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THE REVEREND CHARLES E. COUGHLIN VS. THE FEDERAL RESERVE SYSTEM

Most of the Reverend Coughlin's allegations against the Federal Reserve System center around two main charges. The first is that Congress has unconstitutionally delegated the power to coin money and to regulate the value thereof to a group of privately-owned banks controlled by private citizens. The second is that by virtue of this delegation the Government is losing enormous profits which accrue to private institutions. Neither of these charges can be substantiated.

The Power to Coin Money

All money *coined* in the United States is coined by the United States Treasury in accordance with acts of Congress.

The Regulation of the Value of Money

The regulation of the value of money is at present shared by the President, the Treasury, and the Board of Governors of the Federal Reserve System, acting in accordance with acts of Congress. Congress has not delegated its power; it delegates the exercise of its power, just as it does in the case of all legislation requiring administrative action.

Congress has authorized the President to fix by proclamation the weight of the gold dollar, within the limits of 50 to 60 percent of its pre-1933 rate "at such amounts as he finds necessary from his investigations to stabilize domestic prices or to protect the foreign commerce against the adverse effect of depreciated foreign currencies", (Gold Reserve Act, 1934, Sec. 12).

Congress has authorized the Secretary of the Treasury, with the approval of the President, to handle the Stabilization Fund of $2 billion "for the purpose of stabilizing the exchange value of the dollar", (Gold Reserve Act, 1934, Sec. 10); has authorized the Secretary of the Treasury to purchase silver at such rates, times, terms and conditions as he may deem reasonable and most advantageous to the public interest "whenever and so long as the proportion of silver in the stocks of gold and silver of the United States is less than one-fourth of the monetary value of such stocks", (Silver Purchase Act, 1934, Sec.3).

Congress has authorized the Federal reserve banks, subject to the review and determination of the Board of Governors, to establish rates of discount which "shall be fixed with a view of accomodating commerce and business", (F. R. Act, Sec. 14-d); has authorized the Federal Open Market Committee, composed of the seven members of the Board of Governors and five Federal reserve bank presidents, to engage in the purchase and sale of securities "with a view of accomodating commerce and business and with regard to their bearing upon the general credit situation", (F. R. Act, Sec. 12-A); has authorized the Board of Governors to change the reserve requirements of member banks "in order to prevent injurious credit expansion or contraction", (F. R. Act, Sec. 19); has authorized "Federal reserve notes to be issued at the discretion of the Board of Governors of the Federal Reserve System for the purpose of making advances to Federal reserve banks through Federal reserve agents as hereinafter set forth and for no other purpose", (F. R. Act, Sec. 16); has authorized the Board of Governors to determine the amount of credit that may be extended on any security registered on a national security exchange "for the purpose of preventing the excessive use of credit for the purchase or carrying of securities", (Securities Exchange Act, Sec. 7); has authorized the Board of Governors to fix the percentage of individual bank capital and surplus which may be represented by loans secured by stock or bond collateral "with a view to preventing the undue use of bank loans for the speculative carrying of securities", (F. R. Act, Sec. 11-m).

Many more specific directions by Congress to the President, the Secretary of the Treasury and the Board of Governors, for the administration of monetary power could be cited. A sufficient number has been quoted, however, to demonstrate conclusively that Congress has exercised its power "to coin money and to regulate the value thereof" and has merely delegated the administration of this power to the President, the Secretary of the Treasury, and the Board of Governors.

The next question is, are the authorities and bodies to whom the administration of these powers has been entrusted public or private? There can be no question as to the public character of the President and the Secretary of the Treasury. Reverend Coughlin, however, says that "The Federal Reserve banking system, contrary to the Constitution, permits a small group of citizens to coin and regulate the value of money in this nation to the detriment of the great mass of citizens", (Lecture, December 15, 1935). This is not true. As was noted above, the Board of Governors has the dominant voice in all matters pertaining to national monetary policy that are within the purview of the Federal Reserve System. <u>The Board of Governors is a public body created by Congress, whose members are appointed by the President by and with the advice and consent of the Senate.</u> In one particular the administration of the monetary power is shared with the Presidents of the Federal reserve banks, five of whom are on the Federal Open Market Committee. In this case, however, not only do they constitute a minority on that committee but their appointment as presidents of their respective Federal Reserve Banks is subject to the approval of the Board of Governors.

It is evident that Reverend Coughlin's claim that Congress has unconstitutionally delegated the power to coin money and to regulate the value thereof to a group of privately-owned and controlled banks is entirely without foundation. Both the coinage of money and the regulation of the value of money are in public hands and administered according to the will and directions of Congress.

The Record of the Present Administration in Matters Relating to Monetary Control

Practically all the specific powers enumerated above were secured by the present Administration. Congress exercised its power to regulate the value of money by authorizing measures to stabilize domestic prices and to protect our foreign commerce against the adverse effect of depreciating foreign currencies, and empowering the President and the Secretary of the Treasury to carry out these measures.

The Banking Act of 1933 and the Securities Exchange Act of 1934 gave the Federal Reserve Board increased powers to check speculative excesses. The Banking Act of 1935 made the Board of Governors the dominant authority in the control of the volume of deposit currency of the country. It was bitterly opposed by many prominent bankers and by various reactionary bodies.

Reverend Coughlin recognized the importance of the Banking Act of 1935 in the following words: "The Eccles Bill, which proposes that the government will control the credit of the nation and not own the twelve Federal Reserve banks, is under discussion", (Lecture May 26, 1935). If we substitute for the word "credit" the phrase "deposit currency", this is substantially correct. He went on to say, however, that "the National Union cannot support the Eccles Bill because it permits the Federal Reserve banks to print bank notes against mortgages, stocks, promissory notes, or any so-called assets--be they sound dogs or cats". This is untrue. The "Eccles Bill" proposed to retain the provision that Federal reserve notes be backed up to 40 percent by gold certificates and merely proposed that the requirement that specific collateral against notes consisting mainly of commercial paper be repealed. This latter proposal was not incorporated in the act as passed.

Private Ownership of the Federal Reserve Banks and the Member Banks

Having shown that the control of money is in public hands, we may now turn to Reverend Coughlin's final point that the ownership of banks is in private hands. What are the facts and what is the significance of these facts?

The Federal reserve banks are "owned" by the member banks only in a very special sense of the term. The ownership carries none of the customary prerogatives of ownership. The "owners" have no voice in any of the activities of the reserve banks that pertain to the formulation or execution of national monetary policies. The Chairmen of the Boards of the banks and two other directors are appointed by the Board of Governors; the Presidents of the banks are appointed subject to the approval of the Board of Governors . Member banks are entitled only to a six percent return on their holdings of stock in the Federal reserve banks. All other profits, if any, accrue eventually to the Government, since should a Federal reserve bank be dissolved or go into liquidation any surplus remaining after the payment of dividends "shall be paid to and become the property of the United States", (F. R. Act, Sec. 7). Congress may at any time make such disposition of the surplus of the Federal reserve banks as it wishes. In 1933 it transferred one-half of the surplus of the Federal reserve banks to the Federal Deposit Insurance Corporation.

It is apparent, therefore, that the nominal private "ownership" of the Federal reserve banks is a matter of very little consequence. If the Government bought out the member banks, its control would be no greater than at present and it would save only the difference between the interest on the money it would borrow for this purpose and the dividends at present paid to banks, an amount of $4 million. This would be an infinitesimal figure in the national accounts.

The member banks perform two important services for the community. They act as agencies for the investment and handling of savings and they furnish the means of handling 90 percent of the monetary transactions of the community. Both services are carried out under the strict supervision and regulation of public authorities in accordance with instructions laid down by Congress. Both these services entail expense which the member banks meet by means of interest on loans and investments. Any excess of income over expenses and losses constitutes a return on banks' capital funds. The question at issue is, are these returns excessive?

From 1923 to 1929, inclusive, a period of relatively high interest rates, the return on member banks' capital funds averaged 8.6 percent (Federal Reserve Annual Report, 1934, page 179), without making an allowance for upwards of $100 million of capital funds of member banks that failed. This return was not out of line with the return on capital invested in other types of enterprise in this period. For the period 1923-35, inclusive, the rate of return on member banks' capital was 4.07 percent, again without making allowance for the enormous losses of capital funds in bank failures. Net profits in 1935 were $212 million, or a rate of return on capital funds of 4.14 percent. These <u>facts</u> may be contrasted with Reverend Coughlin's assertion that "while the laborer and dolester are suffering the ravages of depression this privately-owned Federal banking system is enjoying the most lurid prosperity in its checkered career", (Lecture Dec. 8, 1935).

Reverend Coughlin appears to labor under the delusion that banks can subscribe for Government bonds without giving anything in return, that no expense is involved for member banks, that they collect billions of interest on these bonds and that the principal eventually paid will be pure profit. Actually, when a bank buys a government bond it pays for it by a check drawn on its balance at a Federal reserve bank. When it has no excess balance at the reserve bank and cannot dispose of other assets it cannot buy a bond. When the Government spends the balances it acquires in this way at the reserve banks, the individual deposits of member banks are increased. Banks' liabilities increase as rapidly as their assets. When the Government redeems its bonds through taxes, it collects deposits from individuals and turns them over to banks in exchange for the bonds. Both the assets and liabilities of banks shrink. The only thing the bankers get out of this transaction is the difference, if any between the interest received on the bonds and the expenses of handling the additional deposits.

Member banks held on March 4, 1936, $10,564,000,000 of the public debt. The computed annual rate of return on these government securities was only 2.45 percent. In other words, member banks received annually some $260 million from assets of $10½ billion. This is a much lower rate than the Government securities held by the general public yield. On the bonds held by private individuals the computed annual rate of interest was 3.22 at the same date.

From December 31, 1932, to March 4, 1936, member banks increased their holdings of Government securities from $6½ to $10½ billion, or $4 billion. In the same period the amount they received annually in interest from their holdings of Government securities increased only $40 million, to compensate them for the increased expense involved in handling $4 billion additional assets and deposits. The increase in the interest paid by the Government to the member banks amounted only to 6/100 of one percent of the current national income. The total interest paid by the Government to the member banks amounted only to 4/10 of one percent of the current national income. It is difficult to reconcile these facts with Reverend Coughlin's assertion that "the billions of dollars paid to the bankers in interest is the difference between prosperity and depression". (Lecture December 15, 1935).

To sum up, Congress has not delegated its power to coin money and to regulate the value thereof; it has delegated the administration of this power as it does with all its other powers. It has not delegated the administration of this power to private bankers or private individuals; the administration of monetary powers is carried out by the President, the Secretary of the Treasury and the members of the Board of Governors of the Federal Reserve System, all public officials. The private "ownership" of the Federal reserve banks carries with it no powers of monetary control and no right to earnings in excess of a modest dividend. All profits in excess of this dividend accrue eventually to the Government. The member banks operate under the strict regulation and supervision of public authorities. The return on the private capital invested in member banks is in line with the return on other invested capital. The Government pays lower rates of interest on borrowings from the member banks than from other holders of the Government debt. The total amount paid in interest by the Government to the banks is infinitesimal in comparison with the national income.