FEDERAL DEPOSIT INSURANCE CORPORATION

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EXCERPTS OF AN ADDRESS OF HONORABLE LEO T. CROWLEY, CHAIRMAN, FEDERAL DEPOSIT INSURANCE CORPORATION, BEFORE A FORUM MEETING OF NORTH CAROLINA BANKERS

CHAPEL HILL, NORTH CAROLINA JULY 12, 1937

"Frequently during the past few years I have been asked by friends in and out of the banking fraternity what I thought would become of Federal deposit insurance in the event of another depression comparable to that of a few years ago. The obvious answer to that question, of course, is that I believe deposit insurance will accomplish its purpose through many business cycles to come. Otherwise I should certainly not choose to continue my association with the Federal Deposit Insurance Corporation. The factors which will determine the adequacy of the present plan of deposit insurance are quite complex, however, and previous attempts at deposit insurance or guaranty have generally ended disastrously. Wonder as to the chances for success of the present plan is, therefore, quite understandable.

"I should like this evening to present to you my belief as to the future of American banking and, consequently, the future of Federal deposit insurance. The success of deposit insurance will depend principally upon five things: First, the efficacy of new governmental powers of business and credit control; second, the efficacy of bank supervisory policies; third, the management of the Federal Deposit Insurance Corporation; fourth; the steadfastness of the public in time of crisis; and, fifth, the attitude and competence of bankers."

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"If, in the future, booms can be held to the stature of rolling hills and if depressions become glens rather than chasms, the task of bankers will be much more simple.

Given a more level business cycle, I consider it the primary duty of bank supervisors to maintain banks under their jurisdiction in a condition which will enable those banks to withstand ordinary and reasonable cyclical fluctuations. This duty can be served only by intense and continuous attention to three aspects of the banking picture. A permanently sound banking system requires, first, control of the banking structure; second, control of banking practices; and third, the elimination and avoidance of unsound assets."

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Of almost equal importance with the need for supervisory control of the banking structure is the ever present necessity of keeping banking practices within reasonable bounds. It is unfortunately true that the "errors of judgment" of some few bankers have developed a public demand for governmental supervision of banking practices. Yet this responsibility continues to rest primarily with the bankers themselves.

It is axiomatic that the safety of depositors' funds and the soundness of bank capital depend entirely upon the wisdom of decisions made by bankers. Only rarely can a supervisory authority, arriving after the horse is stolen, do anything other than require the elimination of the unsound assets acquired as the result of unsound banking policies. The elimination of these assets and the rectification of managerial errors of judgment nearly always results in losses to the bank. It is distinctly to the banks' advantage, therefore, to follow sound policies and proper practices so that both losses and the necessity for supervision may be kept at a minimum.

Where bankers refuse to accept this responsibility or where they seem unable to exercise their functions judiciously, it is only reasonable to expect that supervisory authorities must act vigorously. The obligation of the Federal Deposit Insurance Corporation in this regard is tremendous. Not only have we accepted a public mandate to protect bank depositors against loss, but we have received a congressional mandate (insuring deposits with an assessment rate less than one-third as great as would have been required to cover the losses from 1870 to 1933) which assumes a higher regard for sound banking practices than has ever existed before. It is the necessity for observing these mandates and for living within our allotted income which leads the Corporation to stress so heavily observance of the fundamental rules which we believe govern sound banking."

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"In several cases our efforts to rehabilitate banks have been thwarted by the ability of bankers to declare dividends without regard for the source of those dividends. It is my recollection that every banking primer carried as Rule Number One the axiom that dividends are to be paid only out of operating earnings after the payment of expenses and the elimination of ascertained losses and depreciation. Let us revert to the primer, for I can think of no more unsound banking practice than the payment of dividends out of capital funds, nor can I think of any practice which will result more quickly in censure by the Corporation.

Our study of the examination reports of banks made by supervisory authorities prior to the collapse of values during the early thirties has convinced us that much of the depletion of capital which occurred during those years, and which resulted in the insolvency of thousands of institutions, could have been avoided had the subject institutions taken depreciation regularly and written off losses as they arose. I lay particular stress, therefore, upon my earlier statement that no dividend should be paid by any bank until all of that institution's deadwood has been cleaned out. Let losses be eliminated currently and depreciation taken on a reasonable and regular basis and your institutions' chances for survival during a period of falling values are improved a thousandfold."

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"The quality of bank management is improving constantly through the working of a number of factors. Chief among these, of course, is Mr. Darwin's law of survival of the fittest. The importance of meetings such as this, however, should not underestimated. Neither should the hours of study put in individually by bankers hoping to supplement, or substitute for, these opportunities for a meeting of minds and an exchange of ideas. In the last analysis there is no sound banking without capable bank management. Further, there is no such menace to the soundness of our banking system as bad or unscrupulous bank management. Capable bank managers who comprehend and practice all of the things I have said and most of the things I have yet to say are fortunately in the majority. Yet, as you know from sad experience, the chicanery of one bad banker can blacken the name of the whole profession and the manipulations and malpractices of one poorly managed bank can pull to ruin thousands of institutions."

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"As to the management of the Corporation I can say that we propose to follow exactly the conservative standards of operation which we propose that bankers should observe. Our activities to date display, I believe, our determination to take our losses as they arise and to forestall an accumulation of weakened and weakening institutions. The Corporation has fortunately been able to develop an excellent operating record during the first three and one-half years of its operation. The income from the investment of our capital funds has been more than sufficient to cover our administrative expenses and our deposit insurance losses and expenses, thereby leaving our original capital and our income from assessments entirely unimpaired. It would be unreasonable to expect that we can continue indefinitely a record such as this, made during a period of recovery and rising values after thousands of weakened institutions had been eliminated during the purge of the 30's. By intelligent administration of our supervisory powers and by taking our losses currently, however, we hope to build a long-term record for conservative operation. Let me emphasize, however, that it is not our financial record we are primarily eager to maintain. We are in the particularly fortunate position of having no need to embellish a failure record, since we charter no banks. If, then, we can continue to weed out the banking system's deadwood as it appears, paying as we go, I shall be satisfied that we are accomplishing our mission and I believe that our financial record will take care of itself."

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I have spoken already of the importance attached to the competence of bank management. The attitude, be it implied or expressed, of bankers toward the Corporation will also be an important factor in determining the success of deposit insurance. If the Corporation is to succeed, the attitude of bankers must and should be cooperative. We ask no favors from you bankers. We do suggest, however, that you think clearly and reasonably about the Corporation and about its relation to you. Those of you who invest in business enterprises do everything in your power to make those enterprises succeed. Is it unreasonable to expect that you will work equally as hard to protect your investment in the Federal Deposit Insurance Corporation? Going a step further, I wonder if you have stopped to imagine what will happen to your banks in the event deposit insurance does fail in time of emergency. You are optimistic indeed if you think any bank or the banking structure can survive a repetition of the 1933 crisis should the Corporation fail in the meantime. The interests of your depositors, the desire to protect your investment in the Corporation, the wish to preserve your own institution as well as our traditional system of banking, all should lead you to do everything in your power to insure the Corporation's success. It is to the bankers' individual and collective advantage to have every institution a sound institution -- that is also the goal of the Federal Deposit Insurance Corporation. It is to the bankers' advantage to have a strong yet flexible banking structure. We, too, are working toward that end.

It is certainly to the good bankers' advantage to have the profession purged of those individuals who indulge in unsafe and unsound practices. We are determined that depositors shall not again unknowingly trust their funds to men of this calibre. Our aims are identical with yours. They are worthy aims.

"In sharp contrast to the help and cooperation the Corporation has had from most bankers, there have come to my attention recently several instances of attempts by supposedly well informed and thoughtful persons deliberately to undermine our efforts. Attacks on the Corporation on the hackneyed grounds that "deposit insurance is no substitute for good banking" we can laugh off as displaying ignorance of our aims and of our record. I must take issue, however, with those bankers who condemn deposit insurance in an offhand way and who campaign against the Corporation at every opportunity. It is particularly unfortunate when these shortsighted gentlemen happen to be leaders in their profession. Such an instance occurred recently when one of your elected leaders was heard to say, "Deposit insurance is fundamentally unsound. I don't believe it has a chance in a million to succeed and I intend to tell bankers so at every opportunity." If the ideas and attitude of men like this are to become the credo of American bankers, then surely Federal deposit insurance will fail. And should it fail, let me say that the guilt will lie directly at the doorstep of the bankers and of the banking system.

"We have no delusions concerning the Corporation's omnipotence. We realize that deposit insurance is nothing more than a technique designed to adapt to our increasingly complex economy a banking system that is in many respects archaic and cumbersome. The persons who so boldly forecast the collapse of deposit insurance lose sight of the fact that they thereby impugn not the Corporation nor the soundness of deposit insurance, but the "fundamental soundness" of the banking system which they profess to support. I believe that the virtues of our system of independent banking by private enterprise outweigh its weaknesses. I believe that deposit insurance can perpetuate the system and that, in any event, the Corporation's effort merit whole-hearted support until their effectiveness has been tested. That is the credo I offer for your consideration."

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