FORD. Assuming that that would not do the trick, then——

Mr. VANDERLIP. Raise the rediscount rate.

Mr. FORD. That would be true, and then, as a final resort, they could raise the reserve rate?

Mr. VANDERLIP. Yes.

Mr. FORD. The reserve requirements?

Mr. VANDERLIP. Yes; and that is an essential thing, and you have written it in this bill exactly right. I would like you to keep it there, but I would like to keep it in the proper hands.

Mr. WILLIAMS. You seem to have criticized the open-market policy set out here; in what respect would you change that, Mr. Vanderlip?

Mr. VANDERLIP. I do not critize the open-market policy. It is a perfectly proper policy to give to the body that should have exclusive power of regulating the currency.

Mr. WILLIAMS. Is it all right as written in here, this policy?

Mr. VANDERLIP. It is perfectly all right as a power, but you are not setting up any objective for the use of it.

Mr. WILLIAMS. I understand that.

Mr. VANDERLIP. It is like starting a chauffeur off with an automobile and——

Mr. WILLIAMS. I understand that. Outside of the objective which you would put in their power, so far as this open market committee is concerned, and their powers are given in there, in your judgment, is that all right?

Mr. VANDERLIP. Perfectly all right. But now, wait a minute. This measure compels the Federal Reserve banks to carry out this open-market operation, and I want the Board, itself, to carry out the open-market operations.

Mr. WILLIAMS. I understood you, a while ago, to criticize that provision which requires them to buy Government bonds?

Mr. VANDERLIP. Yes. I want an independent board to buy Government bonds, if your price level is too low and they want to increase the currency. I want that board to be compelled to sell Government bonds, or somehow reduce your currency, if the price level is too high.

Mr. FORD. Independent of the banks themselves?

Mr. VANDERLIP. Yes; and I do not want to interfere with the banks. I do not want to compel the banks to buy something they do not want.

Mr. WILLIAMS. That is in the bill as it is written?

Mr. VANDERLIP. Yes; but the power is in the wrong hands and applies to the wrong body.

Mr. WILLIAMS. That is what I had reference to, and I understood you did not approve of that part of it?

Mr. VANDERLIP. No, sir.

Mr. WILLIAMS. How would you change it? You say you would place the power in the hands of the board to buy and sell bonds?

Mr. VANDERLIP. Yes; and when they bought, they would issue currency; and when they sold, that currency would come back and be retired. That would not be compelling the Federal Reserve banks to buy and sell; the Board would be doing that, themselves, in their regulation of the value of money.

The CHAIRMAN. What you mean by that, of course, is that you would have that function discharged by the Government in its own right, separate and apart from any private banking interests?

Mr. VANDERLIP. Yes. Now, I am calling it the Federal Reserve Board, but I would really rather separate that from the Federal Reserve System, and it would be the Government.

Mr. HOLLISTER. When you say "Government", you mean a board which is really disassociated from the rest of the Government?

Mr. VANDERLIP. Disassociated from the politics of government, but it is just as much a part of the Government as the Treasury of the United States is.

Mr. HOLLISTER. But it would be operated entirely separate?

Mr. VANDERLIP. Yes.

Mr. HOLLISTER. For the good of the country at large, rather than in cooperation with the temporary policy which the rest of the Government might have?

Mr. VANDERLIP. Yes, sir; to carry out your mandate to keep the dollar stabilized in its purchasing power.

Mr. CROSS. Now, Mr. Vanderlip, I want to get down to a practical question, in view of what we can do in Congress, in the House and in the Senate. I realize that we cannot, in this Congress, separate the Federal Reserve Board, so that there would be such a body, for instance, as a monetary authority, that we talked about last year.

Now, taking this bill as it is, with the political angles in it as it is, the members or the governor of the Federal Reserve Board being appointed and really removable by the President—and that can be manipulated under this bill—with those evil features, but with a wholesale-commodity-price level set-up, do you think this bill is a big advance over what we have got now, under the law as it now stands?

Mr. VANDERLIP. If you will set up your mandate of a price level, if you will permit the Board to manage the currency, you can still call it the Federal Reserve Board; it is all right. And you can still have it somewhat subject to political influences. I do not worry about that so much, if you will set up the mandate, because then anybody who can read can see whether it is necessary to inflate or deflate, and they will know whether the Board is following out your mandate or not; and politically appointed means politically removed, and will not make much difference.

Mr. REILLY. Suppose you had had a complete monetary authority in a financial decade of this country, say about 1930, and you noticed the price index going down, do you believe that you could have pumped enough money into circulation in this country to prevent the fall of prices, and thereby cushion, to a large extent, the trials that come to the country?

Mr. VANDERLIP. Yes.

Mr. REILLY. That is your theory?

Mr. VANDERLIP. Yes.

Mr. REILLY. Then if the present Congress had at that time shot the money out and kept prices from going down, do you not think it is a different problem when you try to raise prices, after they have had a terrific crash, by the same method?

Mr. VANDERLIP. Yes; it is pretty difficult.

Mr. REILLY. And is it not a fact that nobody can tell today what effect on prices we really might have by going through that same process?

Mr. VANDERLIP. I do not believe so. I think you can tell with a great deal of accuracy and have back of your opinion the experience of England and of all of the English colonies.

The CHAIRMAN. Let me ask you this: Under the powers conferred in the bill before us, could we not achieve the result that you think is desirable, if those powers are wisely and constructively administered, and thus accomplish those results?

Mr. VANDERLIP. Well, those powers could be used in just the same way that they would have to be used if you set up a price index.

The CHAIRMAN. That is what I am talking about. Let me ask you this question: Suppose you were the Governor of the Federal Reserve Board, and we passed this law and gave you the power, you could do the job?

Mr. VANDERLIP. No; I would want to cut loose from gold. I would want a free gold market that I could operate in.

The CHAIRMAN. That is the question I meant to ask.

Mr. VANDERLIP. You do not have to make a mandate, if you can be assured that the Board is always going to operate. But wait a minute. You may feel that you could be sure under this administration, but I could imagine an administration in the future that you could not be sure of. You are leaving the thing without a tail, without telling them what it is you mean, when you say to manage the currency. You are proposing that the currency be managed, but you are not setting up the way it should be managed.

The CHAIRMAN. I think there is lots of support for this view, Mr. Vanderlip: That, after all, we are going to be left, to a large extent, to depend upon the wise administration of the law, and to accomplish that, we need a certain amount of political control or political responsibility, in order that the people of the country may know what is going on, and hold their public servants responsible for their action and for the results.

Mr. VANDERLIP. Very good. But you do want to know what direction you are driving in, whether it is north or south or east or west. Now, if you are driving towards a stabilized currency that shall have the same purchasing power throughout a generation, you want to say so, and not leave it to future Presidents and future boards.

The CHAIRMAN. I think that the people of the country, the average voters, the laymen, who know not so much about the technicalities of the law and the intricacies of finance and administration and banking, will judge results, and when the country begins to go to the bad they will vote to turn out those in control. That is what they did in 1932.

Mr. VANDERLIP. We had already gone into the ditch then. I want to keep on the road.

Mr. HOLLISTER. Is it not better to see, if we can, that we get a wise law, always with the understanding that it may not be wisely administered—and we have seen plenty of that in the past year, too—is it not better to get wise laws than to have unwise laws and hope they will be wisely administered?

Mr. VANDERLIP. What is Congress here for?

Mr. REILLY. Is it not a fact that there is much difference of opinion and disagreement between financiers and students of commercial banking, as to the soundness of your views?

Mr. VANDERLIP. Yes; there is a marked difference of opinion and a high degree of ignorance. And I will tell you another thing: The bankers are not speaking their minds. The bankers are very low in their minds. They have got an inferiority complex at the present. More than 6,000 of them have sold preferred stock to the Government, and they are not shouting opposition. They are in somewhat of a reign of terror and they are keeping quiet.

The CHAIRMAN. We cannot do a much worse job than they did.

Mr. REILLY. I asked that question, because if the men who know something about banking and finance would come here, and talk to us about it, we could do something. But they are just as opposite as two poles and——

Mr. VANDERLIP. I would like to argue the case with some of them.

Mr. HOLLISTER. Is that not a large indication of the fact that we ought to study this measure, without going off half-cocked?

(Here followed discussion off the record.)

The CHAIRMAN. If the lessons we have had and the experience that we have had together in these recent years, and the study that has been given by Congress to this legislation, is not sufficient to enable us to act intelligently, the picture is not very encouraging.

Mr. VANDERLIP. It seems to me that the President himself has named the objective. He wants a currency that will have the same purchasing and debt-paying powers throughout. If he felt that, and I must believe he did, because I heard him say it over the radio and he convinced me that he meant it; why do you not enact that into the law?

Mr. REILLY. This is supposed to be his bill, an administration bill.

(Here followed discussion off the record.)

Mr. FORD. Would you give us a definition of asset currency? We have heard a great deal about it.

Mr. VANDERLIP. I do not know what it is.

Mr. FORD. Here is something I worked out in my mind: I take $1,000 to the bank and put it in there, and they loan that $1,000 to somebody on a mortgage or note or bond or something, and then it is an asset and——

Mr. VANDERLIP. Then it is asset currency; and if you want your money back, where are you going to get it?

Mr. FORD. If they take that note to the Federal Reserve bank and get it discounted, when I want my money, and give me the money, is not that asset currency?

Mr. VANDERLIP. No; that would be bad currency, and I used "asset currency"——

Mr. SPENCE. You say that the present machinery in this bill, the open-market operations and the regulation of the discount rates, and the regulation of the reserves, would not be sufficient to establish a price level, unless we cut away from gold?

Mr. VANDERLIP. No, sir.

Mr. SPENCE. How would you practically do that?

Mr. VANDERLIP. You have practically done that. You call yourself on the gold standard, but you are not remotely on the gold standard. Nobody can retain their money in gold. It is a crime to hold gold, and you cannot ship gold unless, under certain circumstances, you can ship it to one of these very few gold-standard countries. That is not on gold. That is not a step, it is just edging a little to get completely off.

Mr. SPENCE. What further step would you take to cut away from gold? You said, in addition to this, we would have to get away from gold, and I want to know what steps we should take.

Mr. VANDERLIP. It would take legislation. You have authorized the President to cut the gold content of the dollar still further, but you have not authorized him to go off of gold altogether, to have no attachment of the currency to gold.

Mr. SPENCE. Well, if we pass this bill and authorize the Federal Reserve Board to issue currency——

Mr. VANDERLIP. You can say that that currency is not redeemable in gold. A single line will do it all.

Mr. CROSS. I am going to ask you the question that we have had mentioned here, Mr. Vanderlip, by the men who have been before us, who have studied the question, and it is this: That the amount of pocket money, plus the check money, multiplied by three, will equal the national income. In other words, suppose you——

Mr. VANDERLIP. Well, it would much more than equal it, I should think.

Mr. CROSS. They claim it will stay at that ratio. Suppose you take the check money and your pocketbook money, or currency, and it amounts to $25,000,000,000, then the national income would be $75,000,000,000, would it not?

Mr. VANDERLIP. It is about $44,000,000,000.

Mr. CROSS. But the check money has dropped down tremendously. I do not know what it is now, but they claim that, through the years, if you will take the amount of currency, plus the check money, and multiply it by three, it will give you for each year the national income.

Mr. WILLIAMS. That is, there is always a definite ratio between the amount of money and the national income?

Mr. VANDERLIP. If that is true, I do not know anything about it, and it is not true today.

Mr. HOLLISTER. And they argue the other way, too.

The CHAIRMAN. All right, gentlemen, if there are no more questions for Mr. Vanderlip.

We thank you, Mr. Vanderlip. Your statement is certainly able, instructive, and helpful to the committee and we thank you.

Mr. VANDERLIP. I thank you for your courtesy and your time.

The CHAIRMAN. Gentlemen, we have with us Mr. J. H. Rand, Jr., of Remington-Rand, and chairman of the Committee for the Nation, whom we shall be glad to hear.

STATEMENT OF J. H. RAND, JR.

Mr. RAND. My name is J. H. Rand, Jr., chairman of the board of Remington-Rand, Inc., 205 East Forty-second Street, New York City.

Mr. Chairman and gentlemen, I would like to give you the impressions and reactions of manufacturers, as I see them, to this bill.

In the main, I subscribe to the changes that were suggested by the American Bankers Association's special committee, and I think that the direction which this legislation is taking is very ominous as to the future course of events in this country, as to reemployment.

When I say "direction" I have reference to certain suggestions that were also made by the Governor of the Federal Reserve Board, Governor Eccles.

Now, the manufacturers are looking to you Members of Congress, as they are the ones to reemploy the 8,000,000 employable unemployed, and naturally you will be interested in knowing what the reactions of the manufacturers are to this legislation.

The most important thing that undermined the ability of the manufacturers to continue employment in the last 4 years was the vicious drop in the price level. I can tell you, authoritatively, that there is one thing, and the only one thing that I know of, in which two Presidents of the United States agree, and that is, that the vicious, unprecedented drop in the values of everything, and in the commodity price level, undermined the solvency of individuals and banks and caused wide-spread distress throughout the country. It is that drop in commodity prices that has made it impossible for a great many manufacturers and merchants to operate at a respectable profit. In fact, it has caused corporations like my own to go on and lose millions and millions of dollars in attempting to keep people employed, who really are deserving of continued employment.

In addition, the drop in commodity prices also removed a lot of buyers from the market, removed the buying power of a large class of buyers. President Roosevelt referred to that in one of his public addresses, when he stated that the 50,000,000 people who are basic producers, either on the farm, or in rural communities and directly dependent upon the farms, have had their buying power curtailed by the drop in prices which the basic producers receive for their products, and that it is necessary for us to correct this disparity.

I can tell you the way that I figure, as a manufacturer, right now: If the price level of the basic commodities, largely farm products—products of the farm, the forest and the mine—were raised to the point that would enable the men who do the work on the farms to buy as many shoes and stockings, radios, gasoline, tires, and automobiles as before; if they could again buy as much, or exchange their products for as many manufactured commodities as in the period of 1921 to 1929, or say 1926—and certainly the basic producers are entitled to a square deal—then you would have today, with that relationship reestablished, purchasing power or income of the basic producers of $6,000,000,000 per year more than they have today, or had last year. And it happens that the $6,000,000,000 which the basic producers could spend with the manufacturers of shoes and stockings and gasoline and radios and whatnot would amount to a sum sufficient to pay to the 6,000,000 at present unemployed the average wage of $20 per week that is now paid in industry.

And you are never going to get those unemployed back to work until you give back to us manufacturers the buying power of the 50,000,000 people who are the basic producers, and who have been denied their normal income during the past 4 or 5 years.

Mr. REILLY. What are you going to do with the 20,000,000 people who now live on the borderline of existence, under present prices? I am getting hundreds of letters every single month from my constituents, protesting as to what they claim are outrageous and unjustifiable increases in the cost of living.

Mr. RAND. You will get those objections to increases in the cost of living whenever there is a movement of as much as 2 percent in the cost of living. But bear in mind that for every one of those that object there are a hundred who realize that they are so much better off, in proportion to what they were, that they would not go back to the lower prices and unemployment they used to have.

We can have everything reduced in this country so nothing could cost over $1, yet nobody would be employed.

The CHAIRMAN. In my section of the country conditions are much better because of the rise in the price of farm products.

Mr. RAND. That is the reaction of the manufacturers. Here is another reaction: Manufacturers pick up the Constitution and read it occasionally, and in it they find that Congress, among other things, shall coin money and regulate the value of money. How can you regulate the value of anything except by regulating its purchasing power or its exchange value?

In order for the Congress to follow the mandate of the Constitution, the Congress must regulate the price of the basic commodity or the price of goods, the average price of goods, because therein is expressed the value of money and by nothing else. It is not expressed in air, or anything else but goods.

A manufacturer has a right to know, in these disturbed times, when currency is gyrating and when the air is full of rumors and uncertainty; they have a right to ask, "Where do we go from here and what is our dollar going to be worth 6 months from now or a year from now?

For instance, I may want to build a plant and put in some modern machinery and stock up on goods, in order to take care of what I think is going to happen, if the administration goes through with a constructive recovery program. Do I do it? The average man says, "No; I will not do it, because I don't know what the value of the dollar is going to be 6 months from today, or a year from today." Yet the Constitution says that the Congress shall fix that value. Therefore, the manufacturers look to you to fix the objective toward which he can operate, if you want him to reemploy people and want him to take the gamble. He is the one who is going to lose his shirt, if he does not make the right decision. You have a right and it is a constitutional mandate, to tell what you are going to do with the value of the money. In other words, fix it. And I take that to mean it is perfectly legitimate for Congress to fix it for at least a year; they can always change their minds.

I submit that one of the underlying causes of trouble today is that uncertainty about what the dollar is going to be worth.

Another thing is this: Banks will not loan money unless they have adequate security. In a period where we have been going through deflation, we have deflated not only bank assets but we have also deflated the unused collateral assets of the country. In other words, the asset value of this country today is as far below the asset value that existed in 1926 as the price level is below the price level of 1926.

When you restore the asset value of collateral of the United States, you will also restore the loaning power and loaning activities of the banks.

I happen to sit on the directorate of a couple of banks, and I know there is a scarcity of eligible, satisfactory collateral today; a scarcity of it. But you raise the price level and see how much of it you will make eligible and make desirable collateral.

Mr. CROSS. The idea is that we should set out in this bill a price level to go to, as a goal to which the Board should drive; is that your idea?

Mr. RAND. Absolutely. I have three or four recommendations. I subscribe 100 percent to what I heard Mr. Vanderlip testify to. I did not know what he was going to say before he testified, but I can go a long way on exactly what he testified to; and I will reiterate, if you will permit me, one or two things. I believe that Congress is making no mistake in drawing the line between the Federal Reserve Board and the regional banks.

And let no one raise that line so far as to permit interference by the Federal Reserve Board with the function of extending private credit, which can best be handled without any political interference of any kind.

Take over and place on the Federal Reserve Board's side of the fence the power of note issue. It will have, under the provisions of this bill, the power of regulating the rediscount rate, conducting the open-market operations, and fixing the ratio of reserves which the banks must carry. If you are going to give it a free hand, why divide up the functions of control and leave some in the Treasury and some in the Federal Reserve Board and some in the regional banks?

If you are going to have a body that is charged with the responsibility of carrying out your mandate, you should concentrate that responsibility in the hands of a definite board; and I suggest that the best way to do that is to give these six functions to the Federal Reserve Board, including those three that they do not have today, which are the currency-issuing privilege, and control over the price of gold, and control over the price of silver.

I differ with Mr. Vanderlip that the administration does not, as here stated, have the authority to go off the gold standard today. The Treasury does, in my opinion, have the authority to go off of gold tomorrow, and should go off tomorrow, in order to permit the proper execution of the program for carrying out your mandate, or the mandate which should be fixed in this bill. All that is necessary is for the Treasury to say, beginning tomorrow, we do not choose to buy any further gold at $35 an ounce except from domestic producers, and that is newly mined gold, the same as they are doing with silver.

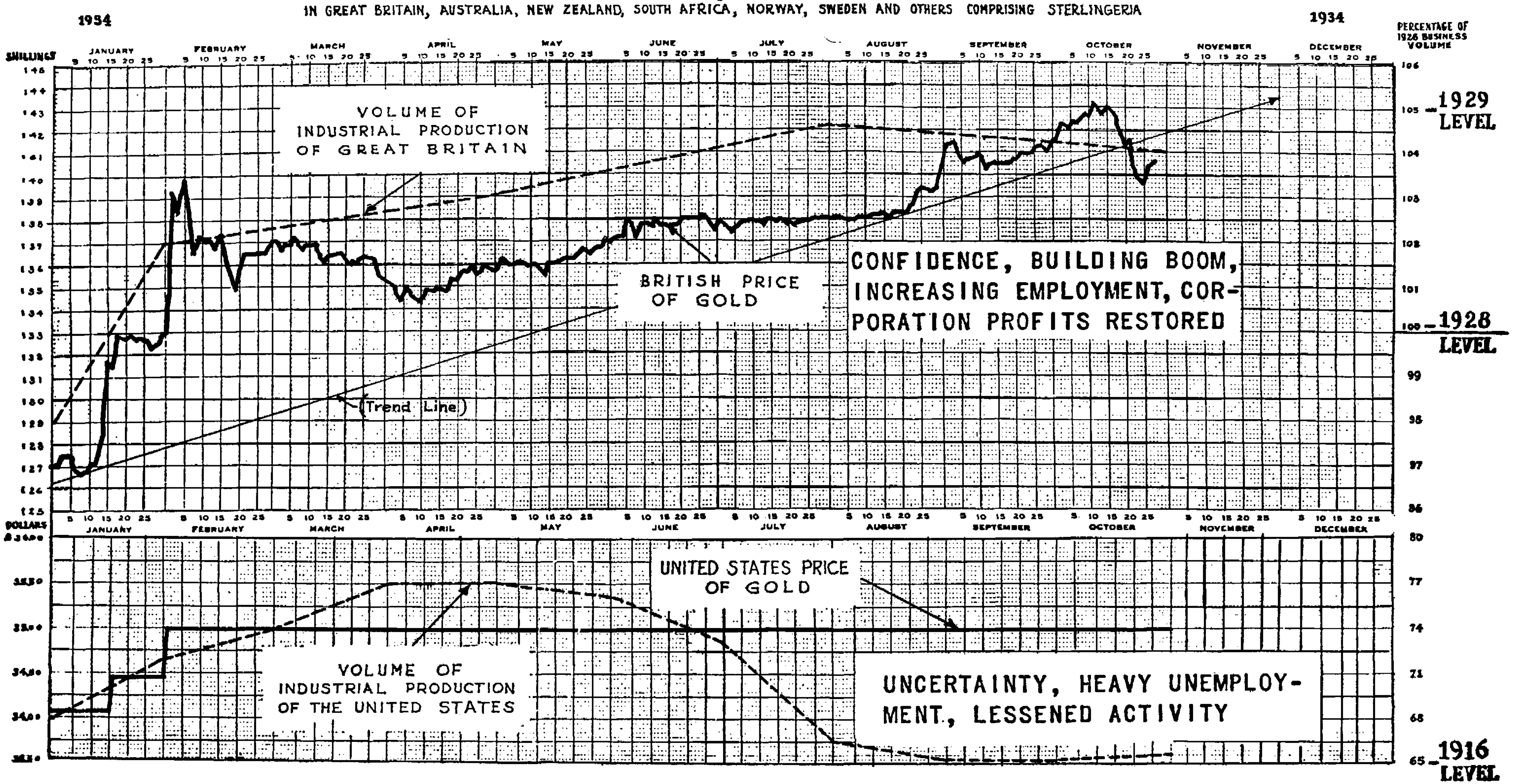
We have no fixed price today at which we will sell anything except gold, or at which we will buy anything, except gold. Let us do the same with gold, and say we do not wish to hoard gold and thereby increase the abnormal demand for gold. We should discontinue buying gold at $35 an ounce from all comers; and if the people of the United States have gold to sell, they should be allowed to sell it in an open market in New York or Washington, or any other market. as is done in London.

(America Must Choose)

WHAT GREAT BRITAIN HAS DONE TO THE PRICE OF GOLD DURING THE PAST 9½ MONTHS

A PERIOD OF GREAT PROSPERITY, APPROXIMATING THAT OF 1929

IN GREAT BRITAIN, AUSTRALIA, NEW ZEALAND, SOUTH AFRICA, NORWAY, SWEDEN AND OTHERS COMPRISING STERLINGERIA



WHAT THE UNITED STATES HAS DONE TO ITS PRICE OF GOLD DURING THE PAST 9½ MONTHS

A PERIOD OF LESSENED BUSINESS ACTIVITY, BELOW 1933

COMMITTEE FOR THE NATION
205 EAST 42ND STREET N. Y. C.

131886—35. (Face p. 127.)

(OVER)

This revised Federal Reserve Board could be used in operating an open gold market much as the Bank of England is, through its treasury committee, which is in constant contact, not by law but in actual practice, with Neville Chamberlain, the Chancellor of the Exchequer, in London. Every morning this committee will meet, consult the Chancellor of the Exchequer, determine at what price it will buy gold or whether it will sell gold. The Bank of England operates in the open gold market under the control of three men, and those three men announce the price the Bank of England will pay for gold. The bank being the largest factor in the open market, naturally it can control the British price of gold about as easily as you could control the price of any commodity.

Mr. CROSS. Do they vary their price much?

Mr. RAND. Let me surprise you. Nearly all of the quotations in the United States in our daily newspapers are in terms of dollars. Occasionally you will see it in terms of pounds, but when they convert the pounds into dollars, you get about the same price we have in this country of $34.96 or $35 per ounce. What has happened during the past year has been that the price of gold, in terms of English pounds and shillings, has gone from 127 shillings in January 1934, to around 149 shillings per ounce within the last 3 weeks. It is now fluctuating between 143 and 145 shillings, against the old parity price of 85 shillings per ounce.

(See chart offered by Mr. Rand for the record.)

Mr. REILLY. What does that mean?

Mr. RAND. That means that Great Britain is using the fluctuating price of gold to control the price level and to endeavor to influence foreign exchange.

Mr. REILLY. But it is always going up?

Mr. RAND. No; they have had a drop of as much as 10 percent inside of 3 months. The general trend is upward, and I believe the general belief among British statesmen is that Great Britain must have now a little higher level of commodity prices for their own welfare.

Now, why do we recommend the stable price level or restoring our prices to 1926?

The CHAIRMAN. Let me ask you right here, has Great Britain obtained a stable price level during the time of this operation?

Mr. RAND. Absolutely. The wholesale prices in Great Britain have not varied more than 7 percent in the past 3 years.

The CHAIRMAN. And variations have been between the pound and gold——

Mr. RAND (interposing). The dollar.

The CHAIRMAN (continuing). And gold?

Mr. RAND. Yes.

Mr. REILLY. In the last 2 years, our price level has gone up, has it not?

Mr. RAND. It certainly has.

Mr. REILLY. Is not that advisable under your theory?

Mr. RAND. Absolutely. The only mistake we made, from my standpoint, is that we returned to the gold standard too soon. In other words, we returned to a hard-and-fast fixed price of gold before we should have. The United States cannot tie to anything in protecting the interests of its people and a productive program, cannot tie to anything as unstable as gold.

The great instability of gold is strikingly shown in a tabulation of the maximum variations in the value of principle basic commodities in relation to each other and in their relation to gold. It is one of the research studies carried out in the Committee for the Nation, of which I am chairman. It shows that gold has been, since 1920, far more unstable than wheat, or cotton, or pig iron, or lead, corn, hogs, copper, etc. Exchanged for one another, such basic commodities show little variation in value; but when exchanged for gold, or money equivalent to a fixed weight of gold, they show that it was gold, not commodities, that changed most violently. I offer the table for your record.

To the dollar to a fixed weight of gold while nearly all of the rest of the world is off of the gold standard, puts our price level under the influence of those who are managing gold outside of this country.

(Table referred to is as follows:)

Maximum percentage variation in the value of commodities in terms of each other and of gold, 1920–34

	Wheat	Cotton	Pig iron	Lead	Corn	Hogs	Copper
	Percent	*Percent*	*Percent*	*Percent*	*Percent*	*Percent*	*Percent*
Gold	395	456	327	265	530	377	278
Wheat	....	36	91	86	72	68	53
Cotton	163	....	125	106	85	138	82
Pig iron	93	120	....	108	93	163	180
Lead	84	104	116	....	134	69	62
Corn	74	71	200	138	....	....	75
Hogs	69	88	148	72	109	....	56
Copper	105	85	171	59	68	57	....

Mr. Cavicchia. Not even the $2,000,000,000 revolving fund we have would help the situation?

Mr. Rand. The $2,000,000,000 revolving fund can never be used for stabilization without taking the tremendous chance which no Administration would be justified in taking. That $2,000,000,000 of gold profit might better be used in retiring Government bonds tomorrow than to be kept sterilized in the vaults of the Treasury, while we are having to borrow money and pay good interest on it.

Mr. Reilly. Is it not a fact that, in the last few years, England's monetary policy consisted in keeping prices down?

Mr. Rand. That is a fact. That seems to be apparent from what appears on the surface that the desire of Great Britain is——

Mr. Reilly. To keep a cheap pound?

Mr. Rand. To have a cheap pound; and it is publicly stated by statesmen, such as Neville Chamberlain, that there is objection to allowing the pound to go too high; and the newspapers in London are full of printed criticism whenever the pound goes up in terms of dollars, saying it is putting Great Britain and the manufacturers of London, Lancashire, and Liverpool at a tremendous disadvantage.

Mr. Reilly. The lower the pound the more advantage they have?

Mr. Rand. Yes. Now, I do not appeal to you gentlemen from the standpoint of the export business so much as I do from the standpoint of bringing to your attention the necessity, during the next 6 months, for a plan of restoring employment in this country. I do not care what happens to the foreign exchanges so long as we are reducing our unemployment in this country even by policies that are detrimental to our export interests. I say our first duty is to restore employment in this country and forget about those unemployed in China and South America and the rest of the world, until we have gotten our own house in order.

Mr. REILLY. Then you are not trying to help us, are you?

Mr. RAND. Then later I would give consideration to the foreign exchange policy.

Mr. CAVICCHIA. Mr. Rand, when you raise our commodity prices, will that ever be any benefit to us unless we know what the value of the dollar is going to be for the next 6 months or next year? Am I correct in that?

Mr. RAND. The raising of prices will not be beneficial, unless we know that?

Mr. CAVICCHIA. Yes.

Mr. RAND. They will be beneficial, but they will not result in as rapid reemployment as it will if you will let the people of the country in on your objective.

Mr. CAVICCHIA. I will put the question another way: There cannot be any appreciable advance in commerce, industry, or in business, unless we do know what the value of the dollar is going to be; is that correct?

Mr. RAND. I would not subscribe to that, that it would not be appreciable. There would be the tremendous advance that we had in 1933 by simply raising your price level, and on this rising price level everybody made a profit.

The history of the world proves that no consistent period of prosperity has transpired which has not been accompanied by a gradual lifting of the general level of commodity prices. When you have a constant decline of commodity prices, you have deflation and unprofitable business. The history of the Dark Ages can be written in one word, "Deflation."

Mr. FORD. A rising price level is a bad thing for an export nation, is it not?

Mr. RAND. A rising price level is bad for an export nation?

Mr. FORD. Yes.

Mr. RAND. It depends on whether your prices are rising in terms of dollars or of gold.

Mr. FORD. I realize that, but, for instance, England has kept her prices at about normal for the past 2 years, for the purpose of enabling her to export a large volume of goods, because she has to import a large volume, and she has to have something to equalize that in order to live. England is an importing nation primarily, and it seems to me that her problem would not be altogether parallel with ours.

Mr. RAND. Might I make a comment on that? I hope you will understand this, because I consider it one of the most important factors in the world situation today. Our company does business in every civilized country in this world, and I might say that all through this depression in our foreign business, which is about 25 percent of our total, we have not operated at a loss in any 6 months' period. So we had to know something about conditions in other countries. Here is something that impresses me very strongly:

In Great Britain or the British Empire you have two definite sections or regions. You have the industrial British island, known as "Great Britain", and you have the agricultural regions of Australia, New Zealand, South Africa, to which you might say that you have added the "sterling area", including Brazil and Argentina. What has been done? If you analyze what has been done by the British—and they are smart in their international finance—they are raising the currency prices of gold in all of the agricultural countries of the "sterling area" in order that those countries might have exchange advantage over all of their competitors. The fact is that they have, and it has resulted to our disadvantage, because the United States raised its price of gold only as high as Great Britain did, namely, 69 percent.

We did not raise our price of gold to what it is in the principal agricultural countries of "sterling area." It is this differential in the price of gold which caused the agricultural West and South of this country to be at a disadvantage in the sale of their products against these higher-priced gold countries of the British Empire.

We would have a similar situation here if we could draw a borderline, let us say, along the Mason and Dixon Line and up the Mississippi River, and take the financial and industrial section of the country and say, "We are going to keep the price of gold for that part of our country, corresponding to financial and industrial England, 69 percent above, but for the West and South we are going to raise the price of gold to 103 percent above what it used to be." Then you would have prosperity in our farming and mining sections, and no disadvantage between our own agricultural and raw-material-producing sections and the corresponding portions of the British Empire.

Mr. Cross. For instance, the pound sterling in London is $4.80, and in Australia $3.84; does that reflect what you said?

Mr. Rand. For years—and I do not know how many years, but for many, many years—the Australian pound exchanged pound for pound with the British pound. When Australia went off of gold and raised its price of gold, I think in two quick jumps, they immediately changed the relationship by arranging with the financial authorities in Great Britain that 4 British pounds bought 5 Australian pounds, instead of pound for pound. In other words they automatically cheapened their pound, in terms of the British pound, by 25 percent, and that gave Australia a tremendous advantage in the sale of her surplus agriculture products.

And I might say that Australia at that time was seething in political unrest, and perhaps next to Russia, was the most socialistic country in the world. As soon as they did this and agricultural prices went up, wool and wheat and what not, and business activity was resumed, all of the people who had been outspoken against the Government turned capitalistic overnight, and the last radical that they chased out of the country landed in San Francisco and started a strike out there for us!

What happened over there was they accomplished something they did not expect. All of their people turned capitalistic and were believers in private property, and as Reginald McKenna has said, Australia has led the world out of the depression.

Mr. Ford. Instead of $35, suppose we put the price of gold at $45, what will happen?

Mr. Rand. If you put the price to $45 you would experience, within 3 months, a repetition of what happened in the spring and early summer of 1933, when this country had the sharpest upturn of business activity that it ever had and the sharpest reduction in unemployment that any country ever experienced during this depression. That is my opinion of what would happen.

I believe, on top of that, that if you would tell the manufacturer that you were going to stabilize at a definite level the wholesale prices of commodities, so they would be sure that commodities after having experienced an advance were not going to go over the precipice and collapse again, you would have the greatest period of prosperity this country has ever seen.

Mr FORD. Then you are advocating two measures: The reduction of the gold content and a stabilization of prices at whatever figure it would take to bring that?

Mr. RAND. I am advocating that the Federal Reserve Board should be given the right to operate in gold and/or silver in such open markets as may exist and——

Mr. CROSS. At whatever price they want to fix?

Mr. RAND. They could go in and buy or sell them, and let the price go up or down; and they being the largest factor in the market, could put the price up or down. The United States Treasury would not do it, but I think the Federal Reserve Board should do it.

Mr. CROSS. Do you not think we ought to tie ourselves to a fixed price?

Mr. RAND. No; the day of fixed price is over, and you will not see, in your life, another international definite fixed price of gold.

You may see it operated through an international clearing house of some kind, but I do not think you will ever see the free flow of large quantities of gold, that are capable of doing as much damage as an invading army can do to a country.

Mr. REILLY. What will happen to the country if all of the nations go off of the gold standard.

Mr. RAND. That will be the real beginning of recovery. The whole world, as such, will attain its recovery from the day the gold bloc goes off of gold; and from information coming to me, I would not be a bit surprised if that happened within the next 6 months.

Mr. WILLIAMS. You are going to make the commodity index of certain commodities. What commodities would you put in there as the basis upon which you would fix the level to which we should strive?

Mr. RAND. I would take the United States Bureau of Labor wholesale average of 784 commodities, or whatever it is.

Mr. WILLIAMS. You would take the Labor Bureau's statistics?

Mr. RAND. I would take that for the purpose of stabilization. Why? Because it has got more of the elements of the cost of living than the purely basic has, but I would operate on the basic commodities.

Mr. WILLIAMS. What do you mean by that?

Mr. RAND. What I mean is this: That I would attempt to establish prices of the staple commodities, the basic commodities, which are about 35, and the prices of which are fixed in the markets of the world, and I would raise those until the United States Bureau of Labor index reached the average of 1921 to 1929, or say the 1926 level.

Mr. WILLIAMS. After you had established your level and the general commodity price levels, could you maintain all of the commodities at that level?

Mr. RAND. Not all of the commodities. You will never be able to counteract the law of supply and demand. That may be effective temporarily, but those influences will be more or less temporary.

Mr. WILLIAMS. Could you stabilize the basic commodities?

Mr. RAND. They are what I would attempt to stabilize, but at the level where the United States Bureau's wholesale price index stood in 1926. That does not mean that the basic commodities would be where they were in 1926; they might be above or below 1926. As a matter of fact, I think they would be above 1926.

Mr. WILLIAMS. You would try to raise the basic commodity prices to the general price level of 1926?

Mr. RAND. Until the general price level reaches 1926, that is right.

Mr. REILLY. When you raise the price of cotton in Texas, the people in Texas continue to produce more cotton.

Mr. RAND. In my opinion, if we take monetary action raising the price level, and announce a definite objective, so that business——

Mr. REILLY. Suppose you announce the objective, what will happen?

Mr. RAND. You will have so much reemployment, so much increase in the consumption of cotton, that with the set-back the South has had in the curtailment of cotton and the discontinuance of production, the South will not be able to produce the cotton we will need in this country.

Mr. CROSS. He keeps on harping on one commodity, but that is the truth about a lot of these fellows and——

Mr. RAND. We have got to forget individual commodities.

Mr. CROSS. Any commodity can go away up or away down, but when you take the entire volume, it will stay on an even keel.

The CHAIRMAN. I want to say right here, about cotton and everything else, and I want to register this opinion of my own—I do not believe we ever had an overproduction.

Mr. RAND. Never.

The CHAIRMAN. The people who produce our cotton crop have cotton clothes to make them comfortable.

Mr. CROSS. For a number of years, we produced in excess of 15,-000,000 bales of American cotton, but the trouble is, we cannot buy it. That is the reason you do not use cotton. The consuming power is here, but they have not got the wherewithal to buy it, but when you get people back to work, they may have.

Mr. RAND. Let me make a point about how people react to that old. well-known law of supply and demand. All orthodox economists had the feeling that the bankers of the United States should go on record against interference with the law of supply and demand; that you should not try to boost up the price of cotton and hold it there, or wheat, or other commodities, but let the law of supply and demand operate freely. That is exactly what I am recommending that you do with the price of gold in the free, open market; and if that price of gold, according to the law of supply and demand, should be higher than it is now, or lower, that is where it should be allowed to go and that is where it will go.

My personal opinion is that the demand will put the price of gold up for the time being, and probably put it up to the same extent that Brazil and the Argentine and all of these agricultural members of the British Empire and the "sterling area" have raised their price of gold, and when it does, they will have no longer an advantage over our agricultural producers, and our agricultural producers will be able to buy $6,000,000,000 more from our American manufacturers, and the recovery problem will be solved.

The CHAIRMAN. What is the position of the manufacturers with reference to this legislation? They are against this legislation, are they not?

Mr. RAND. The manufacturers are not against this legislation.

The CHAIRMAN. The American Chamber of Commerce and the New York Chamber of Commerce are against it, are they not?

Mr. RAND. No; the New York Chamber of Commerce is made up of bankers, not manufacturers.

The CHAIRMAN. How about the American Association of Manufacturers?

Mr. RAND. I can tell you what the opinion of 3,000 manufacturers is as to the price level, but I cannot speak for the New York Chamber of Commerce.

Mr. HOLLISTER. Which legislation are we talking about?

The CHAIRMAN. All of it. They are opposed to this particular proposition as I understand it.

Mr. RAND. While Mr. Vanderlip was testifying someone asked a question as to what we would do with the Federal Reserve Board if you gave them a mandate and they failed to perform according to the mandate, and he said, "Impeach them." Somebody said, "Would you impeach the Supreme Court if they failed to issue the decrees?"

The difference between the two impressed me very forcibly, and I would like to give it to you. The Supreme Court is charged with the duty of interpreting laws. Laws are subject to various interpretations, as we have found many times before. Sometimes they are interpreted by one court one way and another court another way, but we are bound to accept the decisions of the Supreme Court when they interpret.

A price level, however, mandated by Congress, is open to only one interpretation, and that is, that level; in other words, it is not subject to ambiguous interpretation.

Mr. CROSS. If the Supreme Court were to ignore the law, they could be impeached.

Mr. RAND. But you could tell whether the Federal Reserve Board had regulated the price level according to the mandate that you had laid down.

Mr. REILLY. Is it not a fact that we were in this panic largely because, in 1929, we began to produce an overabundance of manufactured goods?

Mr. RAND. No; there has never been any overproduction of any kind. I will tell you what happened in 1929: It was the absence of a clause in the law, the Federal Reserve Act, requiring the Federal Reserve Board to regulate the reserves required of banks behind their deposits. Had that clause been in the Federal Reserve Act, the Federal Reserve could have stepped in at that time and have raised the reserve requirements of the banks and stopped securities from going to heights unknown. In other words, long before security prices had gotten any higher than they were in 1927, the Federal Reserve Board could have stopped it and avoided the collapse. That is what you are doing in this bill that you are passing on, giving Governor Eccles and the administration a clause which permits them to regulate the cash reserves required of banks behind deposits.

Mr. BROWN of Michigan. That is an afterview, is it not? You are not certain that the Federal Reserve authorities, had they had that power in 1927, would have had the good judgment and sense to have ordered that stoppage?

Mr. RAND. No; nobody can be sure. However, they did not have the authority at that time.

Mr. CROSS. If they did have the authority they could have done it?

Mr. BROWN of Michigan. We are not sure, if we give them the authority now, that they will exercise it in that way. What I am pointing out now is, your view is simply an afterview of the thing, but we know you are right, but at that time we do not know whether you would have been right or not.

Mr. RAND. The chances are that it would have been used. We are all aware of the extent of the situation.

Mr. WILLIAMS. Would you change the manner in which this Federal Reserve Board is set up, the provisions of this bill?

Mr. RAND. From the standpoint of political expediency; no.

Mr. HOLLISTER. From the standpoint of wild legislation, how about it?

Mr. RAND. Wild legislation that is never enacted is no legislation.

Mr. CROSS. It might be that, in some other Congress you could do it, but you could not do it now.

Mr. RAND. I would like to reiterate what Mr. Vanderlip pointed out, that I consider to be the most important cue that this committee, or Congress, can possibly have, comes directly from the President in the form of two things: First, on several occasions, he has stated that the price level in this country is not yet at a high enough level, a high enough point that the debtors and creditors are in balance, or that the debtors can pay the creditors without an undue burden of debts; second, that the dollar that America seeks—and I am told this is the dollar that we will have—must have substantially the same purchasing power and debt-paying power " as the dollar which we hope to attain in the near future."

Two years have gone by, or a year and a half has gone by, and we are approaching the maturity of " the near future." Therefore, now that we have this subject under consideration and the whole country is looking to the administration and to Congress to give it some definite information on the future of the dollar, they expect nothing else than what they have heard the President say, personally, over the radio.

Mr. REILLY. The administration has announced there will be no change in the dollar; the Secretary of the Treasury announced that.

Mr. RAND. The President's statement takes precedence over all others.

Mr. WILLIAMS. How much are we short in the price level now, in your judgment?

Mr. RAND. The basic commodities will have to go up approximately 20 percent.

The CHAIRMAN. Let me ask you a question. Suppose we keep up the advance with our move toward a high level, at the rate we are going——

Mr. RAND. Mr. Chairman, during the past year, since we anchored to a fixed price for gold at $35 an ounce, we have not made progress.

The CHAIRMAN. We have made some progress in the last year, have we not?

Mr. RAND. Not noticeable progress; nothing to compare with the progress we made in the preceding year, either in reducing unemployment or restoring solvency.

The CHAIRMAN. Suppose we use the power further and raise the price of gold; what effect would that have?

Mr. RAND. If we raise the price of gold through the operations of the Federal Reserve Board, under a mandate from Congress, you will have an advance in the price level and will increase the purchasing power in the hands of the basic producers of this country, which includes all of the farmers, immediately and with mathematical precision.

Mr. CROSS. In other words, we ought to give the Federal Reserve the right to fix the price of gold as they see fit. and instead of fixing the statutory price like the President has, of $35 an ounce, let that Board say what the price of gold shall be from time to time, just like they do in England now, and you were telling about how they functioned.

Mr. RAND. Absolutely the same as the English do.

Mr. CAVICCHIA. And let this country anchor to a certain value?

Mr. RAND. We want this American dollar of ours to have one certain, stable value, so one can rely on its value, and you can never get that so long as it is in terms of a piece of gum-rubber gold.

Mr. CAVICCHIA. How are you going to stabilize it there?

Mr. CROSS. You tie to a piece of gold and it stretches. Of course, you still hold $35 an ounce, but gold goes up and down and fluctuates in value.

Mr. RAND. I would like to read to you what was said last week by the head of the largest bank in the world, Mr. Reginald McKenna, former Chancellor of the British Exchequer. It is contained in a special wireless dispatch from London to the New York Times:

> The gold value of currency is now coming to be regarded as of secondary importance, and its purchasing power over goods as primary. It may be, therefore, that suppression of the gold clause in American obligations will lead to attempts to safeguard the position of both debtors and creditors by the inclusion in debt contracts of a clause establishing a relationship between money and goods. This may come to form a firmer basis not only for internal but for international obligations, through which fluctuations in the commodity value of money entail such appalling consequences as have been obvious in recent years.
>
> If this development takes place, the world will have cause to bless the names of the five judges who found the means of breaking the shackles by which long custom has bound the dollar to gold and had threatened to prevent its playing its full part in the reestablishment and maintenance of economic health.

Mr. REILLY. Is that the advice that you are giving to us?

Mr. RAND. Reginald McKenna is a banker who differs from most of the bankers in Great Britain and is not regarded as being of the same degree of orthodoxy as is in the make-up of other bankers, and in that respect I compare him with Frank Vanderlip, who is not bound to some of the restrictions that some of our other executives are.

Mr. WILLIAMS. Do you believe that with the power granted to the Federal Reserve Board, that they can raise the price level?

Mr. RAND. Do I believe that the Federal Reserve Board can raise the price level?

Mr. WILLIAMS. Yes; under the powers granted in this bill?

Mr. RAND. No; they could not do it under the bill, without having also the authority to control the price of gold. The Treasury could reduce it, if they did.

Mr. WILLIAMS. Then you do not think that the powers they have in there are sufficient to give them the ability to raise the price level to the desired level?

Mr. RAND. That is right. There are five leverages of control necessary to regulate the price level, and some days you have to use one, and other days something else. Great Britain is using the price of gold in the open market very successfully.

Mr. WILLIAMS. Then we would have to modify this bill in that respect, outside of simply placing the objective that you desire in this bill? We would have to amend it in other respects, in order for them to have the power that you think they ought to have?

Mr. RAND. From the standpoint today of political expediency, I see no basis for any objection on the part of any administrative official to giving this Board the power to issue currency on behalf of the United States Government.

The CHAIRMAN. What you mean to say is, it is unthinkable that there would be cross-purposes between one branch of the Government and the other in the same administration?

Mr. RAND. Yes.

Mr. WILLIAMS. If they would administer this act as it should be administered and we intend it should be administered, they could attain the desired objective?

Mr. RAND. Absolutely.

Mr. WILLIAMS. Without any other changes in it?

Mr. RAND. Except they would have to have the power to issue money and buy and sell gold in the open market, and do little things like that, which you could put in the bill.

Mr. WILLIAMS. Otherwise, it would be absolutely foolish to write in any object that they could not attain?

Mr. RAND. Yes.

Mr. WILLIAMS. There would not be any sense in that kind of legislation, to write into this bill a certain objective, a certain price level which they must attain, and still not give them the power to attain that objective?

Mr. HOLLISTER. You impeach them if they do not do something they cannot do.

Mr. RAND. Yes; and when you do that, you are going to do the greatest thing for the American people, from the standpoint of happiness and continuous occupation—which is a definition of happiness—that has ever been done in the history of this country.

Mr. WILLIAMS. In your opinion there must be two other things put into this bill that are not there at all: One of them being the power of this Board, exclusively, to issue currency; and the other is to vary the price of gold?

Mr. RAND. Yes.
Mr. WILLIAMS. Neither of which are in this bill, at all?
Mr. RAND. No.
Mr. CAVICCHIA. If I understand you, if this power is given, the power to raise or lower the price of gold, that would stabilize the price of the dollar?
Mr. RAND. If they are given the right to buy and sell gold in the open market, the same as the Bank of England does.
Mr. REILLY.. That we ought to give this monetary authority the same power the Bank of England has?
Mr. RAND. Give it the same rights; yes.
Mr. REILLY. The object of the Bank of England has been to keep domestic prices down.
Mr. RAND. No, sir; to keep them stable.
Mr. REILLY. To keep them down.
Mr. RAND. I beg your pardon. I disagree with you on that. I have on good authority, an authority that says that prices are too low now and they should be advanced.
Mr. REILLY. Where?
Mr. RAND. In Great Britain.
Mr. REILLY. That is why I say they have kept them down.
Mr. RAND. They have worked to stabilize prices.
Mr. REILLY. According to all theories, if the dollar depreciates, the cost of living should go up. It has not gone up in London and they keep it there, because it gives an advantage on the export business. You want to raise prices and say this monetary authority should start out and raise prices. That has not been the record of England. The Bank of England has deliberately kept down prices. They have gone in and ruined their labor unions, so they could not get wages.
Mr. RAND. I operate in Great Britain, and I have not noticed any ruination or annihilation of labor in Great Britain. In fact, it is the most unionized country we are operating in.
Mr. REILLY. But they have got no wage scale.
Mr. RAND. The price level in Great Britain was not allowed to drop after September 1931, while our price level continued to drop down to, I think it was, 57 percent. They stopped theirs at 64 percent.
Mr. REILLY. Ours has dropped a great deal since that time.
Mr. RAND. Ours is up to approximately 80 percent now, and theirs is 68 percent, if I remember correctly. The point that I know is that, if we had gone off gold with Great Britain we could have kept our price level steady, and we would never have had the distress and suffering from coast to coast, as we have had.
Mr. CROSS. If we had been given the power to raise or lower ours, because England did——
Mr. RAND. And we would have solved our own employment problem in this country, and I do not care what happens in the other parts of the world.
Mr. REILLY. But you have got two different viewpoints—the monetary authority in London and the one you want to set up here.
Mr. RAND. They operate exactly the same.
Mr. REILLY. But they are going toward different ends.

Mr. RAND. No; Great Britain's price level has been held steady, although it is now relatively below our level, but industrial production or business activity in Great Britain stands at an index of 110 while ours is about 80 percent of its 1928 level.

Mr. REILLY. But you would have no advantage on the export trade, and that is what she is getting, and that is why they have got a different objective.

Mr. RAND. But the mechanism is identical. On a managed currency base you can have any price level that you want. I have never seen anyone dispute that fact. In other words, if you make a mistake in your price mandate, in case you include the mandate in this bill, and guess wrong at 1926 and it should have been 1928 or 1924, Congress can easily change it.

The CHAIRMAN. You have not said a word to us about the debt that is hanging over the people of the country.

Mr. RAND. I did not try to tell you something that you already know as well as I know.

The CHAIRMAN. Of course, this matter of increase in prices goes to the heart of that problem.

Mr. RAND. There is the further fact that President Roosevelt has said that prices have not risen sufficiently to restore the proper relationship between debtor and creditor, and it would be too large a burden on the debtors to establish prices at the present point, and I heartily agree with him.

The average debt that is in existence today was not incurred during the depression. The banks did not loan money during the depression, and mortgage and insurance companies did not buy mortgages during the depression. You did not contract debts during the depression. Your average debts that are in existence today were not incurred in the past 4 years, but they were incurred in the 10 years prior to that, when money was free.

The CHAIRMAN. Is it not true that so long as they are living in dread of constant foreclosure and bankruptcy, they cannot resume normal consumption?

Let me ask you, if nobody has any other questions right now, about some of the mechanics of this bill.

Do you not think that a change, or liberalization, we will say, in the rules for the eligibility of paper at Federal Reserve banks would be very desirable and helpful?

Mr. RAND. I might answer your question by saying this: The maintenance of the price level underlies the solvency of every bank and insurance company, affects individuals, and the entire country, and the Government itself. Maintenance of the price level underlies solvency, and when you let the price level down you destroy the solvency of business.

If you have this mandate in effect and the price level is going to be maintained, your bank assets are not going to depreciate, but they are going to remain intact, by and large, and they are not going to be subject to the influences they were subject to in 1931 and 1932. The bottom is not going to drop out of the value of bank collateral. Therefore, you are now justified in going further on eligibility than you were at any time up to this date; and with your bank-deposit guarantee—for which, Mr. Chairman, I wish to give you a large measure of credit—you will further reinforce the banks against the contingencies which were ever present before.

The CHAIRMAN. Of course, we were in the position where very many solvent banks, judged by all fair rules, were unable to carry on because of the fear that existed, and because of their inability to employ their sound assets to obtain currency with which to meet the demands of depositors.

Mr. RAND. I will never forget, in 1933, testifying before the Senate Finance Committee, I then said, " Unless you enact an emergency law and provide a $2,000,000,000 bank guaranty fund to insure bank deposits, every bank in the country will be closed by March 4."

The CHAIRMAN. We passed a bill like that in the House, setting up a fund of something like $2,000,000,000, in 1932, but a lot of people thought we were crazy for trying to do it at that time.

Mr. RAND. The Senate failed to carry through with that plan.

The CHAIRMAN. Yes.

Mr. RAND. But they did, later. You can increase the eligibility, but the great danger is, when you extend the eligibility to longer than 1 year, the result will be for some banks to go into 5 or 6 or 10 years or perpetual obligations, that will destroy the liquidity of the banks.

The CHAIRMAN. How will we destroy the liquidity so long as they can take their credit assets and use them to obtain currency?

Mr. RAND. I mean there will come a point some day when, if you ever abolish the bank guarantee, that the banks may be plugged up with long-term, nonliquid assets.

Mr. REILLY. Suppose the bank guarantee law is going to live——

Mr. RAND. If the bank guaranty law lives, then your banks are as sound as the Federal Government.

The CHAIRMAN. Well, it should be stated, in that connection, that the guarantee of bank deposits has not been completed. We have only guaranteed about one-third of the deposits, and that job is not finished.

Mr. REILLY. We guaranteed 98 percent of the deposits.

The CHAIRMAN. We guaranteed most of the deposits. That question has not been fully solved, for the reason that you not only want to relieve the citizens of fear and prevent runs on the banks, but we should want to free bankers from fear of runs and withdrawals, so that they will employ bank resources in support of trade and commerce. I think we have done a great deal of good, but I am not sure the job is complete yet.

Mr. RAND. Any further questions you would like to ask?

Mr. CROSS. You think there are two things that ought to be done: One is the Federal Reserve Board should have control of issuing currency, and the next is the right to buy and sell gold in the open market?

Mr. RAND. Yes.

Mr. REILLY. You think that there ought to be a definite price level fixed?

Mr. RAND. Yes; and that is in addition to the mandate. If those three things are injected into this bill and recommended by this committee, my personal opinion is that it will be passed by the House and I have every confidence it will be passed by the Senate.

(Here followed discussion off the record.)

The CHAIRMAN. Of course, we have the right to interpret this legislation in the light of the declared policy and purpose of the administration, repeatedly declared by the President, as has been stated here this afternoon.

Mr. RAND. I would like to put this in as a personal opinion: That with the knowledge that President Roosevelt has demonstrated on monetary subjects and foreign exchange and the relationship of debtor and creditor, and the knowledge that he has demonstrated of conditions that exist in this country, that even without that mandate, we would have what you and I would like to have in the restoration of price level and in the stabilization of the price level; and my recommendations are based upon the belief and conviction that we owe it to the United States of America to perpetuate President Roosevelt's monetary policy in all succeeding administrations, and for generations to come.

The most important contribution that has been made to the progress of civilization is the stabilized dollar.

Mr. HOLLISTER. Has that been achieved?

Mr. CROSS. No; we want to achieve it now.

Mr. RAND. The dollar which President Roosevelt stated to the London Economic Conference we hope to attain in the near future, and which we have——

Mr. HOLLISTER. I did not know that President Roosevelt had any monetary policy; I have never been able to ascertain it.

Mr. RAND. A very definite monetary policy.

Mr. HOLLISTER. What do you conceive it to be?

Mr. RAND. To give to the country a dollar of substantially the same purchasing power and debt-paying power as the dollar which he hoped to achieve in the near future, dating from the time he made the speech.

Mr. HOLLISTER. Do you think the steps that have been taken by the administration have brought about such a result?

Mr. RAND. The steps that were taken up to February 1934, when we again returned to a fixed price of gold, which was advocated by the orthodox economists and which has since then prevented any further rise in the value of commodities and re-employment of the unemployed, and——

Mr. REILLY. The commodity price has gone up since then, has it not?

Mr. RAND. It is my belief that the evidence is so clear that the progress of 1934 is so little compared with the vast strides we made in 1933, that the logical thing for the administration to do is to go back to the policy which showed the greatest results.

Mr. HOLLISTER. You are urging that the administration should return to the policy which the administration has apparently given up?

Mr. RAND. No; only temporarily.

Mr. HOLLISTER. But the last monetary moves the administration has made have not, in your opinion, been similar to the first moves that were made?

Mr. RAND. No; moves that have been made during the past year I think have left us in status quo. We have been frozen to a fixed price of gold, and it has been demonstrated that we cannot progress so long as about one-half of the civilized business world is off gold definitely, and has no fixed relationship to gold.

In other words, those countries that have adhered to a fixed price of gold, including the European gold bloc and the United States, have shown poor results in recovery during the past year.

Mr. HOLLISTER. Then you were not an advocate, were you, Mr. Rand, of the Warren gold-buying policy which was the administration's first attempt?

Mr. RAND. I never was an advocate of the policy of chalking up the price of gold on a blackboard, without being willing to make the price of gold in other markets.

Mr. HOLLISTER. That was the administration's first monetary attempt?

Mr. RAND. It was, as such; but the effective raising of the price of gold began when exportation of gold was embargoed in April 1933, not when the gold buying began 6 months later.

Mr. HOLLISTER. That was given up entirely?

Mr. RAND. It was.

Mr. REILLY. The administration did that to find the real value of the gold, and it fixed the dollar at that value. All that buying of gold was for that purpose, to know where to stabilize the dollar.

Mr. RAND. It always appears wise, when you are conducting a policy of restoring prices, or raising prices, to hesitate for a breathing spell in order to see what the ultimate effect is going to be of what you have already done, and in that respect I believe it was wise to hesitate for 6 months or a year; but there is no need, in my opinion, to hesitate any longer.

Mr. REILLY. But you recognize that it is a more difficult problem to raise prices than to keep them from falling?

Mr. RAND. Everyone recognizes that. You can undo in 1 day what it took generations to build up.

Mr. CROSS. Like climbing up a ladder, you go up pretty slow but come down fast.

The CHAIRMAN. Gentlemen, we will meet at 10:30 tomorrow.

Mr. Rand, I thank you on behalf of the committee. Your statement was very able and helpful, and we appreciate it very much.

(Thereupon a recess was taken until 10:30 a. m., Tuesday, April 9, 1935.)

(Inserted in record of hearings upon request.)

THE SIEGFRIED PLAN

(By Thorwald Siegfried, author of The Siegfried Plan for an Honest Exchange of Values by the Issue of a Sound Money)

WHEN A BANK

(*a*) Permits a manufacturer to "deposit" as cash a 60-day merchandise-draft on a jobber or merchant, and

(*b*) Allows the manufacturer to check against the "deposit" up to its full amount (less the discount for 60 days).

(c) It thereby issues new credit-currency, and by repeating the process builds up the great volume of "deposits" in banks.

(*d*) Inasmuch as the wholesale prices charged to jobbers and merchants by manufacturers include the manufacturers' profits, the bank process described makes available to the manufacturer, as cash, and at the point of production, his anticipated profits before these profits are justified by the verdict of the retail market.

(*e*) Inasmuch as the ratios of profits in merchandise transactions susceptible of discount by banks range from 0 to 100 percent, the "dollars" checked out thereby lack economic parity with one another, and, on the contrary, have disparities corresponding to the profit ratios in the prices of goods which they represent.

(*f*) These disparities operate to the disadvantage of the producers of goods that are least susceptible to the application of high-speed machinery, among whom farmers are the most important class.

(*g*) We favor legislation which will permit banks to discount commercial paper to the extent of the wages paid for the production of the goods represented, and no more, to the end that all "dollars" shall have economic parity, that all currency issued shall pass through the hands of the producing classes, that purchasing power shall be adequate to buy all goods offered, that profits on good goods shall be offset by losses on poor ones, and that the receipt of profits may be deferred until the goods shall have been sold to customers.

MARINE MIDLAND GROUP, INC.,
New York City, April 12, 1935.

LETTER FROM HON. EDMUND PLATT

DEAR HENRY: I am glad to see that the House committee has struck from the banking bill the provision in title I denying deposit insurance to nonmember banks after July 1, 1937. I don't believe in these compulsory features, and have always thought that the whole Reserve System, national as well as State banks, could, now that it is so well established, be put on a voluntary basis, allowing small national banks to withdraw if they care to do so.

I don't know whether you saw the brief I sent to John Hollister on the bill, when I found that I couldn't go down and testify. It is a much milder criticism of title II than most of the economists are making, and contains the argument against compelling State banks to join the Reserve System in order to continue deposit insurance.

Best regards.

Yours sincerely,

EDMUND PLATT.

(The brief above referred to follows:)

Having been actively engaged for more than 10 years, 1920–30, as vice governor of the Federal Reserve Board in the administration of the Federal Reserve Act, and having been a member of this committee under the chairmanship of Carter Glass when the Federal Reserve Act was passed, it is natural that I should not like to see the act radically changed unless there are convincing reasons for the changes. My interest, therefore, is chiefly in title II, which does radically change the Federal Reserve Act in several important particulars. The open-market section practically does away with the autonomy and independence of the regional Federal Reserve banks in some of their most important functions. Section 16 of the Federal Reserve Act, which has reference to the issue of Federal Reserve notes, is largely repealed and entirely rewritten, making the notes asset currency without special collateral; section 13 is so amended that Reserve banks are to be permitted to loan on any sound assets of member banks, doing away with the last vestige of the idea of self-liquidating, short-term commercial paper. The composition of the Board itself, especially with relation to the Governor is so changed as to bind the Board more closely to the political administration in power at the time instead of giving it greater independence; the organization of the Federal Reserve banks through the consolidation of the offices of governor and chairman or Federal Reserve agent and the requirement that the governor must be approved by the Federal Reserve Board is considerably altered. Section 16 relating to reserves is so amended as to remove the safeguards, the affirmative vote of five members and the approval of the President, from the grant of power given in the Emergency Act of 1933 to raise as well as lower the reserves to be maintained by member banks in certain cities, etc., and districts. Finally, in title II the authority of national banks to make loans on real estate is greatly widened.

Governor Eccles in his recent testimony before the committee ably defended these provisions and made suggestions for amendments to several sections which would be improvements, but he did not give any convincing reasons why title II should be passed at this time. In fact, if I understood him correctly, he said in answer to one of his questioners that there was not much that the Federal Reserve banks could do that has not already been done toward aiding recovery, which is certainly true. Commercial interest rates are at unprecedently low levels, and long-term interest rates, held up for a good while by the uncertainty caused by devaluation of the dollar and by inflation agitation, have also begun to come down materially. If business is not borrowing, it certainly is not because the rates are not attractively low. Nothing could be accomplished by trying to make them lower and much harm might be done, as it is difficult enough at present for banks to make money. This being true, it seems to me that there is much to be said for the recommendations of the Chamber of Commerce of the State of New York and of the American Bankers Association for a postponement of consideration of this part of the bill until a thorough study can be made of the questions involved by an impartial commission. The American Bankers Association has suggested the Brookings Foundation, while the chamber of commerce apparently contemplates a commission to be appointed by Congress. There is no doubt that amendments to the Federal Reserve Act made from time to time, particularly by the Banking Act of 1933 and the emergency acts, have produced a patchwork which is somewhat confusing. A thorough study by a competent body should result in greatly simplifying and improving the whole act.

Before going into more detail with relation to title II there are some things in titles II and III to which I should like to refer, though with a few clarifying amendments it seems to me they might well be enacted into law at the present session. I do not like the provision near the end of title I, paragraph 23, which reiterates the requirements of the Banking Act of 1933 that nonmember State banks must become member banks if they are to retain Federal deposit insurance after July 1937. It has never seemed to me wise to attempt to compel State banks to join the system, and I will go even further and say that I have always doubted the wisdom of the compulsory feature even for national banks. There is nothing of this compulsion in European central banking. The system, in my opinion, would work satisfactorily if membership were made voluntary. Compulsion may have been necessary at the beginning in order to get the system started, but, in my opinion, the advantages which all the larger banks unquestionably receive from membership would make it necessary for their own interest to continue as members. The reserve requirements and the provisions that balances in Reserve banks are counted as reserve while balances in correspondent banks are not so counted, and the privilege of keeping up such reserve balances by rediscounting when necessary are of great value to the larger banks. States may, and some of them still do, allow their State-chartered banks to count balances in city-correspondent banks as reserves, but this is of advantage only to the smaller banks which are frequently dependent upon their city correspondents for service and advice. The fact that most of the small banks are outside the system and do not consider membership an advantage does not at all hinder the effective operation of the system. Several campaigns were conducted while I was a member of the Reserve Board to induce the small State banks to become members, and several investigations were carried on by the Board, by the Reserve banks, and by this committee to find out why they did not join the system.

I became convinced that at least some of the reasons the small banks gave for remaining nonmembers were good reasons. One of their chief complaints, the fact that they could obtain no interest on their balances in the reserve banks, but could and did obtain interest from their city correspondents, has been done away with by the prohibition in the Banking Act of 1933 of payment of interest on demand deposits. May I say that I think the present law and the present regulations are a little narrow in defining demand deposits as anything payable within 30 days. In other countries it is customary to pay interest on 15-day deposits and even on 7-day deposits. Therefore, I think the amendment to the first paragraph of section 19 of the Reserve Act contained in the first part of section 323 (p. 64) of title III of this bill, giving the Federal Reserve Board full power to define the terms "demand deposits", "time deposits", etc., is a good one.

This brings me to title III. I have heard some items in this title criticized as being rather obscure, and as possibly containing "jokers", or as going further than they appear to go. However, I know that most of the amendments in this title were recommended by the Federal Reserve Board or by the Comptroller to clarify the provisions of the Banking Act of 1933 and make them more workable. Some of them have been recommended by the Board and by the Comptroller in their annual reports. The amendments in this title are technical, in the main, and I prefer to leave criticism of them to the technicians.

Sections 303 and 307 may permit limited underwriting. This does not seem clear to me but under proper regulations I do not believe it would be necessarily harmful. I have never believed in too narrow restrictions upon the operation of our banks. We can develop good bankers only by giving them some reasonable latitude.

Title II, as Governor Eccles has said, is the heart of the bill and makes some vital and, to my mind, some exceedingly unwise amendments to the Federal Reserve Act. Governor Eccles has suggested several amendments which would be good but even with the improvements the powers of the Federal Reserve Board and its dependence upon political administration would be increased, and the independence of the Federal Reserve banks decreased. As it stands in the bill, section 305 creating a new open-market committee, comes pretty near creating a central bank or monetary authority. The new committee is given full power over the purchase and sale of securities "and the Federal Reserve banks shall conform their open-market operations to the provisions thereof." I wonder if it is generally understood that 90 percent of all open-market operations are carried out in the country's chief money market; that is in New York, and in the main they put money, or funds, into New York or withdraw them. Under the provisions of the bill as drawn this committee could compel the interior Federal Reserve banks, the Atlanta Reserve bank, the Dallas Reserve Bank and others to put money into New York, or in popular terms into Wall Street, without giving them any option, even if their directors were of the opinion that the funds were needed at home. I do not believe that is either wise or necessary, and I do not believe it would be approved if understood. I know the argument that there should be centralization of authority, that the system can't act promptly in case of emergency, etc., but that is theory. The system has always acted as promptly as necessary, possibly in some cases too promptly, so far as open-market operations are concerned. It has not always been so prompt about changing discount rates, particularly in the matter of increases, but the fault has not been with the reserve banks.

In my opinion, the importance of open-market operations has been greatly exaggerated. The system could be successfully operated through prompt and decisive changes in discount rates, without open-market operations except such minor purchases or sales as might be necessary or advisable to make the rates effective. Open market operations became popular in the early 1920's largely because they were not fully understood and were to a considerable extent concealed. In England such operations used to be referred to by the older economists as "the hidden hand", which put money into or took it out of the London market without any announcement and without letting anyone know what was going on except by inference from action of the money rates and the money market itself. The high discount rates, in some of the Reserve banks as high as 7 percent, put into effect by several of the Reserve banks in 1920, were believed by many people to have been the cause of the depression of 1920–21. They were the subject of much oratory in Congress and of much denunciation of the Federal Reserve Board and of its then governor, W. P. G. Harding. In my opinion they had very little to do with the depression, the chief causes of which were easily to be seen elsewhere, but if they were effective in curtailing expansion the operation was certainly justified by the results, for the depression of 1920–21 was exceptionally short and we were soon climbing out of it into an era of almost steadily increasing prosperity. However, rate increases were unpopular, and after the rates had been lowered to normal proportions when it again seemed necessary to exercise some restraint on expansion of credit "the hidden hand" was resorted to and open-market operations became more important than changes in rates in the operation of the system. Securities were sold when expansion seemed to be going too rapidly and were purchased when contraction appeared to be going too rapidly. Generally, these operations were accompanied by slight changes in the rates, usually only one-half of 1 percent at a time, but sometimes they were not accompanied by any rate changes. The net result of the policy was that the member bank reserve balances, the credit base, were generally held rather higher than they should have been until finally the whole matter got out of hand with the great expansion of 1928–29, which was manifested chiefly in the speculative markets.

While a member of the Federal Reserve Board, I was much of the time under the impression that rediscount rates were too low and frequently constituted an unnecessary and unwise inducement towards borrowing on the part of the member banks, particularly the smaller banks whose rates to customers were generally several points above the Federal Reserve rates. However, the policy of the Reserve Board at that time was warmly praised by most of the economists of the monetary school like Maynard Keynes of England, Cassell of Sweden, and Irving Fisher of our own country. Wholesale prices during that period remained relatively steady from about 1923, reaching their highest point in 1925 and then gradually declining somewhat while the country seemed most of the time extraordinarily prosperous. The monetary economists declared that the Federal Reserve Board was stabilizing prices and sought to amend the act to require the system to be so operated as to stabilize prices. "All you have to do", they declared, "is to continue what you are now doing." The Board and the system did continue along about the same policy and the debacle of 1929 followed perhaps as a result of this policy, certainly partly as a result of failure to apply the brakes through both the rediscount rates and open-market sales soon enough, but probably also mostly from other causes which I cannot go into at this time.

In connection with the open-market policy of the Board, a good deal has been said about control of credit, and I wonder just what the people who use the word "control" so glibly understand it to mean. Certainly, if it is understood in its ordinary sense as we use it, for instance, in mechanics, "control" of credit is impossible; at least, without an amount of minute regimentation in all banks and of borrowing that would be intolerable. All that can be done by central banking is to exercise some measure of influence rather than control over the volume of credit. This can be made to be somewhat effective when credit is increasing if the central banking system has the courage to put on the brakes with sufficient vigor, but the experience of the past 4 years in this and other countries shows that not much can be done to prevent a declining volume of credit when the pyramid of debt breaks and a depression gets started. Another word which has been much misused in connection with credit is the word "create." We are told that the banks create credit and the word seems to be understood by many people as in the first chapter of Genesis, conveying the idea that the banks have absolute power to create credit out of nothing. Certainly this is not true. Dr. Walter Leaf in his excellent little book on banking, published in the late 1920s, paid his respects to this theory very effectively. "It takes two to create credit, a banker and a borrower", and the banks are powerless when business men of good credit standing are unwilling to take the risk of borrowing. Furthermore, when banks make loans they do not create anything in the nature of new wealth. They simply enable wealth already long since created and saved to be used conveniently in making exchanges. This is clear enough in the case of mortgages, or of collateral loans. A borrower on real estate, or on bonds, has the property and pledges it for a loan in order to make a purchase instead of trading or bartering it direct. The banks act as brokers making certain properties liquid for trading purposes. In the case of so-called "unsecured loans" to business the principle is the same. Such loans are made on the basis of established wealth on the credit statements of a going business built up through industry and saving. The banks act as brokers in still another sense, enabling the savings of one man or of one business, including temporary savings or current accounts, to be loaned to another man, thus facilitating a much more rapid turnover of transactions than could otherwise obtain. Nothing is created, however, excepting the new wealth which may result from the enhanced liquefaction of assets and the increase of manufacturing or business transactions.

I have no great objection to the consolidation of the offices of Governor and Chairman or Federal Reserve agent in the Federal Reserve banks referred to in section 201, but the abolition of the office of Federal Reserve agent and the repeal or rewriting of section 16 of the Federal Reserve Act, which refers to Federal Reserve notes, abolishing the special collateral now held against such notes, distinctly implies a recognition that the note issues of the Federal Reserve banks are bank notes and not United States Government notes issued to the banks. The office of Federal Reserve agent in each bank was created for the purpose of holding collateral to protect the Government which is issuing its guaranteed notes "for the purpose of making advances to Federal Reserve banks through the Federal Reserve agents." This was always fictitious in actual practice and it is well to have it repealed, but why include after the word "notes" in the second line of the new section 16 the words "which shall be obligations of the United States?" The guarantee of the United States is certainly not necessary with the provision that the notes are to be secured "by a first and paramount lien on all of the assets of such bank."

Under this provision of the bill the notes become strictly an asset bank currency which I think is not seriously objectionable, although I see no particular reason why the change should be made at this time. It goes far away from the original purpose of the Federal Reserve Act which provided that reserve notes could be issued only against deposits with the reserve agents of self-liquidating commercial paper which had been rediscounted with the banks. Taken with section 206, which repeals all the rediscount eligibility restrictions and permits Federal Reserve banks to "make advances to any such member bank on its promissory note secured by any sound assets of such member bank, the change from the original Federal Reserve Act is certainly radical. At the present time it is not only unnecessary but academic. The member banks are not rediscounting with the Federal Reserve banks and will have no occasion to rediscount so long as huge excess reserves are maintained through the ownership by the reserve banks of huge holdings of Government securities. Along with the provision allowing Federal Reserve banks to make advances on "any sound assets of member banks" is to be read section 210 which greatly relaxes the restrictions upon national banks in the matter of real-estate loans and without limiting the sections in which the loans may be made. Under this provision western banks might make loans on New York City real estate and eastern banks might make loans on western farm land. Governor Eccles has happily suggested the restoration of limits, but this attempt to encourage commercial banks to go into the real-estate field is almost certain to lead to trouble and is in strong contrast with the powers of the Canadian chartered banks which are not permitted to make loans on real estate at all. Real-estate loans in Canada are made by mortgage companies or by savings banks, and one reason I think why eastern banks have stood up better than western banks and southern banks in our own country is the fact that a very large part of the real-estate loans in the East has been made by mutual savings banks which are carefully restricted by law and by mortgage companies not so well regulated, many of which are now in trouble. That real-estate mortgages should become the basis of rediscounts in Federal Reserve banks when we have home-loan banks to take care of such matters seems a complete perversion of the principle on which the Federal Reserve Act was founded, not only extremely unwise but entirely unnecessary.

Governor Eccles has recommended an amendment to paragraph 3 of section 203 which, as it stands, requires the Governor of the Board to leave the Board "upon the termination of his designation as Governor." The second paragraph of this section providing for an increase of salary to members of the Federal Reserve Board and for their retirement on pension is in the main good, although I can see no reason why the two members who have served since the original Board was formed should be retired so long as they are able to render useful service. They do not seem to be much older today than they were when I first knew them some 15 years ago and are certainly as intellectually vigorous as ever. In amending the first paragraph of section 10 of the Reserve Act with relation to the appointment of members of the Reserve Board it is to be regretted that the number of members of the Board was left at eight, which permits a tie. The Comptroller of the Currency of the Secretary of the Treasury should be dropped from the Board.

Some consideration should be given to the fact that in rewriting section 15 the provision that "No Federal Reserve bank shall pay out notes issued through another under penalty of a tax of 10 percent" has been stricken out. When the Federal Reserve Act was passed this provision, copied I think from the Canadian law, was considered of considerable importance as insuring prompt redemption of the notes and preventing redundant circulation. I am not sure that it has been found of much service and it certainly has required considerable clerical work. The proposed new section 16 merely requires the sending in of worn out bills or notes. I may add that I hope the gold reserves which rightfully belong to the Federal Reserve banks may be restored to them in due time and that redemption of the notes in gold coin may be again resumed.

Governor Eccles made out a good case in my opinion for section 209, amending section 16 so that the Reserve Board could change reserve requirements of member banks "in order to prevent injurious credit expansion or contraction", and suggested a good amendment as to its application. Such power could be made very useful in checking inflation, but it could be used also in the direction of the so-called "100-percent" bank, and I do not believe the power should be given without limit, or without the safeguard of requiring more than a majority vote of the Board.

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