Address

of

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at the

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Mr. Chairman, Members of the Colorado Bankers Association, Ladies and Gentlemen:

It is a great pleasure to be here in your magnificent State today. I wish to thank you, and Mr. Scarboro especially, for the many courtesies which have been shown me. I was disappointed not to be here earlier to attend your Past President's Dinner and the entire program. But the pressure of affairs in Washington, has made it necessary that I stay at my desk as long as possible and fly out here at the very last moment.

We in the Federal Deposit Insurance Corporation are sincerely appreciative of opportunity tomeet with bankers and discuss with them our mutual problems. Our successful operation depends so much upon your success and in turn, our operations have such a vital relationship to yours, that it is one of our prime duties to keep you informed of our objectives, our activities and our problems. On this occasion I wish to discuss breifly the internal organization of the Corporation, its financial experience to date, and its part in the reorganization of the banking system since the banking holiday.

<u>Set-Up of the Organization</u>. As you know the Corporation is directed by a Board consisting of Mr. Leo T. Crowley, Chairman; Mr. J. F. T. O'Connor, Comptroller of the Currency; and former Senator Phillips L. Goldsborough, who recently was appointed to fill the place left vacant by the resignation of Mr. E. G. Bennett.

The formal organization of the Corporation consists of eight divisions and offices. Five of these - the Legal Department, the Secretary's Office, Controller's office, Public Relations Division and the

Accounting and Auditing Division - perform functions corresponding to those of similar offices in a business corporation. It is the three remaining divisions - the Examining Division, the New and Closed Bank Division and the Division of Research and Statistics - which perform the special duties entrusted to the Corporation by Congress.

Division of Examinations. The Examining Division may, I think, be ranked first in importance since it constitutes the eyes and the ears of the Corporation. It is through the Examining Division that the Corporation maintains contacts with those state banks not members of the Federal Reserve System whose deposits are insured. The Division is headed by a Chief Examiner. There are seven review units in the Washington office and 12 supervising examiners' offices in the 12 districts throughout the Country. The entire personnel of the Division numbers 153 examiners, 190 assistant examiners, and 156 clerks and stnographers, or a total of 529. This is nearly three-fourths of the entire personnel of the Corporation.

Examinations are made of all State nonmember banks applying for admission to the Insurance Fund. In each case the field examiner and the supervising examiner made recommendation as to admission based on the condition of the bank. Summaries of all examinations of banks which are applying for admission to the Corporation are presented to the Board of Review of the Corporation, which is composed of two Directors and various other executives. Such other summaries of examinations are presented to the Board of Review, which meets from two to three times a week, as involve special problems. From the Board of Review the cases with the Board's recommendation proceed to the Board of Directors and are acted upon by them. Besides these admission examinations the Division is making one regular examination each year of all insured banks which are not members of the Federal Reserve System, and such supplementary examinations as may be required. The Federal Deposit Insurance Corporation examines only nonmember banks sin ce the Comptroller of the Currency and the Federal Reserve System examine national banks and State member banks respectively. Under the provisions of the Temporary Fund which is now in operation all banks which were members of the Federal Reserve System, which includes State member banks and national banks, were automatically extended the benefits of insurance. The Corporation therefore was not required to examine these banks. Since member banks are automatically insured by law as long as the Temporary Fund is in operation, the Federal Deposit Insurance Corporation does not concern itself particularly with the affairs of these banks. However, when, in individual cases, examination reports are needed, the Corporation has the authorization officially to request such reports from the Federal Reserve Board or the Comptroller of the Currency as the case may be. All three of these agencies use approximately the same examination forms and conduct the examinations on practically the same basis. The number of insured nonmember banks which the Corporation examines is nearly 7,800, which is more than half of all insured banks.

New and Closed Bank Division. When an insured bank closes the payment of its depositors is in charge of the New and Closed Bank Division. This division organizes a new national bank to pay off the depositors in the failed bank and to handle the necessary records. As soon as an estimate can be made of the amount which will be necessary to pay off the insured deposits the Federal Deposit Insurance Corporation makes this sum available to the new national bank and also sufficient funds to cover its operating expense. The insured depositors of a failed bank file proofs of their claims, assign these claims to the Federal Deposit Insurance Corporation and are paid at once in cash or in checks upon a Federal Reserve bank.

The new bank may accept deposits and honor checks but it may not make loans nor carry on other functions of banking. All of its funds must be deposited with the Federal Deposit Insurance Corporation or a Federal Reserve bank or invested in direct obligations of the United States Government. If capitalized by local interests within two years the new bank may conduct a normal banking business and may become a regular national bank. The Federal Deposit Insurance Corporation acts as liquidating agent when the Corporation is appointed receivers of a failed bank. The Corporation has been appointed receiver for only four banks, two national and two State banks.

As of June 15, 1935, 19 insured banks have failed. The 18 banks the deposits of which we have begun to pay off, had total deposits of nearly four million dollars. Of this amount more than one million dollars were secured or subject to off-set and the Corporation's liability to depositors amounted to over two and one-half million dollars. Of this amount $2,347,638 has already been paid to 18,552 depositors. There remains $238,364 insured deposits to be paid to 6,211 depositors. All of these failed banks were small and had only a few depositors with accounts in excess of $5,000. Since the 18 closed institutions holding an aggregate of $4,000,000 in deposits had only $200,000 of deposits that were uninsured or unsecured the loss to the depositors holding claims in excess of the insurance limits will be small.

All of the 19 new deposit insurance national banks organized to pay off the depositors in these closed banks are still being operated under the Supervision of the New and Closed Bank Division of the Corporation.

Division of Research and Statistics. The Division of Research and Statistics has the duty of collecting statistical information required by the Board of Directors for the intelligent direction of their responsibilities and of engaging in such research as will aid the directors and Congress in making decisions pertaining to deposit insurance. The Division has recently completed a study of losses to bank depositors during the past 70 years for the purpose of providing the best possible actuarial basis for the rate of assessment charged insured banks. It is now engaged in an analysis of the experiences of the various State guaranty funds for the protection of depositors and of the reasons why these funds proved to be inadequate. The Division obtains reports of condition from all insured banks which are not members of the Federal Reserve System twice a year. The tabulations from these reports are combined with those from member banks, thus providing statistics regarding the deposits, other liabilities and assets of nearly all the banks in the country.

Balance sheet of the Corporation. The capital stock of the Corporation is owned by the United States Treasury and 12 Reserve banks, the Treasury subscribing to $150,000,000 of stock and the Reserve banks to $140,000,000. Insured banks have paid assessments to the Temporary Insurance Fund of approximately $41,400,000. The only other important items on the liability side of the balance sheet of the Corporation are approximately one million dollars of reserves for deposit insurance losses and expenses and suspense items, and two and one-half million dollars of surplus derived from an excess of income over expenses during 1934. The asset side of the balance sheet included on December 31, 1934 - $16,000,000 of cash, $315,000,000 of United States Government obligations and $2,000,000 of advances to the depositors of closed banks and subrogated claims of such depositors.

Income and Expense. As has been suggested the income of the Corporation from its investments has exceeded its expenses by more than $2,500,000. The budget for the year 1935 provides for current expenses not in excess of two and a half million dollars while the present rate of income on investments exceeds $8,500,000 a year. The largest item of expense of operation of the Corporation in the future will, of course, be the losses incurred in paying the claims of depositors in banks which close. The size of this item of expense is unpredictable and is likely to be erratic from year to year.

Bank suspensions during the years 1934 and 1935 have been unusually few in number and the amounts involved abnormally small. This is due to several factors. A great deal of liquidation of bank assets of doubtful value is being accomplished through such agencies as the Farm Credit Administration and the Home Owners' Loan Corporation. The Reconstruction Finance Corporation has made large sums available not only in the form of capital but also as direct loans. Further, the liquidation which occurred prior ot the Banking Holiday has eliminated a large proportion of the weak banks. Periods of recovery subsequent to banking crises have in the past been characterized by relatively few bank failures. The low rate of failures since the organization of the Corporation cannot be expected to continue and it is a wise policy for the Corporation to build up reserves at the present time as a safeguard against the large number of failures which are likely to occur in the future.

The foregoing remarks have been concerned with the present structure and activities of the Federal Deposit Insurance Corporation. I would like to add a few words about its background, the banking situation at the time it was established and the aid it has rendered in improving that situation.

Establishment of the Federal Deposit Insurance Corporation. You are familiar with the creation of the Federal Deposit Insurance Corporation by the Banking Act of 1933. The Congressional hearings and discussions of this Act had been conducted during and immediately after the Banking Holiday. The adoption of the principle of deposit insurance was undoubtedly the direct result of the exceedingly large number of banks which had just been closed and the lack of confidence in the banking system of the country. The Congressional committees which reported the banking bill of 1933 to the Houses of Congress stressed two reasons for the inclusion of the insurance of deposits in the Bill. On one hand there was the desire to extend to all bank depositors a protection which would immediately reestablish and maintain confidence in the banks. On the other hand there was the desire to provide a method of advancing to depositors of failed banks the funds which were tied up, to eliminate the inconveniences to which the depositors had been subject and the disturbance to business caused by the inability of bank depositors to use their money.

At the time the Banking Act was passed in June, 1933, the Secretary of the Treasury and State banking authorities were engaged in the licensing of the banks which had been closed during the Holiday. The urgent necessity of reopening the banks made it imperative that all banks which had a reasonable chance of continuing their business should be licensed. The decisions incident to such licensing were necessarily made with tremendous speed and under unusual conditions. It was natural that some banks were licensed which did not have adequate support to really warrant their continuance as banking institutions. During the summer and autumn of 1933 a diligent effort was made by the Federal authorities to determine the actual capital status of the banks of the country. It was felt that while deposit insurance would reestablish confidence in the banking system it was necessary to replace the capital of many banks which had been impaired if the reestablishment of confidence in the banks was to be justified. The real situation in respect to the nonmember State banks first became known when the examinations of banks applying for admission to the Insurance Fund were completed. The deposit insurance law provided that all banks found to be solvent were to be admitted to insurance. Since solvency was defined as the ability to meet deposit liability, many banks were admitted to insurance which had had their entire capital or most of it wiped out through losses. In fact more than 1,450 nonmember State banks among those admitted to insurance were found to have capital funds which were decidedly inadequate.

These weak banks were admitted to insurance benefits on the condition that their capital would be rehabilitated through local aid and funds from the Reconstruction Finance Corporation.

The Reconstruction Finance Corporation had not made material progress in the reconstruction of bank capital prior to September 1933. From September 1933 to February 1934 an intensive campaign was carried on to recapitalize the banks which had been admitted or were applying for admission to insurance. Emphasis was at first placed on the State banks which were not members of the Federal Reserve System because of the active interest which the Federal Deposit Insurance Corporation took in these banks. Toward the latter part of the period the authorities extended their efforts to Federal Reserve member banks believing that many of these banks required capital rehabilitation prior to the anticipated inauguration of the Permanent Deposit Insurance Fund on the first of July 1934.

This program of capital rehabilitation has now been nearly completed. There remain only 500 banks of all classes in the list of those inadequately capitalized. On June 7, the Reconstruction Finance Corporation had a net investment of about $890,000,000 in the capital structures of approximately 6,000 banks in this country. It has invested approximately $4 3/4 million in the capital obligations of 52 Colorado banks as compared with total capital funds of all Colorado banks of about $28 million.

Let me tell you what has happened to those 1,450 weak nonmember State banks which I just mentioned and which were admitted to insurance with the definite understanding that their capitals were to be rebuilt. All but 188 have been recapitalized to the extent that at the end of February there remained only $504,000,000 of deposits in these so-called weak banks. These remaining weak nonmember State banks showed a total book capital of about $59,000,000, while the examiners showed these banks to have a net sound capital of about 2.7 million dollars. In other words, the number of under-capitalized State nonmember banks has been reduced from 1,450 to 188 and the volume of deposits supported by inadequate margins of capital has been reduced from $1,500 million to $304 million.

This, I believe, shows real progress. Many difficulties have been encountered in carrying out the program. The Comptroller of the Currency and the Federal Reserve Board have sufficient power to require banks under their jurisdiction to remove capital impairments and increase their capital if necessary. The Federal Deposit Insurance Corporation had no such authority and could only resort to the powers of persuasion with the aid of the State banking authorities. The credit for the success of the recapitalization program is to be shared with the Reconstruction Finance Corporation whose cooperation made it possible and to the various State banking authorities who also in most cases gave us their hearty cooperation.

Investment by the Reconstruction Finance Corporation in the capital of banks is now practically at an end. The Corporation has announced that it intends to complete its investments in the capital of banks soon after July 1, and that all applications for the sale of capital obligations to the Reconstruction Finance Corporation must be filed by July 15. It is of the utmost importance for the entire banking structure and deposit insurance that those banks still having inadequate sound capital take steps to repair their condition through the Reconstruction Finance Corporation during the next few weeks.

Capital rehabilitation of the banks made it possible to write off from the books of the banks a tremendous volume of losses which had accumulated during previous years. The amount written off during 1933 and

1934 by all commercial banks has exceeded two billion dollars or more than one-third of the book capital of the banks. We estimate that less than one billion dollars of losses which still remain to be written off the books of the banks. It is our policy to do everything possible to accelerate the completion of this house cleaning.

Perhaps you would be interested in the results of a recent tabulation of examiners' reports. In about 7,700 insured nonmember State banks and 5,300 national banks, or a total of almost 13,000 banks with total loans of about $10.4 billion, the national and Federal Deposit Insurance Corporation examiners classified 3.8% as worthless, 3.6% as doubtful and 28.4% as slow. For national banks the worthless and doubtful loans total 7.1% of total loans, while for State nonmember banks this figure is 8.0%.

The insured banks of Colorado which are not members of the Federal Reserve System appear to be in a somewhat sounder position than are such banks for the country as a whole. 25% of all assets of State nonmember banks throughout the country are subject to criticism as being loss, doubtful, or slow, while in Colorado only 17% are so criticized. 7% of the assets of all such banks in the United States are either doubtful or loss while in the Colorado banks 5% of the assets fall in these categories. It must be added that these figures are approximate and that the examinations from which they were taken cover a period of about ten months. In all probability there has been a substantial change since these tabulations were made owing to the rapidity with which donditions - particularly those affecting banks - have improved since last summer, and owing to the fact that large portions of these losses have been since written off.

As we have noted, one of the chief purposes of the Federal Deposit Insurance Corporation is prevention of freezing of bank deposits and consequent economic stagnation. In this connection the Corporation recently undertook and inquiry concerning the deposits still tied up in banks in receivership. At the beginning of this year over 6,000 banks were still in the hand of receivers. Of the 4 3/4 billion dollars of deposits in these banks at time of closing, 2.4 billions or 51% still remained unpaid. Judging by the experience of the past, depositors in these banks probably will not receive substantial dividends in addition to those already paid.

Extent of Insurance Coverage. Insurance of deposits in commercial banks in the United States is now almost universal. 14,203, or 92.85%, of the 15,296 commercial banks. In Colorado 90% of the banks holding 99.6% of the deposits are insured. In the insured banks of the entire country 44% of the deposits are covered by insurance while in Colorado 53% of the deposits of insured banks have such coverage.

Under the present system whereby deposits are insured up to $5,000 the vast majority of accounts are fully insured. In the insured banks of Colorado are approximately 410,000 deposit accounts and 405,000 of these, or 99%, are fully insured. Ninety-eight per cent of the depositors in all the insured banks of the country have accounts with not more than $5,000 to their credit and are therefore protected in full. The aggregate amount of deposits of the fifty million depositors which are fully protected is between 13 and 14 billion dollars. The remaining three or four billion dollars of insured deposits represents the first $5,000 in the accounts of depositors with larger balances.

Seventy per cent of all the insured banks have total deposits of less than $750,000 each. In Colorado 74% of insured banks fall in this class. These banks have an insurance protection covering more than 80 per cent of their total deposit liability. The Federal Deposit Insurance Corporation thus has a very real and tangible interest and responsibility in practically all of the licensed banks in the country and in the great majority of these banks that interest is equal to or greater than 80 per cent of their total deposit liability.

In accord with the Act of June 16, 1933 as amended June 16, 1934, the extent of insurance coverage will be increased at the beginning of next month. In order that they may conform with the law, the banks have been supplied with forms for applying for participation in permanent insurance, and forms for making the remittances required by law. A regulation has been issued by the Federal Reserve Board defining precisely the content of "total deposits", the item upon which the new remittances of the banks to the FDIC must be based. It is legally necessary that the banks remit for participation in the permanent fund before they receive a refund from the temporary insurance fund if they are to have their deposits insured without interruption. However, refunds will be made from the temporary fund as soon as the necessary accounting detail permits. If there are any questions which you may care to ask about the change in deposit insurance which will take place at the end of this month, I shall be glad to answer them to the best of my ability at the conclusion of these remarks.

<u>Bank Losses Under Deposit Insurance</u>. Deposit insurance has radically changed the significance of bank losses. Formerly local depositors and stockholders bore the burdens resulting from bank failures

and the long demoralizing period of liquidation which followed. I need not stress the paralyzing effect of the freezing of deposits resulting from bank failures, for you in this State have suffered intensely from this evil. In the years 1920 to 1934, 149 of your banks with $31,532,000 of deposits failed. Particularly did you suffer in 1923 when banks with deposits of $4,689,000 failed and in 1925 when the failing banks had $9,062,000 of deposits. The economic paralysis and uneconomic liquidation which resulted in many communities is known to all of you.

Now losses which have accumulated in any bank until it fails are shifted to the entire banking system since such losses affect the rate of assessment which must be paid. A bank failure now affects every bank directly in dollars and cents. The Federal Deposit Insurance Corporation considers it one of its chief responsibilities to do everything possible to reduce losses from bank failures. It is not possible, however, for the Corporation to take much specific action which will eliminate bank failures. It can only encourage bankers to conduct their business in such a way as to keep losses at a minimum. This is now your concern as much as ours. It is our hope that you will be instrumental in preventing bank failures, and reducing the losses therefrom. In this way you will be keeping the insurance assessments upon banks at the lowest possible figure.

While deposit insurance has added greatly to the security of bankers and the banking system, it has also added to the responsibility of bankers. It is now of vital interest to the bankers not only that their own banks be sound, but also that other banks be sound. Thus, it is of primary importance to all of us that we continue to be vigilant in the promotion of sound banking.