

CONFIDENTIAL

DRAFT INCORPORATING SUGGESTED CHANGES TO 11/9/38

The enumeration in the legislation of changes in the existing administrative set-up should be preceded by a preamble or declaration to the effect that it is the purpose of the Congress in enacting the legislation to eliminate unnecessary duplication of effort and expense through the redistribution and coordination of existing activities and that it shall be the duty of the agencies charged with the administration of the Federal banking laws to carry out this purpose in the performance of their respective functions. This preamble or declaration of policy should be broad enough to permit and specific enough to make it clear that the Federal banking agencies under the proposed legislation must make joint use as far as possible of existing facilities and organizations and must not necessarily maintain or establish duplicate facilities and organizations.

With the foregoing purpose in view, the legislative program should include:

I. Termination of the office of the Comptroller of the Currency. - Its currency functions should be transferred to the Treasury of the United States. The supervision which the Comptroller of the Currency now exercises over building and loan associations in the District of Columbia should be transferred to the Home Loan Bank System. The bank examination powers of the Comptroller of the Currency and of the Board of Governors should be transferred to the

Federal Deposit Insurance Corporation with a provision that reports of examination shall include such information as the Board of Governors may require for the performance of its functions. The number of examinations and the frequency with which they are to be made should be in the discretion of the Federal Deposit Insurance Corporation. The powers of the Comptroller of the Currency and of the Federal Deposit Insurance Corporation to require reports should be transferred to the Board of Governors, with provision that there shall be included in such reports information required by the Federal Deposit Insurance Corporation for the performance of its functions. The number of reports and their frequency should be in the discretion of the Board of Governors. All powers of regulation as distinguished from supervision should be vested in the Board of Governors.

In order that the foregoing proposal may be more clearly understood, the following functions would be placed in the Federal Deposit Insurance Corporation:

(a) Chartering of all national banks and admission of all State banks to deposit insurance. In lieu of present rigid statutory capital requirements for chartering national banks and admitting State banks to the Federal Reserve System, the Federal Deposit Insurance Corporation should be authorized to determine in each case the adequacy of the bank's capital on the basis of its

deposit liabilities and other corporate responsibilities. The Corporation, in those cases in which the net sound capital and surplus of an insured bank is less than one-tenth of its liabilities, should have the power to prohibit or limit the payment of dividends by such bank when it finds that its net earnings are insufficient to justify the proposed payment or when in its judgment its existing capital and surplus are inadequate in relation to its deposit liabilities and other corporate responsibilities.

(b) Approval of establishment of branches, domestic and foreign, of all insured banks.

(c) Permission to exercise trust powers by all insured banks.

(d) Supervision of holding company and other affiliates. This supervision should be made applicable to all insured banks upon the same basis and not merely to member banks. The recently prepared draft of proposed holding company legislation should be reviewed and revised to such extent as may seem necessary in the light of experience.

(e) Proceedings for the removal of officers under section 30 of the Banking Act of 1933. This section should be revised so as to make it possible for the Corporation to act on the basis of changes of violations of law and of regulations issued pursuant thereto without the necessity of establishing a repetition of such

violations. Unsafe and unsound practices should be eliminated as grounds for such action and the entire procedure should be consolidated in the Corporation.

(f) Enforcement of the provisions of law containing prohibitions against interlocking directors, officers, and employees of banks and between banks and security companies. The existing provisions of law should be revised so as to make the prohibitions applicable to all insured banks and not merely to member banks.

(g) Enforcement of the prohibition against loans to executive officers.

(h) Enforcement of provisions of law relating to full disclosure in the case of sales of securities or property to banks by bank directors.

(i) Enforcement of prohibition against affiliation of member banks with security companies.

(j) Termination of deposit insurance.

(k) Appointment of receivers and conservators.

(l) Liquidation of insolvent banks.

(m) Approval of capital reductions.

(n) Approval of consolidations, mergers, etc.

As previously stated, all regulatory powers would be vested in the Board of Governors. Among those, which for particular

reasons are mentioned, would be included:

(a) Regulations relating to payment of interest on demand and time deposits, payment of time deposits before maturity, determination of what shall be deemed to be payment of interest, etc. (Now partly in Federal Reserve Board and partly in F.D.I.C.)

(b) Regulations governing the purchase of investment securities. (Now in Comptroller of the Currency)

(c) Collection of reports of condition and other statistical data. (Now in Federal Reserve Board, Comptroller of the Currency and F.D.I.C.)

(d) Regulation of extension of credit accommodations by Federal Reserve banks to insured banks. The present oligibility of the Federal Reserve Act should be eliminated, but the right to fix different rates for different classes of paper should be reserved to the Board. This would require a revision of section 16 of the Federal Reserve Act dealing with the collateral requirements of Federal Reserve notes.

II. Membership in Federal Reserve System. - Distinctions between membership as now constituted in the Federal Reserve System and nonmembership of insured banks should be abolished. All insured banks should be admitted at once to the exercise of all privileges now incident to membership in the System and all insured banks, regardless of membership, should be subjected to the same require-

ments of law and regulations. As a part of this program each existing bank with deposits not exceeding \$1,000,000 and located in a place with population not exceeding 2,500 in which there is now a non-par bank, should be permitted to charge exchange in remitting for checks drawn upon itself and until 1941 other existing banks not now on the par list should be granted the same privilege. It should also be provided that the absorption of such exchange charges by correspondent banks other than Federal Reserve banks should not be deemed to be the payment of interest.

III. Ownership of the Federal Reserve Banks. - The capital stock of the Federal Reserve banks should be retired at par plus accrued dividends, the remaining surplus to constitute the capital of the Federal Reserve banks. Each Federal Reserve bank should then be permitted to accumulate net earnings until an aggregate capital of \$300,000,000 (equitably apportioned among the banks in some manner to be determined) has been accumulated. Thereafter, subject to the creation and maintenance of adequate reserves, each bank should pay all of its earnings to the Government as a franchise tax. As an incident to this capital adjustment all interest of each Federal Reserve bank in the capital stock of the Federal Deposit Insurance Corporation should be transferred to the Treasury and final settlement should be made with the Treasury on advances by it to the Federal Reserve banks under section 13(b) of the Federal

Reserve Act. Provision should be made for the liquidation of loans made under such section and for the discontinuance of this function in the future.

IV. Directorates of Federal Reserve Banks. - The directorate of each Federal Reserve bank should be reduced to seven directors in number, none of whom should be an officer, director, or employee of any bank. Three of such directors, actively engaged in their district in commerce, agriculture or some other industrial pursuit, should be elected by the insured banks of the district, under rules and regulations of the Reserve Board, and one of such directors should be the banking supervisory authority of one of the States comprising the district, similarly elected by the banking supervisory authorities of all of the States comprising such district. The remaining three directors, none of whom should be a stockholder of any bank, should be appointed by the Board of Governors. The term of each director should be for three years and no director should be permitted to serve for more than three full consecutive terms. The election and appointment of directors should be staggered so that in each district all insured banks would elect one director and the Reserve Board would appoint one director each year. The manager of a branch of a Federal Reserve bank should be eliminated as a director of such branch and there should be substituted in his place a director elected by the State banking supervisory

authorities in States served by such branch. The office of the Chairman and Agent of each Federal Reserve bank should be separated and, if present collateral requirements for the issuance of Federal Reserve notes is eliminated, that of Agent should be abolished.

V. Interlocking memberships between Board of Governors of the Federal Reserve System and Board of Directors of the Federal Deposit Insurance Corporation. - The Board of Governors should be reconstituted to consist of seven members as now provided but the Chairman of the Board should serve for a term co-terminous with the term of office of the President and should be an ex officio member of the Board of Directors of the Federal Deposit Insurance Corporation. As a corollary, the Chairman of the Federal Deposit Insurance Corporation should also serve for a term co-terminous with the term of office of the President and should be an ex officio member of the Board of Governors. The remaining five members of the Board of Governors should be appointed for terms of ten years each, so arranged as to require the appointment of a member each two years. Members of the Board should be made continuously eligible for reappointment. The Board should be permitted, except as to actions relating to national or System policy, to allocate particular duties to individual members and to delegate authority to Federal Reserve banks. The Board of Directors of the Federal Deposit Insurance Corporation should

be reconstituted to consist of three members as now provided, but to conform to the above program. The third member of the Board of Directors of the Federal Deposit Insurance Corporation should be appointed by the Secretary of the Treasury. Such appointed member should be permitted to act for the Chairman of the Federal Deposit Insurance Corporation in his ex officio capacity as a member of the Board in his absence, and the Chairman of the Board of Governors should be permitted to select one of the appointed members of the Board to act for him in his ex officio capacity as a member of the Board of Directors of the Federal Deposit Insurance Corporation.

VI. Present Federal Advisory Council and present advisory council of Federal Deposit Insurance Corporation. - The Federal Advisory Council should remain as now constituted and the present de facto advisory body to the Federal Deposit Insurance Corporation, consisting of State bank supervisory authorities, should be made a statutory body under an appropriate name.

VII. Open Market Operations. - The direction and control of open market operations of the Federal Reserve banks should be placed in the Reserve Board and the banks should be authorized to purchase Government securities having maturities not to exceed 90 days from the date of purchase directly from the Treasury. The requirements of the present law whereby the size (?) of the System Open Market Portfolio is published in the weekly statement should

be amended.

VIII. Reserve Requirements. - The statutory reserve requirements should be made uniform for all insured banks, differentiating only between demand deposits and time deposits and having one percentage for time deposits, as for example 5 per cent and one percentage for demand deposits, as for example 15 per cent. However, the Reserve Board should have the authority to classify cities as reserve or central reserve cities and within the limits of the authority granted it in connection with changing reserve requirements should have the authority to prescribe different percentages of reserves to be maintained for different classes of cities. The Reserve Board should have sufficient authority to enable it substantially to absorb all excess reserves created from the importation of gold from abroad. In this connection, the Reserve Board should have authority whereby some control can be exercised over balances of foreign Governments and foreign central banks by permitting the Board to require that such balances be maintained only with Federal Reserve banks. The Board also should have authority to prescribe different and higher reserves for foreign balances. Inter-bank balances should be treated as is now provided but an exemption from the assessment base of the Federal Deposit Insurance Corporation should be provided for all balances carried at a Federal Reserve bank.

IX. Issuance of Currency. - All authority to issue currency should be lodged in the Reserve System and all other outstanding authority to issue circulating notes should be repealed. In this connection, provision should be made for the retirement of United States notes by funds made available by the Treasury out of unused gold certificates or other funds made available from other sources. The present collateral requirements for the issuance of Federal Reserve notes should be repealed as well as the penalty provided for one Federal Reserve bank paying out the notes of another Federal Reserve bank.

X. Silver Purchase Act. - The legislation should provide for the discontinuance of the purchase of silver under the Silver Purchase Act of 1934. Certificates for silver already purchased should be issued to the Reserve System at the cost of such silver to the Treasury and the credit thereby established should be used to retire outstanding silver certificates. The Reserve System should have authority to use such certificates as reserves for the issuance of its notes upon a basis of one to one coverage.

XI. Thomas Amendment. - The Thomas Amendment should be repealed.

XII. Mandate. - Consider the possibility of drafting a form of mandate which will enable the Chairman or the Board, acting through the Chairman, to advise the Chief Executive, or such Board

or Commission as may be established for the purpose, as to the need for action or the exercise of Governmental powers beyond the scope of the Board of Governors with a view to accomplishing the purposes of the Board's monetary policies.