Mr. Marriner Eccles  
Board of Governors  
Federal Reserve System  
Washington, D. C.

Dear Mr. Eccles:

The Subcommittee which has been studying the operations of RFC has concluded its work, and a Bill and Report have been reported out favorably to the Congress by the full Committee. For your information, I enclose herewith copies of the Hearings, the Report, and the Bill.

On behalf of the Subcommittee, I want to thank you for your kindness in considering the problems involved in our study and in giving us the benefit of your views on them.

Sincerely,

C. B. Buck
OPERATIONS OF THE RECONSTRUCTION FINANCE CORPORATION

MARCH 10 (legislative day, FEBRUARY 2), 1948.—Ordered to be printed

Mr. BUCK, from the Committee on Banking and Currency, submitted the following

REPORT

[To accompany S. 2287]

Senate Resolution 132, Eightieth Congress, first session, directed the Committee on Banking and Currency, or any duly authorized subcommittee thereof, to conduct a full and complete inquiry into the operations of the Reconstruction Finance Corporation (hereinafter referred to as “RFC” and “the Corporation”) and its subsidiaries, and to report its findings together with recommendations for such legislation as it deemed advisable not later than March 1, 1948. The time for reporting was extended to April 1, 1948, by Senate Resolution 203, Eightieth Congress, second session. Pursuant to this direction, a subcommittee has held hearings on the operations of RFC. The Committee on Banking and Currency has considered the subcommittee’s findings and recommendations and reports favorably a bill to amend certain sections of the Reconstruction Finance Corporation Act, as amended, and for other purposes, and recommends that the bill do pass.

HISTORY OF RFC

RFC was created by an act approved January 22, 1932. Thereafter its powers and functions were expanded and modified from time to time by amendments to the RFC Act and by separate statutes. Public Law 132, Eightieth Congress, approved June 30, 1947 (hereinafter referred to as the “1947 act”), substantially repealed the prior legislation affecting RFC and provided, in effect, a charter for the Corporation containing its basic authority. Under the 1947 act, the Corporation has succession through June 30, 1948.

Since its inception, the Corporation has performed various types of functions. It has engaged in extensive lending operations; it has been used by the Congress as a ready source of funds for the financing of other Government corporations and agencies, and of projects
carried on under the direction of other governmental departments; it also engaged in extensive operations in support of the war effort.

The act of 1947 removed all of the Corporation's war powers. At the present time, there is no general power given to the Corporation by which it may provide funds for the financing of other Government corporations and the like. Such aid has been provided in specific cases, however, as in the case of the initial financing for the emergency European aid. In that case, the Corporation was authorized by the Congress to make advances not to exceed $150,000,000 at the direction of the President until the necessary appropriations were made. Except for the liquidation of some of its wartime activities, the Corporation's functions have been limited by the 1947 act to lending activities, to the priority purchase of surplus property for small business, and to the operation of its wholly owned subsidiary, Federal National Mortgage Association.

Lending authority prior to 1947 act

The Corporation's lending authority under the legislation applicable prior to the 1947 act, enabled it to extend financial aid to the following types of institutions:

(a) Banks and other financial institutions; (b) railroads; (c) public agencies; (d) business enterprises. It also had authority to make (e) catastrophe loans. Further, the Corporation was authorized to subscribe for the stock of national mortgage associations organized under the National Housing Act. Pursuant to this authority, the Corporation subscribed for the stock of the Federal National Mortgage Association, which made and purchased (f) housing loans secured by mortgages on real estate. RFC also subscribed to the stock of The RFC Mortgage Company, which was organized to assist in establishing a normal mortgage market. Subsequently, The RFC Mortgage Company provided a secondary market for Veterans' Administration guaranteed home loans pursuant to section 2 of Public Law 656, Seventy-ninth Congress, second session. Federal National Mortgage Association has provided a similar market for FHA mortgage loans.

Lending authority under 1947 act

Under the 1947 act, the Corporation's lending authority may be used to aid the following:

(a) Business enterprises, including railroads; (b) financial institutions; and (c) public projects. The Corporation also has authority to make (d) catastrophe loans.

The 1947 act abolished The RFC Mortgage Company. Further, the Corporation's authority to purchase loans insured or guaranteed by the Veterans' Administration was removed. The Federal National Mortgage Association, however, was not disturbed and continues to operate with the authority provided in the National Housing Act. A comparison of RFC's lending authority prior to the 1947 act and under that act shows that the fields in which the Corporation may engage in lending operations remain substantially unchanged. There was, however, one important change in the form in which RFC aid may be provided. Under the prior laws, the Corporation had authority to aid banks and insurance companies in appropriate cases
by the purchase of preferred stock of those institutions. The 1947 act permits aid to such institutions only in the form of loans.

Except in these particulars, (1) the removal of the authority to provide a secondary market for Veterans' Administration-guaranteed home loans, (2) the elimination of the authority to purchase the preferred stock of banks and insurance companies, and (3) the repeal of various provisions under which RFC had made funds available to other Government corporations and departments, the present RFC act of 1947 made no substantial changes in RFC's basic authority, but did constitute a major revision and codification of a considerable number of separate acts all dealing with RFC.

**RFC business loans**

RFC has had authority to make business loans directly, by participations with other institutions, and by agreements to participate. It is important for an understanding of the data contained in the hearings before the subcommittee to understand the nomenclature used to identify these various forms which the business loans have taken. A loan in which RFC disburses the full amount of the loan is called a direct loan. When RFC participates with a bank in making a loan, the bank and RFC both disbursing their respective shares of the total loan, it is called an immediate participation. RFC has also made agreements to participate in business loans by which the originating bank disburses the full amount of the loan and RFC agrees to take up its share of the loan on demand. These are called deferred participations.

In compiling its data, RFC has generally included its immediate participations with its direct loans since both represent actual disbursements by RFC. Data on participations usually refer to the deferred participations unless it is specifically indicated that immediate participations are included.

In addition to the regular deferred participations, RFC has made deferred participations under two plans: The blanket participation agreements (BPA) and the small-loan program (SLP). Under the former, which was instituted in March of 1945 to make credit readily available for the reconversion of industry (hearings, p. 37), RFC entered into agreements with banks by which it agreed to participate up to 75 percent, in any loan made by a bank on the bank's notifying RFC of its desire to obtain the participation. This program was discontinued in January 1947, and the small-loan program was inaugurated in its place. The latter is a simplified procedure, limited to applications for loans of $100,000 and under, in which a bank takes at least 25 percent. The bank, rather than the prospective borrower, makes the application for the participation.

These three types of loans—direct, immediate participations, and deferred participations—are made up of both regular and national defense business loans. This distinction is important because the authority to make national defense business loans did not require that the proposed loan meet the credit standards which were applicable to loans made under the regular business loan authority.

RFC has 31 loan agencies located throughout the country. Applications for business loans are processed originally by one of these local loan agencies which have authority to approve any direct loan
up to $100,000 and any participation loan up to $350,000, provided the participating banks take at least a 25-percent share. All other business-loan applications and all such applications which are declined by the local agency are forwarded to Washington for final consideration (hearings, p. 32).

Each local loan agency has an advisory committee consisting of bankers and businessmen in the area. From time to time some of the members of the local committee meet to pass on applications for direct loans over $50,000 which have been approved by the local loan agency, and on all applications for direct loans exceeding $100,000 whether approved or declined by the agency. The advisory committees pass on deferred participations of the same character except those under the small-loan program which are not passed on by the committees at all (hearings, p. 590).

The business-loan procedures have been described in some detail because, as will appear in the discussion which follows, RFC's present lending activities are confined almost entirely to business loans.

National defense and war activities

Under the national defense powers the Corporation had authority to create corporations for the purpose of producing, acquiring, and carrying strategic materials and of constructing plants to be used in the manufacture of equipment and supplies necessary to the national defense. Pursuant to this authority RFC created the following subsidiaries: Metals Reserve Company to aid in the procurement of strategic metals and minerals; Rubber Reserve Company and Rubber Development Corporation for the purposes of purchasing and stock piling natural rubber, of processing natural rubber from foreign sources, and of operating the synthetic-rubber program; Defense Supplies Corporation to buy, sell, produce, or otherwise deal in strategic and critical materials; and Defense Plant Corporation to construct and acquire the industrial facilities necessary to the national defense. These subsidiaries, except for Rubber Development Corporation, which is now in liquidation, were dissolved into RFC by an act of Congress in 1945.

RFC also operated the War Damage Corporation, U. S. Commercial Company (during part of its existence), and the War Assets Corporation, and performed some of the functions of the Smaller War Plants Corporation which were transferred to it in December of 1945. The issuance of policies under the War Damage Insurance program was terminated in March of 1946. The activities of the U. S. Commercial Company are being liquidated at the present time and that corporation's succession expires on June 30, 1948, under the 1947 act. In March of 1946 the functions of the War Assets Corporation were transferred to the War Assets Administration and the War Assets Corporation was dissolved. The powers which had been transferred from Smaller War Plants Corporation expired by operation of law on December 31, 1946. The only important wartime activities now in operation are the Texas City tin smelter and the synthetic rubber plants. Pursuant to Public Law 125, Eightieth Congress, first session, RFC continues to operate the tin smelter until June 30, 1949. The authority to conduct the synthetic-rubber plants was extended to March 31, 1948, by Public Law 24, Eightieth Congress, first ses-
sion (hearings, p. 249). At the present time, a subcommittee of this committee is engaged in holding hearings on the question of the disposition of these projects. In view of these special studies, the committee has not concerned itself with those activities in this study.

A full discussion of the various powers which RFC has had from time to time is contained in exhibit 3 in the hearings before the subcommittee (p. 153).

GENERAL STATEMENT

RFC was created during a national emergency when many banks were experiencing acute difficulty as a result of a general shrinkage of deposits and a shrinkage in the value of their outstanding loans and investments. Its principal activities in this early period consisted of loans to, and the purchase of preferred stock of, banks and other financial institutions. By December of 1934, these outstanding loans and preferred-stock purchases amounted to $1,724,000,000 (exhibit 5F, hearings, p. 180). The largest amount that RFC has had outstanding in all of its loan categories was $2,288,000,000, in September of 1935 (exhibit 5A, hearings, p. 180).

A graphic picture of the amounts which RFC has had outstanding from time to time in the various loan categories is presented by exhibit 5A (hearings, p. 180). The graph shows that loans to railroads were the second most important activity during those early years.

As of June 30, 1947, disbursements in these two categories, financial institutions and railroads, had amounted to 52 percent of the total disbursements in all loan categories (table 9, hearings, p. 163). However, from June 30, 1945, to October 31, 1947, only two loans were authorized in that first category, these being two loans to one insurance company; and only two were authorized to railroads. During that recent period, RFC's new loans have been limited almost exclusively to loans to business enterprises and to the purchase of Veterans' Administration guaranteed mortgages, this latter authority having been removed by the 1947 act (table 10, hearings, p. 163; exhibit 11, p. 212).

Reasons For Continuing RFC

From the foregoing, it is clear that the need which led to the creation of RFC in 1932 is no longer present, and that continuation of RFC must be justified on a basis other than that upon which its original creation was justified, and with the realization that its activity under conditions prevailing today will be limited principally to loans to business enterprises. The committee has concluded, however, that there are sound reasons which justify the continuation of RFC on a permanent basis. Those reasons may be summarized as follows:

(1) RFC performed an extremely useful and vital function during the emergencies of the last depression and of the war. Should such events recur, the existence of such an agency, already established, will permit more prompt and effective action than would be possible if an agency had to be re-created.

(2) There are some limited functions which such an agency can usefully perform during periods which cannot be characterized as times of economic depression or national emergency.

The hearings held by the subcommittee disclose almost complete unanimity of opinion that RFC performed an extremely useful function
in the depression of the early thirties by the assistance which it gave to
the country's financial institutions. Banks which were in difficulty as
a result of illiquidity of assets were able to obtain loans from RFC
on the security of such assets and thus avoid their costly forced
liquidation. Banks which were forced to write down the value of
their loans outstanding were able to avoid insolvency and a shut-down
by obtaining capital funds through the sale of preferred stock to
RFC. These loans and preferred-stock purchases undoubtedly saved
many of these banks and their depositors from disaster. RFC's
records indicate that this was accomplished without loss to the
Government. Should the economy of the country take such a turn
in the future, the existence of RFC will make it possible for the
Government to provide immediate aid of the type which proved so
beneficial in the thirties.

There is no way of determining whether the extent of that spiral
might have been reduced had RFC aid been provided in the very
early stages. It is probable, however, that such would have been the
case. It is also probable that the same results could have been
achieved with less effort on the part of the Government had such
aid been more timely.

It is difficult, if not impossible, to identify unmistakably the
beginning of such an economic downturn. The possibility that
these signs will be recognized in time to permit re-creation of such
an agency in the early stages when its activities can provide the most
effective relief, is remote enough to make it inadvisable to chance
the country's welfare on the occurrence of that possibility. If, at the
first unmistakable signs of such a cycle, it were necessary for Congress
to reenact RFC legislation and for such an agency to be reestablished
out of whole cloth, the attendant delays could only make the accomplish-
ment of its task more difficult and more costly. The severity which
such cycles have achieved, the alleviation which can result from
Government activity of the nature performed by RFC, and the
possibility that the severity of any such decline may be reduced
through immediate aid by such an agency, make it advisable to
continue RFC as a stand-by against any such contingency. It is
the opinion of the committee that RFC provides an inexpensive
check against such national economic distress.

The fact that RFC was available in 1940 and 1941 to provide
speedy financing without direct appropriation enabled the Government
To proceed rapidly with the preliminary steps necessary for the
country's national defense. Should such an emergency arise again,
the presence of RFC will enable the Congress to act promptly in
taking such steps as appear necessary for the protection of the Nation.

The results of surveys of the Nation's banks and of RFC Advisory
Committee members, which were conducted by the subcommittee's
staff, disclose that banks occasionally decline business loans which a
Government agency may make without competing with private
sources of credit and without exposing the Government to undue
risk of loss of the taxpayers' money (exhibits 38A, 66, hearings,
pp. 472, 590).

Commercial banks are engaged in making loans of moneys which
are deposited with them subject to withdrawal on demand. Since
the deposits are subject to immediate withdrawal, there is a reluctance
on the part of some commercial banks to tie up any large portion of
their depositors' money in long-term business loans. Many of the banker members of the RFC Advisory Committee expressed the opinion that commercial banks cannot properly engage in the making of business loans with maturities of long length, for example, over 5 years, because of the nature of their deposits (hearings, pp. 592-593).

The bank survey shows that banks turn down reasonably sound loan applications for other reasons, which are not directly concerned with the risks involved (hearings, pp. 474-475, 482). It is possible that an applicant, who is turned down by one bank because of one or more of those reasons, may be able to find another bank which will make the loan despite that objection. However, banks rely a great deal on the first-hand knowledge and confidence in their prospective borrowers which they gain as a result of customer relationships with those borrowers. Realistically, therefore, some borrowers may have only their regular banks to which they can look in case of a need for credit.

The extent of such "gaps" in the private credit structure may vary with geographic area, size of borrower, general economic conditions, and so forth. Under present conditions they are probably very small. There are some places, however, where even today a meritorious application is declined. The committee believes that the public interest will be served by the presence of a Government lending agency to which an applicant who has been declined credit among private sources of credit may go for a reconsideration of his proposal.

In the past RFC has made loans to provide funds for public projects such as the San Francisco Bay Bridge and the Pennsylvania Turnpike (hearings p. 431). Such loans have been made on revenue bonds, repayment to be made out of the receipts from tolls. It is not difficult to believe that private capital is frequently reluctant to make the initial investments in such projects. An agency such as RFC can perform a useful public purpose by providing the initial funds for such projects, large and small.

Catastrophes such as the Texas City disaster and the fire at Bar Harbor, Maine, may be visited upon the country at any time. By its catastrophe loans RFC can help to relieve the public hardships attendant upon such disasters.

This discussion of the types of loans which RFC can usefully make in times which cannot be termed "emergency," is not intended to be all-inclusive. However, it will serve to give some indication of the permanent service which such an agency can perform.

Despite the existence of these fields in which RFC may make loans in what might be termed "normal times," the committee believes that the first reason for continuing RFC—its readiness to go into action during times of national emergency—is the far more important one. During times such as the present, characterized by an abundance of funds in the lending institutions of the country, high national employment, high national income, demand for goods in excess of supply, the committee believes that lending by RFC should be curtailed. Applications should be carefully considered to determine whether the interests of the public will be served by extending the financial aid requested. Applications which do not serve those interests should be declined.

The committee has given careful consideration to the problem of continuing RFC on a stand-by basis. Although the opinion that
RFC should be continued as a stand-by organization appears in numerous places in the hearings before the subcommittee, no plan was suggested by proponents of this approach as to how this might be accomplished.

If RFC's lending powers were taken away, it is readily apparent that its organization would stagnate. As a result, its ability to cope with emergencies would be considerably impaired. The committee, therefore, believes it advisable to continue those lending powers, especially since they can be exercised usefully even in normal times, in order that a functioning organization will be preserved.

The legislation dealing with the lending powers might be hedged around with qualifications and conditions. No logical basis has been found, however, in the light of which such qualifications and conditions could be intelligently drafted. The imposition of arbitrary restrictions might reduce the operations to a stand-by basis, but probably at the expense of the efficiency and usefulness of the operations.

The committee has concluded that RFC can perform its intended functions, both in normal times and in emergencies, only if it is equipped with adequate powers unhampered by arbitrary qualifications and conditions. The existing law with the amendments proposed by the committee will, therefore, provide RFC with substantially the same powers as it had during the depression period.

External controls of RFC operations

There are, however, certain controls which the committee believes will have the desired effect of curtailing the Corporation's activities in times such as the present. The first of these is the limitation imposed upon the amount of loans which RFC may have outstanding at any one time. By setting this limitation at a low level Congress can force RFC to operate within limited boundaries. When conditions change so as to require expansion of RFC's activities, this limitation can be raised by the Congress.

The second control is through examination of RFC's activities by Congress. Amendments proposed by the committee require the Corporation to file annual reports with Congress disclosing the operations for the year. These will enable the Congress to keep an eye on the extent of the activities. Further, should the Corporation feel that a raising of the over-all limitation previously discussed is advisable, it will have to present the matter to the Congress, at which time it should be required to show the disposition of its outstanding loans among the various loan categories and to explain fully the necessity for any increase in this limitation. This will provide the Congress with an opportunity to review the activities and the over-all need. It is the belief of this committee that a thorough inquiry into the operations of the Corporation such as was made by the House Committee on Banking and Currency last year and by this committee this year, should be made at least once every 4 years. In this manner Congress can be assured that the activities of the Corporation are accomplishing their purpose and are not exceeding the intended bounds.

The third control is an economic one, the influence of which has already been felt by RFC. During the past 2 years the demand for loans in all fields but the business lending field has declined sharply. This has of necessity resulted in a curtailment of activity.
The fourth control will result from compliance with what this committee believes to be the basic principles which should govern the operations of a Government lending agency such as RFC. Those principles are three in number and are as follows:

First. Such activities should not be carried on in competition with private sources of credit.

Second. In deciding whether to grant a loan, the primary consideration should be the interest of the general public rather than the interest of the individual borrower.

Third. Under normal conditions the activities should be conducted so as to make them self-sustaining insofar as it is possible.

The laws governing RFC have always contained a direction that its financial assistance shall not be extended unless it is not otherwise available on reasonable terms. Our system of free enterprise should not be subject to competition from Government. The above limitation is therefore a vital one.

In the bank survey, the banks were asked if RFC had ever made loans which they were willing and able to make. Only 2.4 percent answered this in the affirmative and only 0.3 percent said that this occurred other than in isolated cases (hearings, p. 479). A good many of the bankers complimented RFC on its compliance with this limitation. In some cases RFC has been able to set up a loan, previously declined by a bank, in such manner that it was able to persuade the bank to make the entire loan (hearings, p. 508). The committee believes that, by and large, RFC has carefully complied with this statutory enjoiner that its aid not be granted unless the credit is not otherwise available.

In the field of deferred participations, however, RFC's activities may have been in direct competition with private sources of credit. In answer to the question, "Does RFC take deferred participations which other (and generally the larger) banks are willing and able to take?" several of the advisory committee members suggested that the participations had never been offered by the originating bank to a correspondent bank, and that in many of those cases correspondent banks would have been willing to take the participations (hearings, pp. 598-599). Comments of a similar nature were made by some of the respondents to the bank questionnaire (hearings, p. 493).

The blanket participation agreements permitted a bank to obtain a deferred participation from RFC without ascertaining whether a correspondent bank might have been willing to participate in the loan. Under the small-loan program, RFC makes no independent check to see if the originating bank has attempted to place the participation with a correspondent (hearings, p. 276). It is therefore possible under the small-loan program for a bank to avoid offering a participation to a correspondent bank.

In the case of a deferred participation, the originating bank disburses the entire loan and is paid interest by the borrower, at 4 percent on that share of the loan for which RFC is obligated under its deferred participation. If RFC's participation is 75 percent of the loan, the bank, at the present time, pays to RFC three-quarters of 1 percent as a fee for the participation until such time as RFC is called upon to disburse its share of the loan to the bank. The bank, therefore, receives a gross return of 3½ percent on the guaranteed portion which is, in effect, money lent on a security of the Government. The
originating bank, however, assumes the expense incident to the making and servicing of the entire loan.

The bank may treat the amounts of its loans which are backed by an RFC deferred participation as though they were cash or Government obligations. These amounts need not be included in determining whether the maximum amount which it may safely lend out at risk has been reached. Therefore, by means of deferred participations a bank may lend out at 4 percent funds which it would otherwise have to maintain in cash or readily convertible Government securities.

If the participation had been taken by a correspondent bank, that bank would actually disburse its portion of the loan. The originating bank would disburse only its portion of the loan and receive only the interest on its share.

From the foregoing, it is apparent that a deferred participation from RFC is more advantageous for a bank than an immediate participation from a correspondent bank. It is, therefore, not difficult to believe that the banks, if permitted to do so, will submit loans to RFC for deferred participation without making a serious effort to obtain a participation from private sources.

Exhibit 5b (hearings, p. 180) shows graphically that the regular business lending of the Corporation, both direct loans and participations, has not varied a great deal since 1938, except for a very great expansion of participations through the blanket participation agreements and the small-loan program, the first of which was inaugurated in March of 1945 (hearings, p. 37). Such a marked increase in the normal business lending may have been the result of a relaxing of the requirement that such participations be unavailable among private sources of credit.

The committee is not opposed to the principle of deferred participations, which are, in effect, loan guaranties. Under that practice a local bank considers the application and approves the loan to the extent that it will risk its own funds for at least a portion of the loan. RFC thereby gains the benefit of the knowledge and experience of the local bank. However, the committee believes that such deferred participations should be made available only when correspondent banks will not take the participation and that the granting of such participations on any other basis is a violation of the provisions of the existing legislation. The practice should be designed to assist the ultimate borrower, who is unable to obtain his entire credit from private sources, and not as a service for the benefit of the banks. The attention of the Corporation's Board of Directors has been called to this situation, and they are being asked to look into the matter and to take such steps as may be appropriate to correct such a condition if in fact it does exist.

RFC has not considered that an applicant is unable to obtain credit from private sources if his only difficulty results from an unwillingness to pay the interest rate at which the credit is available among private sources. Unless the interest rate at which the credit is made available is clearly unreasonable, the Corporation's position in this regard is a proper application of the statutory standard.

The committee believes that the language of the existing legislation is sufficient to proscribe any activity by RFC which might compete with private sources of credit. It is only necessary that there be a strict adherence to that proscription. From time to time Congress should assure itself of that continued adherence.
The second principle which should apply to lending operations by RFC is that, in deciding whether to make or decline a loan, the interest of the public should be considered primary and the personal interests of the particular borrower should be considered secondary. The committee believes that RFC should not engage in lending of a purely private character where the benefit to the general public is remote, whether the loans be large or small. The proposed amendatory legislation authorizes RFC—
to aid in financing agriculture, commerce, and industry; to encourage small business; to help in maintaining the economic stability of the country; and to assist in promoting maximum employment and production.

Each application should be measured against the above-quoted language and considered in the light of this second principle. 

Admittedly the above guide is a broad one. However, it is obvious that the purposes to be served by loans of the type made by RFC cannot be reduced to exact language by which the propriety of each loan can be determined with exactitude. In order to provide the flexibility which is necessary to enable the Corporation to provide financial aid to many types of institutions under widely varying conditions, the definition of the purposes to be served is necessarily broad.

Although the statutory guide contains no express reference to the public interest, it should be apparent that the service of that public interest is the paramount purpose of governmental operations of the nature conducted by RFC. The RFC loan to Glenn L. Martin Co. is a good example of a loan which is serving those interests. The hearings before the subcommittee disclose that the Glenn L. Martin Co. contemplated the construction of aircraft for use by the commercial air lines, that those air lines were and are badly in need of aircraft of the contemplated type, and that Martin's attempts to obtain private financing were extensive but unsuccessful (hearings pp. 319-322, 335-342). RFC made a loan to the Martin Co. to finance the building of the commercial aircraft when the efforts to obtain private financing proved futile. The production of such aircraft should serve the public interest in two ways: It will enable a manufacturing company to keep together a nucleus of personnel whose training and skill will be vital should the country ever again have to begin the large-scale production of aircraft for defense purposes; and it will provide the commercial air-lines industry with a source of much-needed new and modern equipment.

In the case of the Martin loan the interest of the public is readily apparent. In other cases, especially in the smaller loans, the interest of the public will not be so clear. In many cases a loan will not serve a public interest as clearly defined or as national in scope as that served by the Martin loan. In the last analysis the determination of whether or not a particular loan will serve the public interest, must be left to the discretion of the Directors of the Corporation.

In the exercise of this discretion, RFC has decided as a matter of policy not to make loans to the press or radio. It cannot be denied that a loan to a newspaper under certain circumstances might serve a very useful public purpose. It is more important, however, for the Government not to become financially concerned with the success of any industry which is engaged in the exercise of our very jealously guarded rights of freedom of speech and press. The committee be-
believes that RFC should have the discretion to make policy decisions of this character. In isolated cases under the BPA program, RFC has participated in loans to night clubs. It seems to the committee that the public interest is only remotely served by the financing of such places of entertainment. The committee believes that RFC can and should decide as a matter of policy not to engage in financing in fields where the national and local interests of the public are served only remotely.

The committee has considered the problem of coordinating the operations of RFC with the monetary and fiscal policies of the Government. RFC has already proved its willingness and ability to cooperate in the carrying out of those policies. During recent months the Government announced an anti-inflation policy. RFC responded promptly by notifying all of its agency managers that RFC activity should not be permitted to nullify the effect of that policy and that inflationary loans should not be made (hearings, pp. 44-45). If banks, in compliance with a governmental policy of credit restriction, decline loans which they might have made in the absence of such a restriction, it is probable that RFC will receive many more applications than it might otherwise have received. If RFC adheres to the policy of not making inflationary loans, it will find it necessary to decline most if not all of those additional applications. It is believed that the existing legislation, with the proposed amendments, provide a guide by which RFC can coordinate its activities with the credit policies of the Government.

In view of the foregoing, the committee feels that it is unnecessary to impose direct controls on RFC for the purpose of making its operations subject to the policy of the fiscal agencies of the Government, such as the Secretary of the Treasury or the Federal Reserve System. Any such efforts would result in a division of RFC responsibility which the committee believes is undesirable.

Operations should be self-sustaining

The third principle which should govern the operations of RFC is that its lending activities under economic conditions such as prevail today should be conducted, insofar as is reasonably possible, on a self-sustaining basis after taking into consideration the operating expenses and reasonable reserves for losses.

The present law requires that RFC’s loans be “of such sound value or so secured as reasonably to assure retirement or repayment.” The committee believes that a fair application of this standard will yield the desired results.

The three principles just discussed are, in the opinion of the committee, of equal importance. Loans must not be made in competition with private sources of credit. They must meet the requirement that the public interest be served. They must measure up to the credit standards set forth in the act. If an application for financial assistance is deficient in any of these respects, it should be declined despite the fact that it may eminently qualify under the remaining two principles.

Decisions of RFC directors

The responsibility for the application of these three principles lies with the directors of RFC. They should, therefore, be free to use their best judgment in the application of those principles to the loans
which they consider. The danger attendant upon the interference with that exercise of judgment is illustrated by the loan which RFC made to the Lustron Corp. in June of 1947. The loan was made to finance the manufacture of prefabricated houses. RFC agreed to advance $15,500,000 as against the advance of slightly less than a $1,000,000 by the equity interests (hearings, p. 359). Application to RFC for the loan was apparently made at the suggestion of the Housing Expediter. The loan was made by RFC under its national defense authority at the urging of the Housing Expediter who had the authority under the Veterans' Emergency Housing Act to issue directives to other Government agencies to exercise their powers in aid of Veterans' Housing. RFC was undoubtedly motivated by the fact that the Housing Expediter had that authority.

It is the opinion of this committee that, in those fields in which RFC has the responsibility for its actions, it should be allowed to exercise its discretion free from interference by other governmental agencies and departments and, for that matter, free from all influence whether from officials in the Government or from Members of Congress. Only under those circumstances can RFC be expected to do its job properly and with full accountability. Attempts to influence the business judgments of RFC by the use of political influence, even though well intended, are a constant menace to sound administration. While the general policies of the RFC, like those of other Government agencies, should be reviewed and coordinated by the President, this general review should not extend to particular loans. The business decisions of RFC should be the independent judgments of its Board of Directors.

Record of financial success of operations

As previously indicated, the committee believes that RFC should conduct its operations without loss, at least in times like the present. In order that all costs will appear in RFC's statements, the committee is proposing amendments which will reduce the funds which the Corporation uses, without payment of interest to the Treasury, to $100,000,000 of capital and a maximum of $50,000,000 of surplus. Prior to the 1947 act RFC paid a rate of interest on its borrowings from the Treasury which was lower than the average rate at which the Treasury was able to borrow. Section 7 of the 1947 act requires that RFC future borrowings should bear interest at a rate determined by the Secretary of the Treasury after taking into consideration the current average rate on marketable obligations of the United States. This left unchanged RFC's notes in the neighborhood of $1,000,000,000 which were outstanding as a result of the regular lending operations prior to the effective date of that act. In order that RFC's statements may reflect a truer picture of the income or cost to the Government, the committee felt that these old borrowings should bear the current rate of interest paid by the Treasury. RFC has assured the committee that it will renew these notes on the effective date of the proposed amendatory legislation at the going rate of interest.

As a result of these changes, RFC's annual statements will include substantially all the costs involved in the conduct of the operations. It should then be possible to obtain from those statements a true picture of the financial success of the over-all operations. An amendment proposed by the committee requires RFC to include in
its annual reports an analysis of the accumulated net income. This analysis will show the changes in net income as a result of the year's operations.

The committee believes that RFC should maintain its accounts so that the net result of each of its major activities can be readily determined from its annual statements. RFC has not maintained its books in a manner which will permit an appraisal of any particular lending activity. For example, it is not possible to determine with sufficient accuracy what financial success RFC has heretofore enjoyed in the business lending field. An appraisal of that financial success would be especially useful at this time since the bulk of RFC's present activity is in that field.

Reference has previously been made to the fact that the maximum outstanding to banks and other financial institutions at any one time was $1,724,000,000. In contrast, the maximum outstanding at any one time in direct business loans, other than national defense loans, was only $156,000,000 (exhibit 5b, hearings, p. 180). In addition to these direct loans, RFC has had regular deferred participations as well as BPA and SLP deferred participations. These amounted to only $311,000,000 as of June 30, 1947 (exhibit 5a, hearings, p. 180). As of that date, RFC total disbursements (authorizations in the case of deferred participations) in the field of business loans, except for national defense loans, amounted to only 16 percent of RFC's total disbursements in all categories (table 9, hearings, p. 163.)

In view of the foregoing, it is apparent that continuous losses in the field of business lending may have been absorbed by successful operations in the other fields of activity. Therefore, the Corporation's accumulated net income of $550,000,000 as of June 30, 1947, is not, of itself, a satisfactory indication of the financial success of the business lending.

From the results of the bank survey, from the results of a study in 1941 of a sample of RFC business loans, and from the testimony of the RFC Chairman, it appears that RFC borrowers are substandard from the standpoint of bank credit (hearings, pp. 475, 287, 35). The committee believes that the usefulness of RFC's business lending is measured by the success which those borrowers achieve in rehabilitating themselves and in paying off their loans. The success of the borrowers in that regard will be reflected directly in the surplus or deficit which results from the RFC operations. The absence of separate accounting information as to the results of the business lending forecloses an appraisal of the value of RFC's activities in that field in the light of its financial success.

The committee considered a requirement that RFC maintain its financial records in accordance with cost-accounting principles so that such information might be available in the future. RFC has, however, undergone some fundamental changes in its accounting practices in the last 2 years, and has recently undertaken a large-scale plan of decentralization. In view of the foregoing circumstances, the committee has decided against recommending the inclusion in the statute of a mandatory provision for such accounting, and in favor of allowing RFC to complete and absorb its present changes and to set up at its earliest convenience a practical method for ascertaining the net result for each of the major categories of loans and other activities, based upon income, loss, and some appropriate distribution of administrative expense.
Federal National Mortgage Association

The Federal National Mortgage Association was established to assist in the creation of a normal mortgage market, and, to achieve that purpose, it created a secondary market for FHA mortgage loans. The record of its activities for the past few years shows that its activities have been greatly curtailed (hearings, pp. 410, 411). The committee believes that no need exists at the present time for the continuance of its functions, and therefore proposes to dissolve it into RFC. This will relieve RFC of authority to provide a secondary market for Government guaranteed or insured mortgages. The removal of RFC’s authority in this field is not intended to prevent RFC from making loans to business enterprises on the security of real estate, or from granting construction loans for the erection of housing which are secured by mortgages on the housing to be constructed. These loans fall within the business lending authority of the present act.

The committee has some miscellaneous comments and criticisms concerning RFC and related activities. These are discussed in the paragraphs which follow.

Liquidation of loans and investments

As RFC is intended to be merely supplementary to private sources of credit in the country, it is clear that RFC should dispose of loans and investments whenever private sources of credit are willing to take them over. If it can sell an investment, or if a loan can be refinanced so that RFC can be reimbursed for its principal and interest, RFC should make every effort to liquidate its holding. The committee has not considered it advisable to make this mandatory by legislation because there may be circumstances where such disposal might be a distinct disservice to the borrower.

RFC interest rate

The problem of what interest rate RFC should charge is a difficult one. In the past, it has followed the practice of charging a uniform rate, at the present time 4 percent (hearings, p. 65). Interest rates charged by banks, on the other hand, vary, with the credit standing of the borrower and with the size of the loan, from 2 percent to as high as 8 percent (exhibit 64, hearings, p. 588). Interest rates also vary in different geographic areas of the country. Ideally, RFC should charge a slightly higher rate than the going rate for that type of loan in the community of the applicant so that use of RFC facilities will be discouraged when the credit is available elsewhere.

The administrative problem involved in attempting to determine the going interest rates on loans of varying types and sizes and in different geographic areas is clearly a difficult one. Further, such a varying rate could lead to considerable dissatisfaction on the part of borrowers who might feel that RFC had discriminated against them in fixing interest rates on their particular loans. Such dissatisfaction, whether justified or not, should be avoided.

A suggestion was made that the RFC advisory committees, which are composed of private bankers and businessmen in the areas served by the RFC local loan agencies, might establish the schedule of interest
rates for their particular areas. Although this proposal appears to be a reasonable solution, all of its implications cannot be anticipated. The committee has concluded that the difficulties involved in this interest rate problem make it inadvisable to attempt a solution by legislation and that the resolution of the problem should be left to the discretion of the RFC board of directors.

*Number of RFC employees*

According to RFC's 1947 Annual Report, the number of its employees is more than twice what it was in 1938. As the liquidation of the wartime activities is brought to a conclusion, it should be possible to reduce the number of personnel even below the 1938 figures since the current operations of the Corporation will be greatly reduced unless there is marked change in the country's economic condition. There has already been some criticism of the number of employees maintained at some of the local RFC loan agencies (hearings p. 608). It is obvious that excess personnel must be promptly eliminated if RFC is going to retain the necessary efficiency of operation which will be vital in the event of its transformation from normal operations to one of emergency operation.

*Legal opinions concerning extent of RFC authority*

The Corporation has generally relied on the opinions of its general counsel in matters involving the interpretation of the extent of its own powers. In cases of importance where RFC deems it necessary to obtain the advice of counsel on questions involving the extent of its authority or duties, the committee believes that the Corporation should seek an independent opinion. Such questions should be referred to the Attorney General so that his office may consider the question and render an opinion from a disinterested standpoint.

*RFC files and records*

The staff of the subcommittee has reported deficiencies in the records maintained by the Corporation. It is impossible to determine from an examination of the papers in the files of the RFC the whole story of negotiations leading up to its loans. Many conferences are held, of which no record is ever made. In other cases, the results of the conferences are reduced to a memorandum for the private files of the particular employee. Some important documents do not appear in the official files, and unless one knows the identity of every RFC employee who worked on an application, it is practically impossible to determine what information is available bearing on the loan. There has grown up a custom of maintaining "private files" which, while they may be proper in a private organization certainly have no place in a public corporation. The turn-over in the personnel of this public corporation requires a thorough overhauling of its filing system, so that full and complete information may be available in the files for the use of successors and other interested Government officials. No reason exists for incomplete files or failure to include in the files important oral or written transactions bearing on the loans and investments.
Federal Reserve lending authority

By Section 13b of the Federal Reserve Act, the Federal Reserve banks are authorized to make direct loans and to guarantee loans to business enterprises under certain circumstances. Senate bill 408, which has been reported out favorably by this committee, would in effect expand the powers of the Federal Reserve banks to make these loans. This authority is no different from authority which RFC possesses under the RFC Act. The committee believes that there should not be two separate Government agencies engaged in performing identical lending functions. It would be inadvisable to make the Federal Reserve banks the sole agency in that field because this would involve granting to those banks far broader powers than are contained in the present section 13b or in the provisions of S. 408 in order to provide the scope of financial aid which can be afforded by RFC under its various lending powers. The committee has concluded, therefore, that the lending powers granted to the Federal Reserve banks by Section 13b of the Federal Reserve Act should be removed entirely.

RFC Loans to the Baltimore & Ohio Railroad

The committee has held extended hearings concerning loans made by RFC to the Baltimore & Ohio Railroad (hereinafter referred to as the B. & O.), the first of which was in the amount of $7,000,000 and was disbursed April 8, 1932. In 1939, the B. & O. filed its petition for debt readjustment under chapter XV of the Bankruptcy Act. This resulted in a judicially approved plan of readjustment that in effect created a moratorium on a substantial portion of its fixed charges for a period of 6 years. Included in this plan of readjustment was a debt of approximately $85,000,000 due to RFC. The proceedings were before the District Court of the United States for the District of Maryland.

On July 2, 1945, the B. & O. filed in the same district court a second petition under a reenacted chapter XV of the Bankruptcy Act, alleging its inability to meet its debts, matured or about to mature, and seeking approval of a plan of readjustment, dated September 20, 1944. The company stated that it was unable to meet, except through a temporary extension, $13,490,000 principal amount of notes, which would mature August 1, 1944, and would be similarly unable to meet another obligation of $71,083,381 maturing on November 8, 1944. Both of these debts were owing to RFC. The company also stated that it would be unable to meet maturities in 1948, 1950, and 1951 on three large first lien bond issues aggregating in excess of $200,000,000. As to these maturities, the company stated that prospective earnings would not provide cash sufficient to meet them and that it was not believed that refinancing at the respective maturity dates would be possible.

The 1944 plan of readjustment extended the maturity dates of the first mortgage bonds, converted the RFC loan from a note basis to a bond basis, extended the maturity and reduced the interest of the refunding and general mortgage bonds, and provided for the issuance of $25,000,000 of principal amount of new securities to be senior in lien to the refunding and general mortgage bonds. The rights of the holders of the preferred and common stock remained unchanged. As an intervening party in interest, Randolph Phillips appeared and
objected to this plan of readjustment, charging that the petition had not been brought in good faith by the B. & O. and that the financial condition of the company made it unnecessary. After hearing the special three-judge court, composed of Circuit Judges Morris A. Soper and Armistead M. Dobie and District Judge W. Calvin Chesnut, approved the plan in an opinion dated November 20, 1945, confirming the same by a final decree dated March 13, 1946.

In connection with the proposed extension of RFC, the committee inquired into the circumstances of the loan to the B. & O. and of the 1944 plan of readjustment. Hearings before the full committee were held on April 10, 11, 29 and 30, and May 5, 6, 22 and 23 in 1947. The central question turned on whether the petition had been filed in good faith, and without collusion between officials of the B. & O. and RFC. In substance, the charges considered by the committee were that the B. & O. had falsified its corporate records to indicate that the 1944 plan of readjustment had been conceived in that year and not in 1942; that there had been collaboration between the officials of the B. & O. and of the RFC; that the B. & O. had misstated its financial condition and had diverted funds otherwise available for the payment of the RFC obligation; that the B. & O. had altered its minutes with respect to the amount of working capital required; and that various other improprieties existed, relating to collusion between officials of the B. & O. and the RFC.

It is characteristic of a reorganization that some or all creditors must forego a portion of their existing rights in the interest of establishing the company in reorganization on a sounder financial basis. From this viewpoint, the RFC did not seriously suffer in reorganization, except as it may have done so by giving up secured notes in exchange for bonds payable in 1965. While the RFC received no additional security or better lien position, the collateral securing the bonds was the same as that securing the notes. Perhaps the most serious disadvantage sustained by RFC in the reorganization was its surrender of the possession and control of this collateral, with the right to dispose of it by sale. In the reorganization, there was an extension of the maturity dates of all issues.

One of the many serious factors which makes it difficult to evaluate the facts on which the charges of bad faith are based, arises from the circumstance that several former employees of RFC were officials of the B. & O. at the time of the negotiations relating to the 1944 plan of readjustment, notably Russell L. Snodgrass, vice president of the B. & O. in charge of finance, and Cassius M. Clay, general solicitor of the B. & O. Mr. Clay resigned his position as general solicitor on September 15, 1945, giving as his ground for doing so his disapproval of the plan for readjustment, which he characterized as a "fraud upon the court."

The hearings before the committee were published in August 1947. On September 3, 1947, Randolph Phillips filed a motion to vacate the decree of the district court, which had approved the plan of readjustment. In his motion, Mr. Phillips, as an intervening party in interest, alleged that the judgment had been procured by fraud upon the court, as he had previously contended, and that the hearings before the Senate Banking and Currency Committee placed in his possession newly discovered evidence of fraud unknown to him at the time of the prior hearings which preceded the court's approval of the plan. In support of his charges, Mr. Phillips offered in evidence the hearings.
before the Senate Banking and Currency Committee. The special
three-judge court denied the motion to vacate the decree and in its
order made the following finding:

All the allegations of fact in the motion, when taken together and considered
in the light of the testimony taken during the hearing of the case, are insufficient
to establish the charge of fraud or to justify the court in reopening the case and
reviewing its decision.

Mr. Phillips petitioned to the Supreme Court of the United States,
October term, 1947, No. 442 for a writ of certiorari to the United
States District Court for the District of Maryland. This petition
was denied in January 1948 and a petition for rehearing filed by Mr.
Phillips on January 15, 1948, has also been denied.

On January 16, 1948, the subcommittee of the Senate Banking and
Currency Committee which has been conducting this inquiry into the
operations of RFC, incorporated by reference in its records the pro-
ceedings before the full committee on the RFC loans to the B. & O.
which have been studied primarily for their value in the general
inquiry which the subcommittee has been making to determine the
present and future usefulness of RFC. Since the adjudication of the
District Court of the United States for the District of Maryland has
considered and passed upon the specific charges of fraud considered
in the Senate Banking and Currency Committee hearings, the com-
mittee believes that no further action regarding the B. & O. loan
transaction can be appropriately taken by it and accordingly declares
that the hearings on this subject be closed with this report of the
proceedings.

EXPLANATION OF THE AMENDMENTS BY SECTIONS

SECTION 1

This section amends Section 1 of the RFC Act. The existing pro-
visions are designated as subsection (a), and new subsections (b) and
(c) are added.

The capital stock of the Corporation is reduced from $325,000,000
to $100,000,000. The purpose of this is to reduce the amount of
money which the Corporation uses without the payment of interest
so that the Corporation's statements will more nearly reflect the actual
cost to the Government of conducting the operations.

The new subsection (b) requires RFC to submit to the Congress
an annual report of its operations, including a balance sheet, a state-
ment of income and expense, an analysis of accumulated net income
or deficit, and a schedule showing the names of borrowers to whom
RFC has made a direct loan or a participation loan of $100,000 or
more, whether in the form of a direct loan, a purchase of a participa-
tion, an agreement to participate, or a purchase of an investment or
obligation. This report will enable the Congress to appraise the
operations of the Corporation each year. A new provision has been
included which requires the Corporation to pay to the Treasury each
year as a dividend, the amount by which its accumulated net income
exceeds $50,000,000. As the Corporation has $100,000,000 in
capital funds for which it pays no interest, the committee feels that
any net income after provision for reasonable reserves should be
returned to the Government as a return on the capital funds. The
accumulation of net income permits the Corporation to use that
amount of money without charge. The committee believes that more
economical operation may result if that “free money” is not allowed to accumulate. Further, a truer cost picture of the operations will be presented by the statements in the RFC reports, if the amount of capital which RFC uses free of interest is kept at a low figure. The Corporation is allowed to retain $50,000,000 in accumulated net income to act as a buffer against future losses which might impair its capital. Since the Corporation had $1,331,000,000 outstanding in its various loan categories on June 30, 1947, it appears reasonable to allow it to retain that amount, even though it has a reserve for losses of $100,000,000.

Subsection (c) provides for the retirement of the Corporation’s present capital stock in excess of the $100,000,000 which is authorized under the amended subsection (a).

SECTION 2

This section amends section 2 of the RFC Act. The third sentence has been rewritten to make clear that the office of director of the Corporation is a full-time position. The terms of the present directors are extended to June 30, 1950, to make their terms of office coextensive with the Corporation’s fiscal year. Provision is made for staggering the terms of the directors thereafter with the ultimate term of office extended from 2 to 3 years. The committee believes that a longer term will help the Corporation to attract and hold the caliber of men necessary for the successful operation of the Corporation. Staggering of the terms of office will insure some continuity of management. It is also proposed that the President shall, after confirmation of the directors by the Senate, designate one of the directors as chairman to serve for a period coextensive with his term as director.

SECTION 3

This section amends section 3 (a) of the RFC Act. The succession of the Corporation is extended from June 30, 1948, to June 30, 1960. As the committee believes that RFC should be continued on a permanent basis, it is recommending that RFC be given a long period of succession in order that it may give assurance of extended employment to competent personnel. The committee is recommending that the powers of the Corporation be extended to 1958. A limit is placed thereon to insure that Congress will review this entire problem at that time. It was thought inadvisable to grant perpetual succession when the powers are being so limited.

The position in the section of provisions which accord RFC the same immunities and exemptions from the payment of costs, charges, and fees in court proceedings as are granted to the United States and which accord it the usual privileges with respect to use of the mails, has been changed.

Because of recent United States Supreme Court decisions it may be that RFC is entitled under the present law to the same priority in bankruptcy which is enjoyed by the United States. The committee believes that RFC should not have this priority with respect to the recovery of funds advanced under its regular lending operations. A sentence is therefore added to this section which will remove that priority except with respect to obligations owed to RFC as a result of certain of its wartime activities.
SECTION 4

This section amends section 4 of the RFC Act. The phrase "to encourage small business" has been added to the purposes set forth in the introduction to subsection (a). This is not intended to restrict RFC's aid to the field of small business, but the committee believes that it should be made clear that RFC aid is intended to be available to small business.

A new provision is added to subsection (a) (2), which restores to RFC the authority to buy the preferred stock of banks and insurance companies on certification by the Secretary of Treasury that funds are needed by such corporation for capital purposes. RFC used this power extensively during the depression of the thirties. At one time it had over $1,000,000,000 outstanding in such preferred stock issues. This has been reduced to a little under $150,000,000 (hearings, p. 221). It is apparent that this power was extremely useful in the rehabilitation of the banks during that period and the subcommittee feels that RFC should possess that power in the event there should be a recurrence of those conditions.

Loans to banks and insurance companies are useful where those institutions are experiencing illiquidity of assets. Where those institutions are forced to write down the value of their assets, as occurred during the depression of the early thirties, the problem is one of solvency, not liquidity. In that situation a loan is of no assistance since the new cash is equaled by a new liability in the same amount. A purchase of preferred stock, on the other hand, permits an increase in the assets with no increase in liabilities.

It is intended by the committee that this power should be used in emergencies only. It is not a means by which those institutions can obtain equity financing in the usual sense, but a means whereby the Corporation can lend money in appropriate cases where aid in the form of a loan would not accomplish the desired purposes. RFC should have little occasion to use this power unless there should be a recurrence of the conditions which led to the use of the power in the past depression. The requirement of a certification by the Secretary of the Treasury should tend to prevent the exercise of this authority unless a real justification for its exercise is present.

Subsection (a) (3), which authorizes RFC to make loans to aid in financing public projects, is amended to permit the extension of that aid to States as well as to municipalities and subdivisions of States as is presently provided in the section. No logical reason appears why these loans should not be made to States. The committee gave consideration to a requirement that these loans be self-liquidating but concluded that this would be too restrictive. This authority contemplates, in general, projects which are self-liquidating in whole or in part, or which are revenue producing in whole or in part, or which are to be financed, in whole or in part, by taxes or assessments resulting directly or indirectly from the project.

The provisions of the present subsection (b) are designated as subsection (b) (1) and new subsections (2), (3), and (4) are added. Subsection (2) requires that RFC's loans (except catastrophe loans) shall bear an interest rate reasonably calculated to enable the Corporation to operate without loss. Fees charged for deferred participations are required to be at rates which will give reasonable assurance that those operations will be conducted without loss. At the present
time RFC charges varying rates for its deferred participations depending upon the percentage of its participation. Its fee for a 75-percent participation is three-fourths of 1 percent. Because of the relative newness of that activity on a large scale, RFC has had insufficient experience upon which to determine the soundness of its deferred participation fees. It has, however, incurred obligations on such participations in excess of $1,000,000,000. The fees which it has collected for these deferred participations total $4,400,000 (hearings, pp. 427-428). This return of less than half of 1 percent on the total of outstanding liabilities seems hardly adequate to cover the expenses of the program and a reasonable reserve for the potential losses. It has already been pointed out that the originating banks may be enjoying an unusually large return on these arrangements. It is certainly not intended that RFC’s operations should be conducted at a loss in order to increase the return to the banks. The committee has therefore felt it advisable to include a provision requiring that the fees be such that the operations can be conducted with the expectation that they will be self-sustaining.

Subsection (b) (3) provides that maturities for loans to business enterprises and to financial institutions and for catastrophe loans shall not be longer than 10 years. Business loans made prior to July 1, 1947, may be renewed or extended for periods not to exceed a total of 10 years. In the case of the purchase of capital notes or debentures of banks and insurance companies or of loans secured by preferred stock, capital notes or debentures of those institutions, the maturity period may be 20 years. This is the period which was used by RFC in most cases during the 1930's. Prior to the 1947 act there was no maturity limitation on the Corporation’s business loans and loans to public agencies because of a clause in section 5d of the old RFC Act. The elimination of this clause in the comparable section of the 1947 act and the failure to repeal a general maturity provision in a 1935 act has resulted in a situation in which under the present law maturities may not extend beyond January 31, 1955. Such a maturity deadline is purely arbitrary and has no relation to the purpose which RFC is intended to serve. The committee recommends a limitation of 10 years because it believes that that will allow RFC to engage in longer-term financing where a need for such aid exists, and yet will tend to prevent the supplying of capital funds which is really the task of private investors. This limitation does not apply to securities or obligations received in bankruptcy reorganization or receivership. Financial assistance in aid of public projects may carry a maturity up to 40 years. It is obvious that projects of this character cannot be financed over a period as short as 10 years.

Subsection (b) (4) limits RFC’s deferred participations to 65 percent in loans of $100,000 and under, and to 50 percent in loans over $100,000. Since the originating bank disburses the full amount of such a loan and continues to handle the servicing of the entire loan, the committee believes it advisable to limit this practice to cases where the originating bank takes a large enough share to insure that it will give consideration to the loan in a degree commensurate with the amount involved. A distinction is made in favor of loans of $100,000 and under in order to make the practice more attractive in the field of smaller business where the need for credit appears to be greater.
Subsection (c) reduces the maximum amount which the Corporation may have outstanding at any one time in loans under the 1947 act (since June 30, 1947) from $2,000,000,000 to $1,000,000,000. In the 2 years from June 1945 to June 1947, RFC disbursed only $30,000,000 in all loan categories other than the business-loans category (table 10, hearings, p. 163). It is readily apparent that there is no large demand at this time for these types of loans, i.e., loans to financial institutions, railroads, and public agencies, and catastrophe loans. The maximum which RFC has ever had outstanding in the business loan field was about $900,000,000 in June of 1943. This included direct loans, participations, and direct loan commitments (for all categories), both regular and national defense (exhibit 5b, hearings, p. 180). It is readily apparent that under present conditions the amount of RFC's loans to business enterprises should be greatly reduced from the maximum which occurred in the middle of the period of war financing.

The committee believes that the foregoing figures demonstrate clearly that a $1,000,000,000 ceiling not only will permit the Corporation to conduct its operations effectively under present-day circumstances but also will leave a substantial cushion upon which the Corporation may call in the event of a sudden change in economic conditions requiring immediate extensive action. Loans made prior to July 1, 1947, which are renewed or extended pursuant to the new provision in section 4 (b) (3), are not intended to be included under this ceiling except to the extent that any new funds are disbursed.

Subsection (f) is amended to extend the Corporation's powers from June 30, 1948, to June 30, 1958.

No changes in the remaining subsections are proposed.

SECTION 5

This section amends section 203 of the 1947 act by adding a new provision dissolving the Federal National Mortgage Association.

SECTION 6

This section amends the repealer section of the 1947 act by adding for repeal two sections of the act approved January 31, 1935. The first section limited disbursements on a commitment to 1 year following the date of the commitment. The value of such a provision is doubtful and it does have definite disadvantages. In the case of deferred participations, this provision would require RFC to disburse its share within a year. In the opinion of the committee it is better that the financing should be continued by the originating bank as long as possible. Further, in the case of large construction loans, the full amount of the funds are oftentimes not required in the first year of construction. A requirement which results in the funds being disbursed before they are needed is unwise from the standpoint of sound credit practice. The committee therefore recommends the repeal of that section. The second of these sections to be repealed provided that RFC maturities should not extend beyond 1955. This arbitrary limitation is repealed and the maturity limitations provided for in section 4 (b) (3) hereof are enacted in its place.
This section repeals section 208 of the 1947 act, thereby removing RFC's authority to purchase, under a Government agency priority, surplus property for small business. The committee believes that this provision should be eliminated partly because this has resulted in some cases in giving priority to some small business at the expense of other small business, but principally because the benefits to be achieved by the section have already been attained.

The Corporation's budget for 1949 discloses that these purchases amounted to $54,000,000 during 8 months of the fiscal year 1947. The estimate for the current year is $25,000,000, while the estimate for next year is only $3,000,000.

This section merely changes the dates in section 209 of the 1947 act to authorize the Corporation to use its general funds to pay administrative expenses in the event that appropriation legislation is not enacted by the end of this fiscal year. It is not expected that that will occur, but no harm is done in taking this precaution.

This section changes a paragraph in section 24 of the Federal Reserve Act by striking out a reference to participations by RFC under provisions “of section 5d” of the RFC Act. That section contained the lending authority of RFC. The comparable section of the 1947 act is section 4 (a). The question has arisen as to whether this provision of the Federal Reserve Act is effective any longer since, literally speaking, there are no participations made today under section 5d. By striking out the reference to “section 5d,” section 24 of the Federal Reserve Act will have the same effect as it had prior to the 1947 revision of the RFC Act.

Section 24 of the Federal Reserve Act authorizes national banks to make real-estate loans. The amounts of such loans may not exceed 50 percent of the appraised value of the real estate except that the loans may be in an amount not to exceed 60 percent if the obligation provides for amortization of 40 percent or more. Section 328 of the Banking Act of 1935 added a paragraph to this section 24 excepting loans “to established industrial or commercial businesses” from the foregoing provisions in certain cases, one of them being the situation in which RFC “cooperates or purchases a participation under the provisions of section 5d of” the RFC Act. The proposed amendment merely gives effect to this exception in section 24 of the Federal Reserve Act by eliminating the incongruous reference to “section 5d.”
IN THE SENATE OF THE UNITED STATES

MARCH 10 (legislative day, February 2), 1948

Mr. Buck, from the Committee on Banking and Currency, reported the following bill; which was read twice and placed on the calendar

A BILL

To amend the Reconstruction Finance Corporation Act, as amended, and for other purposes.

1 Be it enacted by the Senate and House of Representatives of the United States of America in Congress assembled,

2 That section 1 of the Reconstruction Finance Corporation Act, as amended, is amended to read as follows:

3 "Sec. 1. (a) There is hereby created a body corporate with the name 'Reconstruction Finance Corporation' (herein called the Corporation), with a capital stock of $100,000,- 000 subscribed by the United States of America. Its principal office shall be located in the District of Columbia, but there may be established agencies or branch offices in any
city or cities of the United States under rules and regula-
tions prescribed by the Board of Directors. This Act may
be cited as the 'Reconstruction Finance Corporation Act'.

"(b) Within six months after the close of each fiscal
year the Corporation shall make a report to the Congress
of the United States which shall contain financial statements
for the fiscal year, including a balance sheet, a statement
of income and expense, and an analysis of accumulated net
income. The accumulated net income shall be determined
after provision for reasonable reserves for uncollectibility of
loans and investments outstanding. Such statements shall
be prepared from the financial records of the Corporation
which shall be maintained in accordance with generally
accepted accounting principles applicable to commercial cor-
porate transactions. The report shall contain schedules
showing, as of the close of the fiscal year, each direct loan
to any one borrower of $100,000 or more, each loan to
any one borrower of $100,000 or more in which the Cor-
poration has a participation or an agreement to participate,
and the investments in the securities and obligations of any
one borrower which total $100,000 or more. After the end
of each fiscal year, beginning with the fiscal year ended
June 30, 1948, the Corporation shall pay over to the
Secretary of the Treasury as miscellaneous receipts, a divi-
dend on its capital stock owned by the United States of
America, in the amount by which its accumulated net income exceeds $50,000,000.

"(c) Within sixty days after the effective date of this amendment, the Corporation shall retire all its outstanding capital stock in excess of $100,000,000 and shall pay to the Treasury as miscellaneous receipts the par value of the stock so retired."

SEC. 2. Section 2 of the Reconstruction Finance Corporation Act, as amended, is amended to read as follows:

"SEC. 2. The management of the Corporation shall be vested in a board of directors consisting of five persons appointed by the President of the United States by and with the advice and consent of the Senate. Of the five members of the board, not more than three shall be members of any one political party and not more than one shall be appointed from any one Federal Reserve district. The office of director shall be a full-time position. The term of the incumbent directors is hereby extended to June 30, 1950. As of July 1, 1950, two directors shall be appointed for a term of one year, two directors shall be appointed for a term of two years, and one director shall be appointed for a term of three years. Thereafter the term of the directors shall be for a term of three years, but they may continue in office until their successors are appointed and qualified.

Whenever a vacancy shall occur in the office of director other
than by expiration of term, the person appointed to fill such vacancy shall hold office for the unexpired portion of the term of the director whose place he is selected to fill. After the confirmation of the directors by the Senate, the President shall designate one of the directors to serve as chairman for a period coextensive with his term as director. The directors, except the chairman, shall receive salaries at the rate of $12,500 per annum each. The chairman of the board of directors shall receive a salary at the rate of $15,000 per annum."

SEC. 3. Section 3 (a) of the Reconstruction Finance Corporation Act, as amended, is amended to read as follows:

"SEC. 3. (a) The Corporation shall have succession through June 30, 1960, unless it is sooner dissolved by an Act of Congress. It shall have power to adopt, alter, and use a corporate seal; to make contracts; to lease or purchase such real estate as may be necessary for the transaction of its business; to sue and be sued, to complain and to defendant, in any court of competent jurisdiction, State or Federal; to select, employ, and fix the compensation of such officers, employees, attorneys, and agents as shall be necessary for the transaction of the business of the Corporation, in accordance with laws, applicable to the Corporation, as in effect on June 30, 1947, and as thereafter amended; and to prescribe, amend, and repeal, by its board of directors, bylaws,
rules, and regulations governing the manner in which its
general business may be conducted. Except as may be
otherwise provided in this Act or in the Government Corpo-
ation Control Act, the board of directors of the Corpora-
tion shall determine the necessity for and the character and
amount of its obligations and expenditures under this Act
and the manner in which they shall be incurred, allowed,
paid, and accounted for, without regard to the provisions of
any other laws governing the expenditure of public funds,
and such determinations shall be final and conclusive upon
all other officers of the Government. The Corporation shall
be entitled to and granted the same immunities and exemp-
tions from the payment of costs, charges, and fees as are
granted to the United States pursuant to the provisions of
law codified in sections 543, 548, 555, 557, 578, and 578a
of title 28 of the United States Code, 1940 edition. The
Corporation shall also be entitled to the use of the United
States mails in the same manner as the executive depart-
ments of the Government. Debts due the Corporation,
whether heretofore or hereafter arising, shall not be entitled
to the priority available to the United States pursuant to
section 3466 of the Revised Statutes (U. S. C., title 31,
sec. 191) except that the Corporation shall be entitled to
such priority with respect to debts arising from any trans-
action pursuant to any of the following Acts or provisions
6

in effect at any time: Sections 5d (1) and 5d (2) of the
Reconstruction Finance Corporation Act added by section
5 of the Act entitled ‘An Act to authorize the purchase by
the Reconstruction Finance Corporation of stock of Federal
home-loan banks; to amend the Reconstruction Finance
Corporation Act, as amended, and for other purposes’, ap-
proved June 25, 1940 (54 Stat. 573); sections 4 (f)
and 9 of the Act entitled ‘An Act to mobilize the productive
facilities of small business in the interests of successful prose-
cution of the war, and for other purposes’, approved June
11, 1942 (56 Stat. 354, 356); section 2 (e) of the Emer-
gency Price Control Act of 1942 (56 Stat. 26); the Surplus
Property Act of 1944 (58 Stat. 765 and the following);
sections 11 and 12 of the Veterans’ Emergency Housing
Act of 1946 (60 Stat. 214, 215); and section 403 of the
Sixth Supplemental National Defense Appropriation Act
(56 Stat. 245).”

SEC. 4. Section 4 of the Reconstruction Finance Corpo-
ration Act, as amended, is amended to read as follows:

“SEC. 4. (a) To aid in financing agriculture, commerce,
and industry, to encourage small business, to help in main-
taining the economic stability of the country, and to assist
in promoting maximum employment and production, the
Corporation, within the limitations hereinafter provided, is
authorized—
“(1) to purchase the obligations of and to make loans to any business enterprise organized or operating under the laws of any State or the United States: Provided, That the purchase of obligations (including equipment trust certificates) of, or the making of loans to, railroads or air carriers engaged in interstate commerce or receivers or trustees thereof, shall be with the approval of the Interstate Commerce Commission or the Civil Aeronautics Board, respectively: Provided, further, That in the case of railroads or air carriers not in receivership or trusteeship, the Commission or the Board, as the case may be, in connection with its approval of such purchases or loans, shall also certify that such railroad or air carrier, on the basis of present and prospective earnings, may be expected to meet its fixed charges without a reduction thereof through judicial reorganization except that such certificates shall not be required in the case of loans or purchases made for the acquisition of equipment or for maintenance.

“(2) to make loans to any financial institution or insurance company organized under the laws of any State or of the United States. If the Secretary of the Treasury certifies to the Corporation that any bank or trust company, under the supervision of the Comptroller of the Currency or a State banking department, or any
insurance company, is in need of funds for capital purposes, the Corporation may subscribe for or make loans upon nonassessable preferred stock in such bank or trust company or insurance company. In any case in which, under the laws of the State in which it is located, such institutions so certified are not permitted to issue nonassessable preferred stock, or if such laws permit such issue of preferred stock only by unanimous consent of stockholders, the Corporation is authorized to purchase the legally issued capital notes or debentures of such institutions.

“(3) in order to aid in financing projects authorized under Federal, State, or municipal law, to purchase the securities and obligations of, or make loans to, (A) States, municipalities, and political subdivisions of States; (B) public agencies and instrumentalities of one or more States, municipalities, and political subdivisions of States; and (C) public corporations, boards, and commissions: Provided, That no such purchase or loan shall be made for payment of ordinary governmental or non-project operating expenses as distinguished from purchases and loans to aid in financing specific public projects;

“(4) to make such loans, in an aggregate amount not to exceed $25,000,000 outstanding at any one time,
as it may determine to be necessary or appropriate because of floods or other catastrophes.

"(b) The powers granted in section 4 (a) of this Act shall be subject to the following restrictions and limitations:

"(1) No financial assistance shall be extended pursuant to paragraphs (1), (2), and (3) of subsection (a) of this section, unless the financial assistance applied for is not otherwise available on reasonable terms. All securities and obligations purchased and all loans made under paragraphs (1), (2), and (3) of subsection (a) of this section shall be of such sound value or so secured as reasonably to assure retirement or repayment and such loans may be made either directly or in cooperation with banks or other lending institutions through agreements to participate or by the purchase of participations, or otherwise.

"(2) All such loans made, or obligations and securities purchased under section 4 (a) (1), (2), and (3), shall bear such interest or yield such return as to be reasonably calculated to enable the Corporation to operate without loss. The fees charged for agreements to participate in loans shall be at such rates as reasonably to assure the Corporation that these operations will be conducted without loss. Loans made under section
4 (a) (4) shall bear interest at such rates as the Corporation may determine.

"(3) No loan, including renewals or extensions thereof, may be made under sections 4 (a) (1), (2), and (4) for a period or periods exceeding ten years, and no securities or obligations maturing more than ten years from date of purchase by the Corporation may be purchased thereunder, except that capital notes and debentures purchased, and loans made on preferred stock, capital notes or debentures, under section 4 (a) (2) may have maturities not to exceed twenty years: Provided, That the foregoing restriction on maturities shall not apply to securities or obligations received by the Corporation as a claimant in bankruptcy or equitable reorganization: Provided further, That any loan made to a business enterprise prior to July 1, 1947, may, in aid of orderly liquidation thereof or the interest of the national security, be renewed or extended for such period not in excess of ten years and upon such terms as the Corporation may determine. The Corporation may, in carrying out the provisions of subsection 4 (a) (3), purchase securities and obligations, or make loans, including renewals or extensions thereof, with maturity dates not in excess of forty years, as the Corporation may determine.
“(4) In agreements to participate in loans, wherein the Corporation’s disbursements are deferred, such participations by the Corporation shall be limited to 65 per centum of the balance of the loan outstanding at the time of the disbursement, in those cases where the total amount borrowed is $100,000 or less, and shall be limited to 50 per centum of the balance outstanding at the time of disbursement, in those cases where the total amount borrowed is over $100,000.

“(c) The total amount of investments, loans, purchases, and commitments made subsequent to June 30, 1947, pursuant to section 4 shall not exceed $1,000,000,000 outstanding at any one time.

“(d) No fee or commission shall be paid by any applicant for financial assistance under the provisions of this Act in connection with any such application, and any agreement to pay or payment of any such fee or commission shall be unlawful.

“(e) No director, officer, attorney, agent, or employee of the Corporation in any manner, directly or indirectly, shall participate in the deliberation upon or the determination of any question affecting his personal interests, or the interests of any corporation, partnership, or association in which he is directly or indirectly interested.

“(f) The powers granted to the Corporation by this
section 4 shall terminate at the close of business on June 30, 1958, but the termination of such powers shall not be construed (1) to prohibit disbursement of funds on purchases of securities and obligations, on loans, or on commitments or agreements to make such purchases or loans, made under this Act prior to the close of business on such date, or (2) to affect the validity or performance of any other agreement made or entered into pursuant to law.

“(g) As used in this Act, the term ‘State’ includes the District of Columbia, Alaska, Hawaii, and Puerto Rico.”

SEC. 5. Section 203 of title II of the joint resolution entitled “Joint resolution to extend the succession, lending powers, and the functions of the Reconstruction Finance Corporation”, approved June 30, 1947 (Public Law 132, Eightieth Congress), is amended (a) by inserting, immediately after “Sec. 203”, “(a)”, and (b) by adding at the end thereof the following:

“(b) All assets and liabilities of every kind and nature, together with all documents, books of account, and records, of the Federal National Mortgage Association, a corporation organized under title 3 of the National Housing Act, all the capital stock of which is owned and held by Reconstruction Finance Corporation, are hereby transferred to Reconstruction Finance Corporation and the said Federal National Mortgage Association is hereby dissolved. With respect to
the assets, liabilities, and records transferred, ‘Reconstruction
Finance Corporation’ for all purposes is hereby substituted
for ‘Federal National Housing Association’, and no suit,
action, or other proceeding lawfully commenced by or against
such corporation shall abate by reason of the enactment of
this Act, but the court, on motion or supplemental petition
filed at any time within twelve months after the date of
such enactment, showing a necessity for the survival of such
suit, action, or other proceeding to obtain a determination
of the questions involved, may allow the same to be main-
tained by or against Reconstruction Finance Corporation.”

SEC. 6. Subsection (m) of section 206 of title II of
the joint resolution entitled “Joint resolution to extend the
succession, lending powers, and the functions of the Recon-
struction Finance Corporation”, approved June 30, 1947
(Public Law 132, Eightieth Congress), is amended to read
as follows:

“(m) The first section and sections 2, 3, 9, 11, and 13
of the Act approved January 31, 1935 (49 Stat. 1), as
amended.”

SEC. 7. Section 208 of title II of the joint resolution
entitled “Joint resolution to extend the succession, lending
powers, and the functions of the Reconstruction Finance
Corporation”, approved June 30, 1947 (Public Law 132,
Eightieth Congress), is hereby repealed.
SEC. 8. Section 209 of title II of the joint resolution entitled "Joint resolution to extend the succession, lending powers, and the functions of the Reconstruction Finance Corporation", approved June 30, 1947 (Public Law 132, Eightieth Congress), is amended to read as follows:

"SEC. 209. During the period between June 30, 1948, and the date of enactment of legislation making funds available for administrative expenses for the fiscal year ending June 30, 1949, the Corporation is authorized to incur, and pay out of its general funds, administrative expenses in accordance with laws in effect on June 30, 1948, such obligations and expenditures to be charged against funds when made available for administrative expenses for the fiscal year 1949."

SEC. 9. The third paragraph of section 24 of the Federal Reserve Act, as amended by section 328 of the Banking Act of 1935, as amended, is hereby amended to read as follows:

"Loans made to established industrial or commercial businesses (a) which are in whole or in part discounted or purchased or loaned against as security by a Federal Reserve bank under the provisions of section 13b of this Act, (b) for any part of which a commitment shall have been made by a Federal Reserve bank under the provisions of said section, (c) in the making of which a Federal Reserve bank partici-
pates under the provisions of said section, or (d) in which
the Reconstruction Finance Corporation cooperates or pur-
chases a participation under the provisions of the Recon-
struction Finance Corporation Act, as amended, shall not
be subject to the restrictions or limitations of this section upon
loans secured by real estate.”
A BILL

[Report No. 974]

S. 2287

25th Session
80th Congress

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