UNITED STATES SENATE

Committee on Banking and Currency

February 7, 1951

Dear Mr. Vardaman:

This will acknowledge receipt of your statement of February 5, 1951 and the attached memorandum requesting any comment that I might care to make.

The first part of your statement relates to your version of what took place at the January 31st conference between the President and the Federal Open Market Committee. Naturally, I cannot determine whether your report of that conference or the report of Governor Evans is correct. However, the aftermath of confusion which has followed a conference intended to clarify matters convinces me that the President has failed to grasp the basic issues of fiscal policy which are at the bottom of the dispute between the Treasury and the Federal Reserve Board.

Your statement makes it clear that you feel that the Board should support the financing and bond program advocated by Secretary Snyder. If this opinion is based on economic rather than legal considerations, I do not question your right to advance it. My own view is that the Treasury's fiscal policies will result in disastrous inflation. Since May, 1950, the Board's holdings of government securities have increased by $3,500,000,000 which in turn has led to a six-fold expansion of credit. The proposal that the Board should continue to support the Treasury's cheap money policies has been accurately described by Mr. Henry Hazlitt as "fighting fire with gasoline."

The concluding paragraph of your statement is one of the most amazing ever uttered by a public official in recent years. You say, "The question of statutory prerogatives . . . should be subordinated to the all important necessity of supporting the Government and the Presidency in this national emergency." The meaning of this euphemism is that the laws passed by Congress should be disregarded whenever the President feels that the national emergency so requires. I am unalterably opposed to that sort of totalitarian philosophy either in war or in peace.

You also say in the final paragraph of your statement that you "unhesitantly waive any theoretical statutory authority and prerogatives in order to support the Government and the Presidency at this time." First, I would like to point out that the laws of the United States are not "theoretical" for 150,000,000 American people. They must obey them or go to jail. By what right do you presume to waive statutory authority in violation of your oath of office?

Finally, I invite your attention to the fact that the Federal Reserve System is accountable to the Congress and not to the Presidency as you suggest. Congress has not charged the Board with the duty of supporting the price of government securities, but rather with the duty of supporting the value of the dollar.

Until such time as the duties of the Board may be changed by Act of Congress, I trust that you will see the impropriety of your suggested waiver of statutory authority and prerogatives.

Sincerely yours,

(Signed) John W. Bricker

The Honorable James K. Vardaman, Jr.
Board of Governors
Federal Reserve System
Washington, D. C.

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BOARD OF GOVERNORS OF THE FEDERAL RESERVE SYSTEM

RELEASED FOR PUBLICATION February 15, 1951
MORNING PAPERS

FEB 19 1951

Dear Senator Bricker:

Your letter of the 7th is acknowledged with thanks. I particularly appreciate your having taken time to read my statement, although the connotation of "totalitarianism" which you place on it surprises me almost as much as if you had suspected me of cannibalism, for instance. That interpretation, and fear that you may have drawn really serious conclusions just as foreign to my intent, make it necessary for me to make myself more clear than I evidently did in my statement. Therefore, I will reply to each paragraph of your letter in detail.

In my statement of February 5th I said that in my opinion Governor Evans' account of the conference between the President and the Federal Open Market Committee was correct as to what was actually said. But I expressed the thought that regardless of the words spoken the President was allowed to leave the conference with the erroneous belief that the Committee would support the Government's program. I understand that some other members of the Board had the same thought; and only one member, so far as I know, has denied that the President was allowed to leave the conference with a false impression.

You are correct in interpreting my statement to indicate my belief that this Board should support the Government's program as officially promulgated on January the 18th by the Secretary of the Treasury, the spokesman for the Government in this field. My advocacy of such support is based upon both legal and economic reasons. However, my statement did not indicate approval or disapproval of the Government's plan, nor did I discuss its economic advantages or weaknesses. I simply say that since this Board has absolutely no statutory authority to alter or to cancel the Government's debt financing plan, and has not even the remotest suggestion of statutory authority to initiate a substitute plan, it should support the Government's program until such time as the Congress clarifies the situation by legislative enactment which will either:

(1) Give the Board authority in the area of public debt management, or

(2) Give the Board more effective control of investments and reserves of banks and insurance companies and other depositaries, lending agencies and institutions whose operations materially affect the national credit structure, or

(3) Relieve this Board of some of its responsibility for credit control.

The Federal Reserve has supported the Government bond market at arbitrary price levels whenever necessary for the past nine years. While the Board has repeatedly reported to Congress the dilemma which confronts it, so far as I know the Board has never asked the Congress for relief from its implied obligation to continue this self-imposed practice, and the Congress has not seen fit to direct the Federal Reserve System to stop this practice. Failure of the System at this time to give the same degree of support to the Government plan, and the withdrawal of this arbitrary price support, would probably result in a chaotic Government bond market and a decline in the price of long time Government bonds to some figure below par. Just where the price would go is anybody's guess, but any material decline under present circumstances might result in some sort of a buying panic that would further decrease the purchasing power of the dollar.

If I may be permitted a question at this point: Would you as a citizen or as a United States Senator recommend that the System withdraw its arbitrary support from the Government bond market, and allow the bonds to go below par?

If you will read again my statement you may consider it less "amazing" if you note that I did not advocate waiver of any actual statutory responsibility, authority or prerogative. What I did advocate was that we do not now raise a question regarding prerogatives and authority which this Board has never had nor claimed to have; and which if they ever existed by Congressional intent or otherwise, have most probably been waived and forfeited by this Board's actions or lack of action.

In this connection it should be borne in mind that the Board issued a public statement on December 8, 1941 which said in part:

> "The System is prepared to use its powers to assure that an ample supply of funds is available at all times for financing the war effort and to exert its influence toward maintaining conditions in the United States Government security market that are satisfactory from the standpoint of the Government's requirements."

Since December, 1941, the Federal Reserve has consistently and without exception supported the United States Government bond market at arbitrary price levels whenever it considered such support advisable or necessary. The System is currently following the same course. Under present conditions and in view of the actions of the Board extending over a period of more than nine years it seems to me that any statutory prerogatives in the premises, if they ever existed, have been forfeited by the precedent set by the Board itself.

You might be interested in knowing that for more than a year I have advocated, and I believe some other members of the Board have done likewise (but I speak only for myself), that conversations with the Secretary of the Treasury and action by the Board be initiated with a view to reducing to par the arbitrary price on long time Government bonds. I could not then see any justification for supporting those bonds at high premiums, while at the same time owners of "E" savings bonds, mostly small individual savers, were penalized by loss of some interest if their bonds were cashed before maturity.

Also I was afraid that if we continued such high level arbitrary support the market might become frozen into that pattern by circumstances and events which would make it inadvisable or impossible to change the arbitrary price without disrupting our economy. The Board has not acted to free itself of this shackle to a pegged price which the Board voluntarily put on itself in December 1941 and has consistently worn since that date. Therefore, the System, which is a creature of the Congress, now finds itself in a situation where public debt management, an area in which the Board has no authority, is having a material affect on credit control, an area in which the Board does have statutory authority.

The dilemma is serious and warrants the most careful and constructive consideration by every thoughtful citizen, and especially you and your colleagues in the Congress. And until the Congress acts I do not see any constructive course of action left open to this Board other than to carry on the same general policy it has followed during the past nine years, because the Government's financing program has been officially promulgated and stands today as the only financing program which the Government has. If we do not support that program, what are we to do, since we have no authority to cancel or change it and no authority to initiate one of our own?

And here again let me emphasize that I am speaking in this letter only for myself.

My statement does not indicate in any way that I am willing to waive, nor did I advocate that the Board waive, any statutory authority or prerogative which the Board as such may have or which the individual board members may have under the law or under their oaths of office. Educated as a lawyer and having enjoyed more than twenty years successful experience as a practicing attorney, banker and businessman, the law is

very real to me. I have always believed that our Constitution with its implementing framework of statutory laws is the most sacred and valuable asset which we as a nation possess. And, incidentally, I have spent more than six years in the combat forces of our amphibious Army and Navy defending that belief. In civil life my most serious disagreements with friends in public office have been based on my thought that their actions were in some way interfering with the operation and perpetuation of our constitutional republic. In view of this well known official and personal record, your inference that I am a sponsor of totalitarianism seems to me to be less than justified.

As to this Board's accountability to the Congress the minutes of the Board should show that during my nearly five years membership I have emphasized on several occasions my firm belief that we were accountable to the Congress and to no one else. From time to time and particularly during recent years we here in the Board have had more than one discussion of this subject, and I have been critical whenever one of my colleagues acted in any way which I felt might jeopardize our limited right to freedom of action as provided under present law.

The admonition in the last paragraph of your letter is cordially and wholeheartedly accepted and I assure you in your official position as a United States Senator that as long as I serve as a member of the Board I will not willingly waive my responsibilities under the statutes or under my oath of office.

Let me repeat, the law is silent as to the Federal Reserve's authority in the area of debt management, and on the other hand the law is quite specific in placing responsibility for management of the public debt in the hands of the Secretary of the Treasury. Therefore, I feel that the welfare of the Nation would be better served if this Board continued to support the official Government financing program just as it has since 1941 and that the Board should immediately approach the Congress with an explanation of its position and ask for such clarification as the Congress might care to make in the premises. To do otherwise, that is, to withdraw the arbitrary support of Government bond prices which we have maintained continuously during the past decade, could result in near panic in the Government bond market which might easily depress Government bond prices to some unknown level. On the other hand if we continue to give the Government financing program the Board's customary support until the Congress shall determine otherwise it is possible that the present pressing necessity for arbitrary support of the market might be considerably lessened or even eliminated during the coming months.

Again, please accept my thanks for writing to me as fully as you have. And I would welcome an opportunity to discuss these grave questions with you personally, or with any of your colleagues who may take the problem under advisement.

With best wishes, I am

Sincerely,

(Signed) J. K. Vardaman, Jr.

J. K. Vardaman, Jr.

Washington, D. C.

February 16, 1951.

Memorandum from J. K. Vardaman, Member of the Board of Governors, Federal Reserve System.

On the 12th instant I received from United States Senator John W. Bricker of Ohio a letter dated the 7th in which he comments on my public statement of February 5th. Inasmuch as Senator Bricker's letter was official and published in the Congressional Record, I am writing an open letter in answer rather than a private letter in order to reply to certain inferences in the Senator's letter.

Attached is a copy of Senator Bricker's letter to me and a copy of my reply dated February 15th.

J. K. V.

Attachments.