

*White House*

February 4, 1935.

Mr. Marvin H. McIntyre,  
Secretary to the President,  
White House,  
Washington, D. C.

Dear Mr. McIntyre:

In accordance with our telephone conversation this afternoon, I am transmitting herewith two copies of a draft of a letter which I have prepared pursuant to a request which the President made to me last week, and which pertains to the proposed banking legislation. I shall appreciate it if you will bring it to the President's attention as soon as possible and I sincerely hope that it will be of some assistance in connection with the banking legislation.

Very truly yours,

Marriner S. Eccles,  
Governor.

Inclosures.

February 4, 1935.

Draft of President's letter to the Committee Chairmen:

I recommend to your Committee certain changes in the laws concerning banks.

The Banking Act of 1933, the legislative history of which extended over the preceding three years, was designed in large part to prevent a recurrence of the speculative excesses and abuses that culminated in the stock market debacle of 1929. In addition, as a result of the great number of bank failures that occurred from 1930-1933, provision was made in this Act for the insurance of bank deposits.

I am convinced, however, that further changes in our banking laws are urgently needed for smoothing the path of economic recovery and for preventing the recurrence of conditions that led to the collapse of the banking system in the spring of 1933.

It is proposed to make certain revisions of the deposit insurance law which has been extremely helpful since its enactment but requires amendment in the light of a year's experience under the temporary plan.

During the first six months of the year 1934 deposits were insured to the extent of \$2,500 for each depositor. During the last six months of the year the insurance was extended to \$5,000 for each depositor and it is found that this protects 98.39% of all depositors in the insured banks in full. This degree of protection has proved adequate to restore confidence in the insured banks as a whole and in the nine banks which closed during the year the payments by the Federal Deposit Insurance

Corporation have entirely relieved the communities of the hardships and disturbances which heretofore have generally accompanied a bank failure.

Under existing law the permanent plan would give increased benefits to only 1.61% of the number of depositors but it would almost double the liability of the Corporation by increasing it from approximately \$16,500,000,000 to more than \$29,000,000,000. I recommend, therefore, that the limitation of \$5,000 for each depositor be continued and made a part of the permanent insurance plan.

The original purpose of the Temporary Fund of the Federal Deposit Insurance Corporation was to provide insurance of deposits for a six months' period before the necessary arrangements could be completed for instituting the permanent plan. The Temporary Fund has been raised through assessments contributed by the banks based upon their insured deposit liability. The permanent plan in the existing law contemplates assessments based upon the entire deposit liability of the insured banks. It is believed that the general benefits both to the public and to the banking structure of the Country resulting from the insurance of deposits call for an assessment plan substantially as provided in existing law, but limited in amount. The plan of assessing upon the insured deposit liability alone, considering the general benefits, throws a disproportionate share of the burden upon the smaller banks and upon banks in which small deposits predominate.



Provision should be made which will enable the Corporation to allocate to surplus part of its existing capital of approximately \$290,000,000, contributed by the Government and by the Federal Reserve banks, and to enable it to set up reserves from the proceeds of the assessments so that the insurance may be continued at all times upon a sound basis, at no greater cost than is necessary and without becoming unduly burdensome in times of stress.

In view of the liability of the Federal Deposit Insurance Corporation to depositors of failed banks, it is important to give to the Directors of the Corporation authority to protect the funds of the Corporation from the consequences of bad management and unsound banking practices on the part of insured banks. This should be accomplished with due regard to the existing authority for direct supervision.

The cornerstone of our banking structure is the Federal Reserve System and it is proposed to make this system more directly responsive to national economic needs and to make the commercial banks better adapted to meeting the credit requirements of commerce, industry, and agriculture.

The Federal Reserve System was established more than twenty years ago and has rendered invaluable service to the nation during the war, the post-war period of readjustment, and during the present depression. The experience of twenty years, however, has shown that in certain respects the System needs to be strengthened in order to meet changing economic

conditions in this country and in the world. Our problems, especially in the field of banking, have become more and more national in their scope. Commercial banks, through the creation of credits, supply the bulk of the nation's means of payment. Effects of changes in the volume of credits are nation-wide and regulation of this volume should be entrusted to a body which represents the nation. Therefore, while it is desirable to retain regional management and responsibility at the Federal Reserve banks in matters of local concern, it is essential to unify the responsibility for national policies. For this purpose it is proposed to change the composition of the Federal Open Market Committee so as to include representatives of both the Federal Reserve Board and the Reserve banks and to give the Committee the power to determine the open-market policy of the Federal Reserve System. Since operations of the Federal Reserve banks in the open market are frequently the most important single element determining changes in the volume of credit available to the people and in the rates required to be paid for borrowed money, unified control of these operations is imperative.

It is also proposed to combine the office of the Governor of the Federal Reserve bank, who is now appointed by the directors of the bank, with the office of Chairman of the Board of Directors, who is now appointed by the Federal Reserve Board, and to have the occupant of the combined office appointed by the board of directors, subject to the approval of the Federal Reserve Board. The proposal would promote economy and efficiency

by doing away with the present dual organization of the banks and the consequent diffusion of responsibility.

To enable the Federal Reserve banks to respond more effectively to the changing needs of the country it is important to remove some of the restrictions upon their activities imposed by the original Federal Reserve Act, fully recognizing that these restrictions were wisely imposed upon a system that was new and untried. Among these is the rigid definition of the kinds of paper that are eligible for discount at the Reserve banks. Changes in our economic life and financial practices have greatly reduced the volume of self-liquidating paper of the kind to which Federal Reserve bank discounts are largely limited. In consequence, in times of stress, when help from the Federal Reserve System was most urgently needed, there were many banks devoid of assets available for borrowing at the Federal Reserve banks. It became necessary to remove these restrictions temporarily by emergency legislation, but this action was not taken until much harm had been done to the country. At the present time there is evidence that the restrictions on eligibility of paper for discount at the Reserve banks contribute to the difficulty of persons who need to borrow money and possess perfectly sound assets but are unable to obtain the required loans because these assets are technically ineligible for discount. For these reasons, legal restrictions on eligibility should be removed and the Federal Reserve Board, which is always in session, should be given authority to determine the character of paper that shall be eligible for discount by a Reserve bank.



It is also proposed that segregation of collateral behind Federal Reserve notes be no longer required. These notes are obligations of the United States Government and prior liens on all the assets of the Federal Reserve banks. Segregation of collateral back of these notes, therefore, adds nothing to their safety. It caused serious difficulties, moreover, in tying up gold over and above the 40 per cent required reserve in 1931 and 1932 when there was a foreign drain on our gold.

In the field of commercial banking the proposals are few but vital for the speeding of recovery. They are directed toward the object of making it more feasible for the banks to meet the credit needs of their localities and to relieve them of some of the unnecessary restrictions which are at the present time a handicap to recovery. With this in view it is proposed to liberalize the authority of the banks to make mortgage loans. This class of loans is essential for the revival of building activity and, under proper safeguards, present restrictions can be relaxed without endangering the soundness of the banking system.

I hope and believe that the enactment of these proposals would spur the commercial banks to go further in their efforts to serve the country's needs and to lend their unstinted support to economic recovery.

The proposed legislation also contains corrective and clarifying amendments to existing law which will provide for simplification of administration. They are mostly of a technical nature and were in large measure embraced in the so-called "Omnibus Banking Bill" approved by both Committees of the Seventy-Third Congress.

Very truly yours,