FEDERAL RESERVE ACT AMENDMENT

HEARINGS

BEFORE THE

COMMITTEE ON BANKING AND CURRENCY
HOUSE OF REPRESENTATIVES

SEVENTY-EIGHTH CONGRESS

FIRST SESSION

ON

H. R. 1699

A BILL TO AMEND SECTION 12B AND SECTION 19
OF THE FEDERAL RESERVE ACT

REVISED

MARCH 25, APRIL 1, 2, 5, 7, 1943

Printed for the use of the Committee on Banking and Currency

UNITED STATES
GOVERNMENT PRINTING OFFICE
86330 WASHINGTON : 1943

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FEDERAL RESERVE ACT AMENDMENT

THURSDAY, MARCH 25, 1943

House of Representatives,
Committee on Banking and Currency,
Washington, D. C.

The committee met at 10:30 a. m., Hon. Henry B. Steagall (chairman) presiding.

The Chairman. The committee will please be in order. I called the committee this morning to consider H. R. 1699. I am sure members of the committee are familiar with the bill; it has been pending in the committee for several days.

(The chairman read H. R. 1699, which is as follows:)

[H. R. 1699, 78th Cong., 1st sess.]

A BILL To amend section 12B and section 19 of the Federal Reserve Act during the continuance of the war and for six months after the cessation of hostilities

Be it enacted by the Senate and House of Representatives of the United States of America in Congress assembled, That the second sentence of paragraph (1) of subsection (h) of section 12B of the Federal Reserve Act (U. S. C., title 12, sec. 264 (h) (1)), as amended, is hereby further amended by substituting a colon for the period at the end thereof and adding the following: "*And provided further*, That during the continuance of the present war and for six months after cessation of hostilities any balance payable to the United States by any insured bank, whether represented by a deposit account or otherwise, arising solely as a result of subscriptions made by or through such insured bank for United States Government securities issued under authority of the Second Liberty Bond Act, as amended, shall be excluded from the definition of 'deposit' for the purpose of determining the assessment base."

Sec. 2. That the last sentence of section 19 of the Federal Reserve Act (U. S. C., title 12, sec. 462a–1) be amended by substituting a colon for the period at the end thereof and by adding the following: "*Provided*, That during the continuance of the present war and for six months after its termination no deposit payable to the United States by any member bank arising solely as the result of subscriptions made by or through such member bank for United States Government securities issued under authority of the Second Liberty Bond Act, as amended. shall be subject to the reserve requirements of this section."

The Chairman. I call your attention to a discrepancy in the two sections of the bill in one particular. Under section 2 the act would be effective until the end of the war and for 6 months after the cessation of hostilities. Under section 1 of the bill, which relates to the matter of reserves, it would be effective during the continuance of the war and for 6 months after its termination.

I should imagine that the termination of the war would relate to an official declaration of the President declaring the end of the war, or an Act of Congress for that purpose; whereas, under section 2 the cessation of hostilities would be the guide.

We have with us Mr. Crowley, Chairman of the Federal Deposit Insurance Corporation. I am sure members of the committee will be

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glad to hear Mr. Crowley; and I am sure I am justified in saying that every member of the committee will listen to him with interest and with the highest regard for any views he may express.

Incidentally, I want to say here and now that I feel sure I speak not only for the members of this committee who have had frequent and intimate contact with Mr. Crowley during his service, but for the entire membership of the House, when I make the statement that I think he has made a most worthy and commendable record in the management of the Federal Deposit Insurance Corporation, and rendered a great service for the protection of the depositors, the stability of the banks, and of the national economy. [Applause.]

Mr. CROWLEY. We shall be glad to have you discuss the bill.

Mr. DILWEG. Mr. Chairman, may I say that he is an illustrious son of the State of Wisconsin.

Mr. STEAGALL. The State of Wisconsin has produced many illustrious sons, and there is an illustrious son of Wisconsin who honors us by his presence and his association with us as a member of this committee—in fact, we have two splendid sons of Wisconsin. I was addressing my remarks to the gentleman on my right, but they apply equally to the gentleman on my left, Mr. Hull, who is one of the most modest, but one of the most hard-working, conscientious, and valuable members of this committee and of the House.

Mr. Crowley, will you proceed?

STATEMENT OF HON. LEO T. CROWLEY, CHAIRMAN, FEDERAL DEPOSIT INSURANCE CORPORATION; ACCOMPANIED BY DONALD S. THOMPSON, CHIEF, DIVISION OF RESEARCH AND STATISTICS

Mr. CROWLEY. Mr. Chairman and members of the committee:

I appreciate, of course, Mr. Steagall, your kind remarks, and the confidence and the cooperation that the Federal Deposit Insurance Corporation have always had from this committee.

This bill, H. R. 1699, is a bill that we agreed to sponsor at the request of the Secretary of the Treasury. They feel that with all of the heavy financing that is coming along, especially the financing that may be necessary in April, they would like to have this bill enacted as promptly as possible.

This bill eliminates from our deposit assessment the deposits known as the war loan account. That is an account that may be set up in a bank, as an agency for the Treasury, for the subscription of war-loan bonds.

That account is to be used for the purchase of bonds by individual depositors, or by the banks' funds themselves. The balance remains in that account until the Treasury takes it out and puts it in their working balances.

The balance is withdrawn gradually so that on the average these war-loan accounts may remain in the banks possibly 60 days before you get the turn-over of those deposits into a working account and into the hands of individuals and business.

We anticipate that this bill will reduce the income, that the Insurance Corporation would collect by $2,500,000 to $3,500,000.

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We are, of course, reluctant to talk about a reduction in the deposit insurance income with the uncertainties that face us during the post-war period, but out capital and surplus at the end of this year will be upward of $700,000,000. Our income is running now—anticipated for this year—about $85,000,000 a year. So that we feel that if this will help to make a contribution to financing the war, and will get many of these smaller banks to take these war loan accounts, we are willing to sponsor this legislation in order to help the Treasury in their financing.

Substantially, that is the story. We have a lot of testimony we can submit here with reference to our income; with reference to what the figures show would be eliminated from it. We have the figures of losses of banks and insured banks since we started, which we would be very happy to go into with you, if you would like.

But we do want to sponsor and support the passage of this bill and we would like to have it passed out of this committee so that you can get it out in time for the April financing. That date is April 12.

As far as deposit insurance is concerned, we have been able, during the term of our existence, to set aside all of our income into surplus, and a large part of our income from investments. So that to date Deposit Insurance has a capital of $289,000,000 and a surplus of about $325,000,000.

We are adding to that surplus at the rate of about $70,000,000 to $75,000,000 a year.

If the losses over the period of the next 65 years were to be similar to those experienced since 1865, and we were to experience no recurrence of major banking crises, it would take about the income that we have now to take care of the losses. So for that reason we are reluctant to talk about giving up any further income for deposit insurance.

I think the thing that is most necessary in financing this war is that we continue to have the complete confidence of the depositors of this Nation, which we have now. Your banking system is in the best shape that it has ever been, asset-wise.

To illustrate that, let me refer you to page 7 of my prepared statement, which is in front of you.

The quality of the assets of the banks today is better than at any other time of record. Total assets of the banks were appraised by examiners at 99.8 percent of book value in 1942, compared with 99.4 percent in 1939 and probably not over 90 percent in 1933–34. Only 2.5 percent of the assets were considered to be substandard in 1942, compared with at least 25 percent in 1933–34. In 1942, more than 97 percent of the assets were not criticized; in 1933–34, less than two-thirds of the assets of the banks escaped criticism. The improvement has reflected in part the elimination of weak and insolvent banks, in part the charging off by operating banks of more than $4,000,000,000 of losses during the past 9 years, in part improvement in credit standing of debtors accompanying business recovery and rising income, and in part the acquisition by banks of a large volume of new assets consisting chiefly of United States Government obligations, cash and balances with other banks, and sound loans.

That is a very significant thing, to go into a war with your banks in that sound position. It is a real credit to your banking system.

During the period of Deposit Insurance, we had liquidated 390 insured banks with 1,260,000 depositors, with $485,000,000 in deposits, that were protected 97.8 percent; and the losses to depositors that were not insured were less than $3,000,000. The losses to us were about $50,000,000.

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There has been much talk on the Hill here about aid to small business. It would be interesting to study the record of the banking system and see how successful your little banks have been in carrying on, and how much money they have been able to make, and how they have been able to prosper, as against the small businessman, during this war. I think a lot of that is due to the policy of this committee in encouraging your small unit bank, and in encouraging your dual banking system. I think Deposit Insurance has made a real contribution to your small bank, because it has restored confidence and helped them in their local communities.

If we had been able to do something like that for your small businessman, it would have helped him materially during this period.

On page 5–A of my statement there is a table that shows the increase in deposits over a period of a great many years.

Mr. FORD. That 1942 figure of $77,200,000,000 of deposits, how much of that is reflected in Government bonds?

Mr. CROWLEY. About 46 percent, Mr. Chairman, that substantially is what I have to present. I would be very happy, of course, to answer any questions the committee would like to ask.

The CHAIRMAN. Mr. Wolcott desires to make some inquiries with respect to deposits that have some relation to matters which will arise in the debate on the tax bill which is now pending in the House, and I am going to recognize Mr. Wolcott now so that he may make such inquiries as he may desire. I do this in anticipation of the meeting of the House, and the necessity for members to be on hand in the House today because of the importance of the matter under consideration.

Mr. WOLCOTT. Mr. Crowley, do the banks pay the Government any interest on these war loan deposits?

Mr. CROWLEY. No, sir.

Mr. WOLCOTT. Can you give us the total amount of time and demand deposits in banks as of the most recent date which you have?

Mr. THOMPSON. These are partly estimated. The demand deposits of individuals, partnerships, and corporations, about $47,000,000,000.

Mr. WOLCOTT. Can you give me the total, Government and all?

Mr. THOMPSON. The total deposits, including mutual savings banks, are about $100,000,000,000.

Mr. WOLCOTT. $100,000,000,000?

Mr. THOMPSON. Yes, sir.

Mr. WOLCOTT. As of what date?

Mr. THOMPSON. December 31, 1942.

Mr. WOLCOTT. Will you break that down for us?

Mr. THOMPSON. Insured commercial banks, $88,000,000; noninsured commercial banks, about $1,500,000,000; insured mutual savings banks, $2,000,000,000.

The CHAIRMAN. What is that $1,500,000,000 figure?

Mr. CROWLEY. That is the amount of deposits in noninsured banks throughout the Nation.

Mr. THOMPSON. Those are the commercial banks.

Mr. SMITH. Did you say December 31?

Mr. THOMPSON. Yes, sir.

The CHAIRMAN. What is the number of noninsured commercial banks?

Mr. THOMPSON. A little under 1,000.

Insured mutual savings banks, $2,000,000,000.

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Noninsured mutual savings banks, between $8,500,000,000 and $9,000,000,000. Of the total deposits in all banks, $8,500,000,000 were to the credit of the United States Government.

Mr. WOLCOTT. Of the total of $100,000,000,000?

Mr. THOMPSON. Yes, sir.

Mr. WOLCOTT. And how much was that?

Mr. THOMPSON. $8,500,000,000, or which $8,000,000,000 were war loan accounts.

The total time deposits, including the time deposits in the commercial banks and the savings deposits in the mutual savings banks, are about $26,000,000,000.

Mr. WOLCOTT. The rest would be demand deposits?

Mr. THOMPSON. Of various classes; yes, sir.

Mr. WOLCOTT. How much of an increase has there been in deposits recently?

Mr. THOMPSON. I believe reporting member-bank individual deposits have increased since the first of the year about $4,000,000,000. That is due largely to the withdrawal by the Treasury of its war loan deposits and the spending of them. I do not have estimates of total deposits but they have increased slightly.

Mr. WOLCOTT. This increase of $4,000,000,000 is due to what; will you repeat that?

Mr. THOMPSON. It is due to the withdrawal by the Treasury of its war loan deposits and the spending of that money in war expenditures. That went into the deposits of individuals.

Mr. WOLCOTT. How much have the war loan accounts increased recently?

Mr. THOMPSON. They went up to a peak of slightly over $8,000,000,000 in connection with the December financing. They have now declined to around $3,000,000,000.

Mr. WOLCOTT. On page 5–A of your statement, you anticipate that in 1944 the deposits of our commercial banks will reach $122,000,000,000.

Mr. THOMPSON. Yes, sir.

Mr. WOLCOTT. And 1945 they will reach $147,000,000,000; and at the end of 1945, $160,000,000,000.

To what do you attribute that increase?

Mr. THOMPSON. Largely to the purchase by the banks of United States Government securities.

Mr. WOLCOTT. Which means, in other language, spending by the Government?

Mr. THOMPSON. Yes, sir.

Mr. WOLCOTT. Will that money be available for the payment of private taxes?

Mr. THOMPSON. Of course, these resources or any resources can be converted into cash presumably to pay taxes, but it is not necessarily a part of the income of the individual.

Mr. WOLCOTT. To what do you attribute the increase in individual deposits?

Mr. THOMPSON. I beg your pardon?

Mr. WOLCOTT. To what do you attribute the increase of individual deposits?

Mr. THOMPSON. To expenditures by the Federal Government in war plants; expenditures by the war plants in the form of increased

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wages, distribution of dividends, payments for goods, the general processes of trade.

Mr. WOLCOTT. Do you know what percentage of these deposits are made up of cash reserves of, not only corporations, but individuals? I suppose it would be rather difficult to determine it with respect to individuals?

Mr. THOMPSON. Yes, sir.

Mr. CROWLEY. I think this, Mr. Wolcott: It is reasonable to assume that where corporations have large balances, to some extent that is cash accumulated out of depreciation reserves and things like that; because they are not able to use their depreciation account for improvements and expansion, and that naturally goes into cash. So that has a contributing effect toward liquidity of many concerns, like railroads, who cannot buy any new equipment.

Mr. WOLCOTT. It does not necessarily imply that the corporation or the individual has any more assets.

Mr. CROWLEY. It may be a liquidation of his capital.

Mr. WOLCOTT. What is that?

Mr. CROWLEY. It may be a liquidation of a part of his capital.

Mr. WOLCOTT. In other words, if a man is forced to sell his business and cannot buy another business, he takes the cash and puts it into the bank against the time when he can buy another business with that cash.

Mr. CROWLEY. If you had a large retail store, or a large jobbing house, and you could not replenish your merchandise, as you sold it off, you built your cash position up when you formerly used to invest the capital in merchandise.

Mr. WOLCOTT. As these business inventories decrease, there is a tendency for their cash resources——

Mr. CROWLEY. To become more liquid.

Mr. WOLCOTT. To increase, and that is reflected in deposits?

Mr. CROWLEY. That is right.

Mr. WOLCOTT. What I was trying to get at—and I wish you would comment upon it—is this: It has been contended by a great many members of Congress, including members of the Senate, that there is more cash available in deposits today for the payment of taxes than ever before. Do you want to comment upon that? Of course, I suppose that this cash, where you liquidate a business and put it in the form of cash, is available for the payment of taxes; but whether that is indicative of any increase in available resources or not is of interest to us.

Mr. CROWLEY. I think that naturally most of your concerns are more liquid than they have been in a long, long time. And when your volume of business increases and your turn-over is greater, naturally your cash position is always greater on account of the volume of business you do, and undoubtedly people have more cash than they ever had before, on account of the rise in wages, and things like that.

Mr. WOLCOTT. We have had an increase in currency in the last 10 years of about $10,000,000,000. Is much of that reflected in deposits in the banks?

Mr. CROWLEY. I would prefer to have the Federal Reserve answer that, because I think they make a better study of that than we do.

Mr. WOLCOTT. Do you have anything else you want to contribute to this general thought that might be helpful?

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Mr. CROWLEY. No, sir; I do not think so.

Mr. CRAWFORD. Mr. Crowley, suppose Mr. A has a stock of goods and accounts receivable, as of January 1, 1942; and as of January 1, 1943, he has liquidated that substantially. We will say in the first instance $100,000 and in the second instance, $25,000; that is he has gotten liquid to the extent of $75,000. It is in the form of demand deposits. Mr. B was not in business, but he has his accumulated savings over the years in the form of $75,000 demand deposits. Is there any reason, under our system, why Mr. A should be protected against the payment of Federal taxes any more than Mr. B?

Mr. CROWLEY. I do not understand that he is.

Mr. WOLCOTT. The question goes, I suppose, to the availability of this money with which to pay taxes.

Mr. CROWLEY. I think that a man who is in liquidation, or whose company is in liquidation naturally tends to accumulate cash during the course of liquidation. If he goes back and buys merchandise, he does not have the cash to pay taxes; I mean, his liquidity is gone.

Mr. CRAWFORD. Very well; my point is this: I do not propose to get confused with the idea that the fellow who liquidates his business should be so protected, so far as his tax position is concerned, that he can go in business when he gets ready, any more than the fellow should be protected who stays liquid all the time. Do you get the point?

Mr. CROWLEY. Yes, Mr. Crawford. If I liquidate my business and have $100,000 in cash, what tax would you want me to pay? I would have no income from the $100,000, if it was lying in the bank.

Mr. CRAWFORD. I should want you to be just as liable for Federal taxes as the fellow who was liquid all the time. In other words, I would not want you coming up and making an excuse to me that you could not use any of your cash for the purpose of paying Federal taxes because you wanted to save it so that you could go back into business some day. I am not meaning to say that you are recommending that to us.

Mr. CROWLEY. No, no.

Mr. CRAWFORD. But I am just developing the position of these two people who are in liquid positions by reason, in one case, of a fellow who stayed in a liquid position; he always was long on dollars; and the other fellow went long on inventory and receivables, and then later became short on those and went long on dollars.

My contention would be that any man today who has demand deposits to his credit is in a position to pay Federal taxes with that; especially if he has no liabilities. I do not care whether it is some fellow who liquidates his business or not.

Mr. CROWLEY. You are assuming that they both owe income taxes?

Mr. CRAWFORD. Surely; I am assuming that they both owe income taxes, and I am assuming that both are living under our system here in the United States, under present concepts and practices and commitments.

Mr. CROWLEY. But the man who is 100-percent liquid and has all of his assets in cash, does not have much of an income tax to pay because he has no income.

Mr. CRAWFORD. Let us assume that during the year 1942, for instance, he received $50,000.

Mr. CROWLEY. You mean as a profit?

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Mr. Crawford. No; as salary.

Mr. Crowley. I think he is in a position to pay his income tax the same as any other man, of course.

Mr. Crawford. Let us assume that the fellow who liquidated his inventory also made $50,000 on that liquidation in 1942. My contention is that one is just as subject to taxation and should be, justly so, as the other.

Mr. Crowley. We agree on that.

Mr. Wolcott. I want to make myself clear in that regard. The question in my mind was not as to whether there was enough cash available to pay income taxes; but what I was developing here is whether we were justified in raising the amount of income taxes, and predicating that increase of taxes upon an increase in deposits. I was trying to find out what these deposits represented; if they represented current earnings or if they represented the liquidation of assets. Now, if they represent the liquidation of assets, that does not necessarily imply that the man's income has increased or that he is in any better position to pay Federal taxes than he was before.

That is what I was trying to develop, because both sides of this question on the tax bill seem to be predicating at least part of their case upon the fact that because deposits in the banks have increased, people are in a better position to pay at a higher rate of income tax than they were before.

Mr. Wright. Is it not better to take the increase in national earnings over the year?

Mr. Wolcott. Yes.

The Chairman. It is evident that members of the committee desire to attend the session of the House, and I am going to suggest that gentlemen withhold further discussion of the bill until we have more time.

Mr. Kean. May I ask Mr. Crowley just one question?

The Chairman. Yes.

Mr. Kean. How do you handle, on your books, the question of assets which you have taken over and which may or may not be good? For instance, last year you saw certain photographs of certain properties in Jersey City which you had taken over from the banks, and on the photographs they did not look very good. Now, how do you carry those as assets?

Mr. Crowley. For instance, let us assume that we go in and consolidate a bank and we get $1,000,000 of assets.

Mr. Kean. Questionable assets.

Mr. Crowley. That is right. We appraise those assets on our own values, and we set that up on our books so that it is at the value at which we appraise it. In other words, we take our loss immediately.

Mr. Kean. You take your loss immediately. That is what you should do and I wanted to know whether you did it.

Mr. Crowley. As a matter of fact, our reserves are far in excess of our losses on that.

Mr. Talle. Mr. Crowley, I believe you stated at the outset that the banking system is now in the best position it has been in during our history asset-wise. Will you comment on its condition incomewise?

Mr. Crowley. As to earnings of insured banks, their income is about $400,000,000 for last year, and I think their invested capital is

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about $7,000,000,000, so their earnings were very satisfactory last year.

Miss SUMNER. Was that after taxes, Mr. Crowley?

Mr. CROWLEY. Yes, Madam.

Mr. CRAWFORD. Mr. Crowley, was there a remark in your prepared statement to the effect that some 6 or 8 months after hostilities ceased, reserve requirements of banks will go up?

Mr. CROWLEY. No; what we said was that demands upon the banks would go up. We did not say anything about reserves.

Mr. MONRONEY. Mr. Chairman, why can we not report this bill now?

The CHAIRMAN. Of course, when it comes to reporting the bill, it is the wish of the committee and not the chairman that will rule, but I should assume that members of the committee will want an opportunity to discuss the bill and try to understand it.

Mr. WOLCOTT. Mr. Chairman, a couple of years ago, we gave consideration to a bill to reduce premium rates. I think there are three things to which we have got to give consideration—the maintenance of these reserves in the light of the recommendation that we might reduce premium rates; the effect of relieving the banks of the requirement that they pay premium on Government deposits, that is, whether that shall be denied them hereafter. Then there is another question which does not come to my mind right now, that affects this situation. There are three things we have got to consider before we report this bill out. We might want to amend this bill to cover some of those other points.

Mr. WRIGHT. May I ask one question, Mr. Chairman? Do you think it would be necessary or advisable to raise the premium rates in order to compensate for the loss which you are going to take on relieving these particular depositors?

Mr. CROWLEY. No, we do not anticipate anything like that.

Mr. WOLCOTT. The banks are all in favor of this, of course?

Mr. CROWLEY. That is right.

Mr. WOLCOTT. And they are also in favor of reducing the premium rates?

Mr. CROWLEY. Surely.

Mr. WOLCOTT. They cannot have their cake and eat it, too.

Mr. CROWLEY. That is right.

Mr. WOLCOTT. I think we should hear from the banks as to whether they want this or a reduction in premium rates.

Mr. FORD. To what extent will taking these deposits out from under the Federal Deposit Insurance Corporation affect reserves? You are also taking them out of reserves, too, are you not?

Mr. CROWLEY. That is right; you are taking the deposits out of the reserve requirements and relieving the assessment at the same time.

Mr. MONRONEY. Does the Government have any priority on the assets of failed banks for its own deposits?

Mr. CROWLEY. Yes; that is the thing that the Congressman was getting at, with respect to Government accounts. Our Government accounts are secured accounts with Government securities. I would be glad to talk to you about that later, because a lot of people seem to think that because that account is secured, there is no risk to the Federal Deposit Insurance Corporation; and that a secured account ought to be eliminated from our total base for assessment.

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As a matter of fact, you are taking the other peoples' assets, the war depositors' assets, to secure somebody else. And I have never understood why a public body should have their deposits secured any more than some person who had an account in there as a result of his sweat and work in producing the deposit. I have always felt that it was morally wrong to have secured deposits.

The CHAIRMAN. The committee will stand adjourned and, if practicable to meet on Monday, we will meet then.

(Whereupon the committee adjourned to meet on the call of the chairman.)

FEDERAL DEPOSIT INSURANCE CORPORATION

TESTIMONY BEFORE THE HOUSE COMMITTEE ON BANKING AND CURRENCY OF LEO T. CROWLEY, RE H. R. 1699, THURSDAY, MARCH 25, 1943

I am here to explain the position of the Federal Deposit Insurance Corporation with respect to the exemption of war loan deposits from insurance assessments, as proposed by H. R. 1699. Since the proposal to eliminate reserve requirements on war loan deposits (sec. 2 of the bill) affects the operations of the Federal Reserve System primarily, I prefer not to comment upon that phase of the bill.

War loan deposits.—A description of how the war loan deposit account operates may be useful in understanding the effect upon the banks of the elimination of the deposit insurance assessment on these deposits.

The war loan deposit account results from two types of transactions, each of which involves the sale of securities by the Treasury. The two transactions are the direct purchase of new issues by a bank and the purchase through a bank of new issues by an individual or firm. When the bank subscribes to a new issue it creates on its books a credit to the Treasury in a war loan deposit account. When an individual or firm buys through a bank he gives the bank a check. The bank charges the account of the individual or firm (thereby reducing that account) and credits the Treasury's war loan deposit account, increasing it correspondingly. The Treasury draws upon its war loan deposit account as it needs the money. The withdrawals are gradual and fairly regular over a period of time. When the Treasury withdraws money from a war loan deposit account and disburses it, the money goes back into the hands of bank customers, and deposits of individuals and business enterprises increase correspondingly.

Upon the securities which it buys the bank receives interest from the date of purchase and is prohibited by law from paying interest on the deposit owed to the Treasury. The average rate of interest received on securities purchased by the banks in 1942 was about 1 percent per annum. In effect, therefore, the banks pay on an installment basis with no down payments and no interest for securities upon which they average a return of 1 percent per annum; they also sell to customers for cash, securities for which they do not have to make immediate remittance to the Treasury. Put another way, after deducting insurance assessments of one-twelfth of 1 percent the banks receive a net income at the rate of about eleven-twelfths of 1 percent per annum on funds they have promised to loan, but haven't yet actually turned over, to the Treasury.

Effect of bill upon the Corporation and upon the banks.—Treasury borrowings for the fiscal year 1943 were estimated to amount to about $60 billion in the President's Budget. So long as the Treasury borrows at this rate, we estimate that war loan deposits in insured banks will probably average between $3 and $4 billion and that insurance assessments thereon would amount to between $2.5 and $3.5 million per year. The Corporation's income from assessments in 1942 was slightly over $55 million; for 1943, it will be about $70 million, according to our present estimates. Insured bank profits are currently running between $450 and $500 million after taxes. The financial effect upon either the banks or the Corporation of the elimination of assessments on war loan deposits does not appear to be very important. With the growth in deposits total assessments paid in future years will, of course, be larger in amount. Should deficit financing exceed $60 billion in a year the amount of the war loan deposits would probably be correspondingly higher. In addition, the amount will be affected by Treasury policy regarding (1) minimum balances, (2) frequency of borrowing, and (3) extent to which various issues may be paid for through the war loan deposit account.

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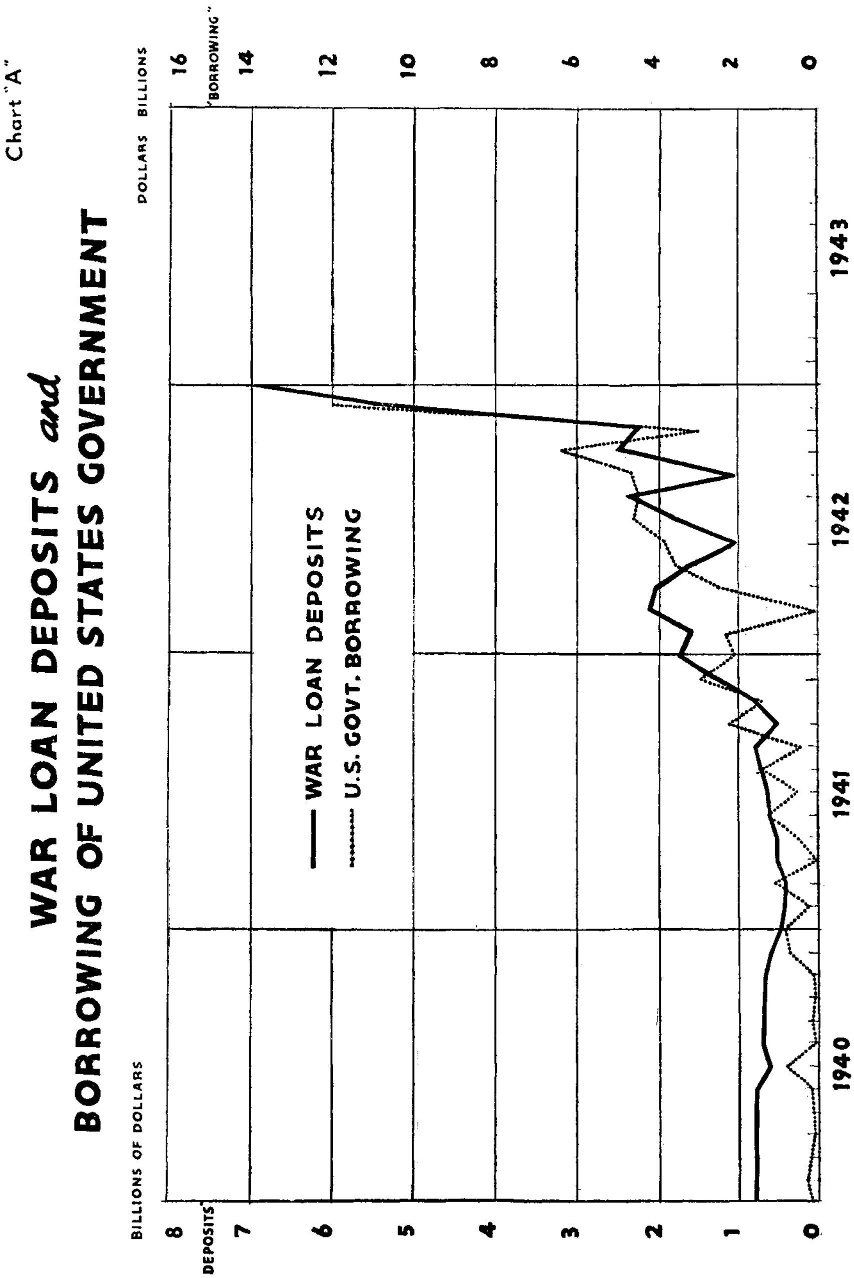
Chart "A"
WAR LOAN DEPOSITS and
BORROWING OF UNITED STATES GOVERNMENT
WAR LOAN DEPOSITS
U.S. GOVT. BORROWING
BILLIONS OF DOLLARS
"DEPOSITS"
8
7
6
5
4
3
2
1
0
DOLLARS BILLIONS
"BORROWING"
16
14
12
10
8
6
4
2
0
1940
1941
1942
1943

The chart (chart A) which I have here shows net monthly receipts of the Treasury on public debt transactions and average monthly balances in the war loan deposit accounts from January 1940 to January 1943, inclusive. The data are presented in table 1. The net monthly receipts are plotted on a scale which is double that used for the deposit balances, because in 1941 and 1942 (as the chart shows) the Treasury's net monthly public debt receipts were about double the average amount of war loan deposits. It is on this basis that we have estimated the effect of this bill (H. R. 1699) upon the banks and the Corporation.

TABLE 1.—*War loan deposits and Treasury net borrowings, monthly, 1940–43*

[In millions of dollars]

Month	1940		1941		1942		1943	
	War loan deposits [1]	Treasury borrowings [2]	War loan deposits [1]	Treasury borrowings [2]	War loan deposits [1]	Treasury borrowings [2]	War loan deposits [1]	Treasury borrowings
January	819	167	506	852	1,787	2,074	7,030	2,899
February	816	256	478	213	1,658	2,369		
March	815	175	475	1,083	2,162	39		
April	814	118	554	58	2,079	2,542		
May	813	150	552	490	1,690	3,609		
June	811	160	652	1,241	1,077	3,852		
July	653	803	672	551	1,833	4,714		
August	718	135	751	1,408	2,459	4,549		
September	716	168	828	425	1,167	4,798		
October	714	64	578	2,238	2,569	6,420		
November	712	136	845	1,456	2,320	3,212		
December	625	752	1,345	2,898	5,537	12,054		

[1] Daily average of special deposits on account of sales of Government securities.
[2] Monthly excess of public debt receipts over expenditures.

The exemption of war loan deposits from the assessment and from reserve requirements will practically eliminate the cost of handling such deposits. As a consequence, war loan deposits will be very profitable accounts.

The Corporation supports the bill as a war measure.—We have been told that many bankers have made representations to the Treasury to the effect that they are loath to participate in the handling of war loan deposits because of our assessment of one-twelfth of 1 percent per annum. As a consequence, the Treasury has requested this exemption as a war measure to facilitate war financing. The exemption is to be effective only for the duration of the war and for 6 months thereafter and we approve the provisions of the pending bill, strictly as a war measure.

The Corporation does not consider other reduction or exemption advisable.—We do not consider advisable any other reduction in the assessment whatsoever, nor the exemption from assessment of any other class or type of deposit. Our reasons are set forth below.

Losses versus assessments.—We have no assurance that the present rate of assessment is adequate to meet future needs. From 1865 to 1940, losses to depositors in closed banks would have averaged one-fifth of 1 percent per annum of deposits in all commercial banks if, as has been the case in recent years, there had been no stockholders' double liability throughout the period. Those losses are more than double the present rate of assessment. Had there been no major post-war adjustments and no major banking crises during that 76-year period, the rate of loss would have been just about equal to our present rate of assessment.

The favorable experience of the Corporation over the past 9 years is characteristic of similar periods of recovery from major banking crises. This is brought out by the accompanying chart (chart B). The supporting figures are presented in table 2. The chart shows that if a deposit insurance fund had been established at the close of the Civil War with the same rate of assessment and the same capital in relation to deposits, and the same relative borrowing power as the Federal Deposit Insurance Corporation, it would have enjoyed a favorable record in early years but would have become insolvent in 1877. Reestablished in 1880, the fund again would have enjoyed an early favorable record but would have become insolvent again in 1893. Reestablished in 1898, once more it would have enjoyed an early favorable record but would have become insolvent for the third time in 1930. The banking collapse of 1933 would have removed any hope of restoring solvency to the insurance fund.

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Chart "B"

TOTAL RESOURCES OF DEPOSIT INSURANCE FUNDS WITH CAPITAL-ASSESSMENTS OF 1/12 OF 1 PERCENT

As percent of total deposits in all commercial banks

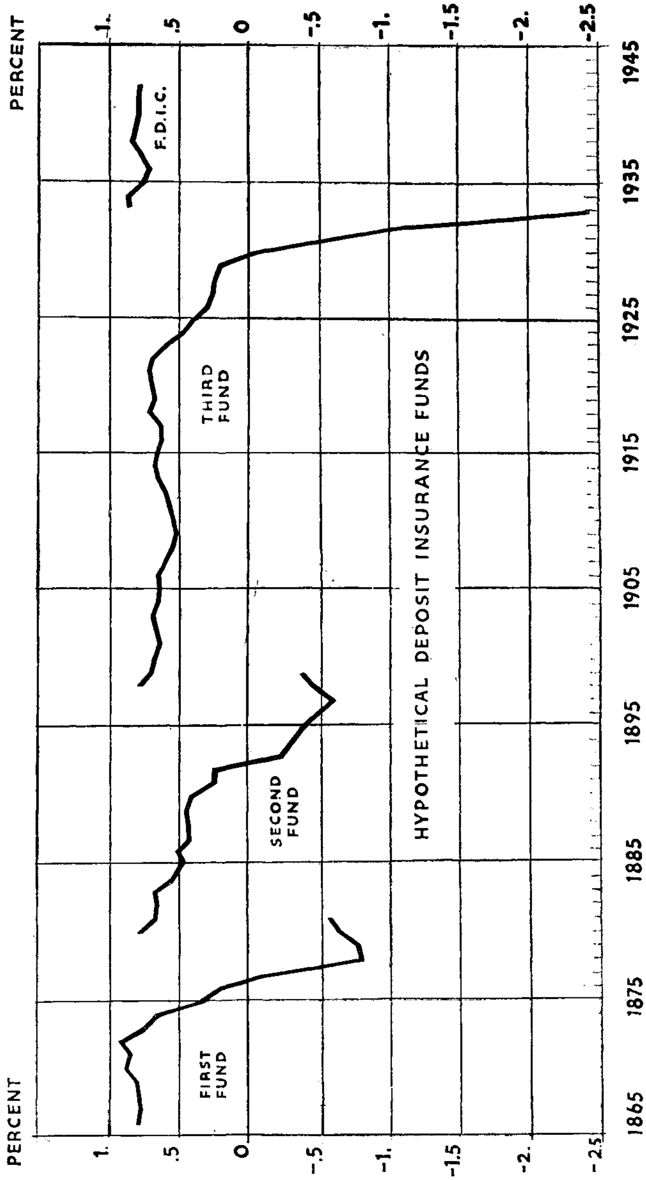

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TABLE 2.—*Total resources of hypothetical deposit insurance funds, 1865–1933, and of Federal Deposit Insurance Corporation*

Year ending—	Total resources: In thousands of dollars	Total resources: As percent of bank deposits [1]	Year ending—	Total resources: In thousands of dollars	Total resources: As percent of bank deposits [1]
1865	7,225	1.07	1874	8,798	0.66
1866	7,321	.79	1875	4,902	.37
1867	7,623	.78	1876	2,773	.21
1868	8,548	.80	1877	−1,283	−.10
1869	9,582	.81	1878	−9,418	−.78
1870	10,822	.89	1879	−10,962	−.75
1871	11,108	.85	1880	−11,036	−.64
1872	11,376	.93	1881	−11,418	−.55
1873	9,153	.76			
NEW FUND STARTED					
1880	13,621	0.79	1906	85,969	0.66
1881	14,226	.68	1907	79,727	.61
1882	14,354	.68	1908	75,165	.55
1883	15,285	.69	1909	79,427	.53
1884	11,655	.54	1910	86,515	.55
1885	11,325	.49	1911	95,790	.58
1886	12,857	.51	1912	107,691	.61
1887	12,958	.44	1913	119,300	.66
1888	14,045	.44	1914	128,698	.69
1889	16,162	.46	1915	140,107	.67
1890	15,910	.43	1916	160,700	.64
1891	10,011	.26	1917	184,757	.64
1892	10,736	.25	1918	211,135	.70
1893	−9,634	−.24	1919	242,411	.69
1894	−13,544	−.31	1920	263,298	.71
1895	−16,337	−.37	1921	249,309	.73
1896	−20,488	−.48	1922	250,203	.70
1897	−25,688	−.54	1923	232,159	.60
1898	−25,864	−.45	1924	202,056	.48
1899	−25,257	−.37	1925	185,916	.41
1898	44,280	.78	1926	150,956	.32
1899	47,693	.71	1927	135,367	.28
1900	52,054	.69	1928	133,175	.26
1901	56,721	.65	1929	105,114	.21
1902	63,258	.67	1930	−18,573	−.04
1903	70,046	.71	1931	−289,498	−.65
1904	71,970	.66	1932	−441,594	−1.20
1905	77,911	.65	1933	−812,753	−2.44
FEDERAL DEPOSIT INSURANCE CORPORATION					
1933	289,300	0.87	1938	421,622	0.85
1934	333,283	.89	1939	456,114	.83
1935	337,210	.79	1940	497,209	.81
1936	353,172	.73	1941	555,662	.81
1937	385,340	.79	1942	620,000	.80

[1] Total deposits of all commercial banks.

At the beginning of deposit insurance the Corporation's resources amounted to about 1 percent of total deposits of insured banks. Today our resources amount to about three-fourths of 1 percent of deposits. Three years from now, if present tendencies continue, the ratio will be even lower (two-thirds of 1 percent). Of course, a major part of the growth in deposits is being accompanied by a corresponding growth in bank holdings of Government securities and later will probably be accompanied by some increase in reserves.

In that connection I should like to show the committee this chart (chart C) which gives deposits of all commercial banks in the United States from 1865 to 1945, and our estimates of the volume of deposits for 1943, 1944, and 1945, if present financing tendencies continue. The supporting figures are given in table 3. The period from 1934 to 1942 is the period of operation of the Federal Deposit Insurance Corporation. Widespread failures and heavy losses ordinarily do not occur during such a period of recovery and growth, particularly following such a thorough housecleaning as took place in the period 1930–33. An intensive

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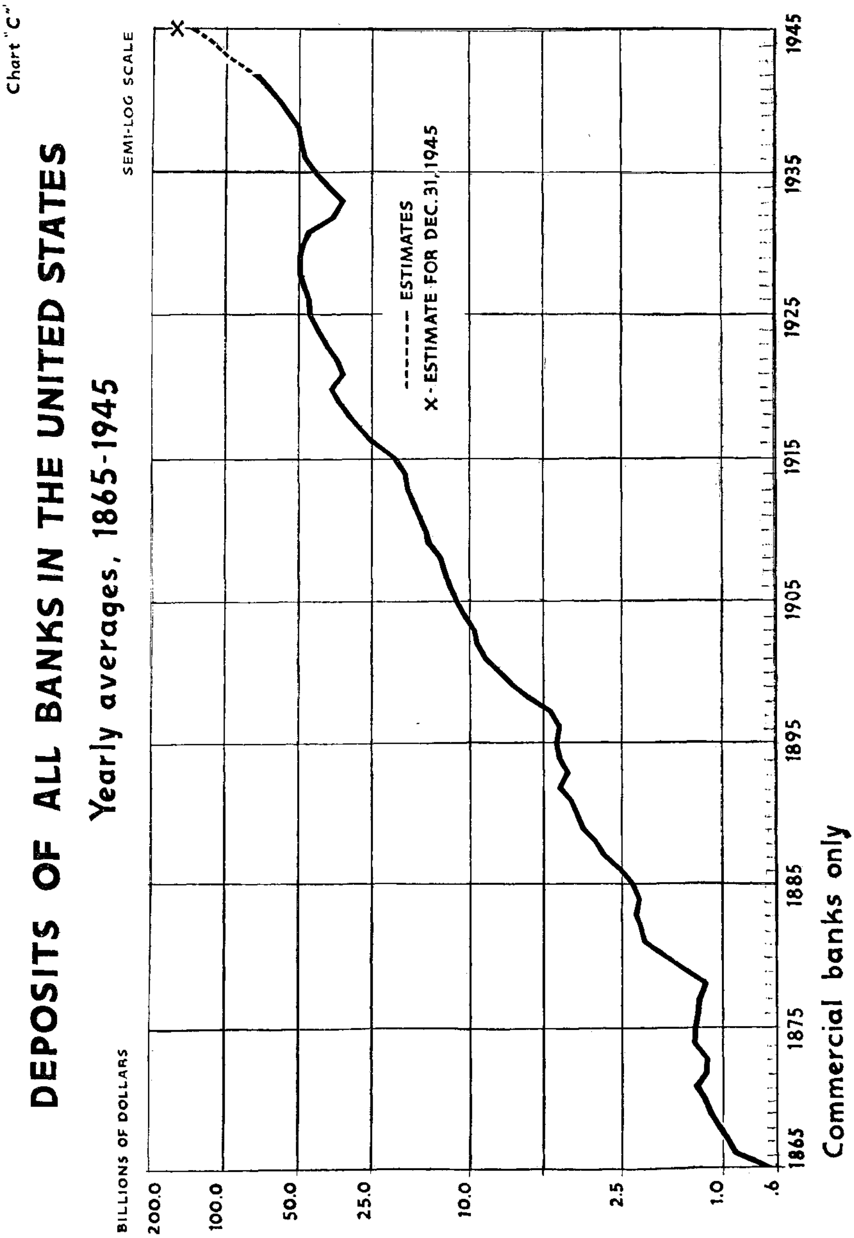

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program of rehabilitation was also undertaken by the Federal Deposit Insurance Corporation during the early years of its existence to further strengthen the banking system so that many banks were restored to health which might otherwise have become insolvent and been forced to suspend operations even during the period of recovery.

TABLE 3.—*Deposits of all commercial banks, 1865–1945; estimated average deposits by years*

	Amount		Amount
1865	$677, 000, 000	1906	$12, 946, 000, 000
1866	924, 000, 000	1907	13, 176, 000, 000
1867	980, 000, 000	1908	13, 713, 000, 000
1868	1, 068, 000, 000	1909	15, 004, 000, 000
1869	1, 181, 000, 000	1910	15, 730, 000, 000
1870	1, 217, 000, 000	1911	16, 605, 000, 000
1871	1, 302, 000, 000	1912	17, 515, 000, 000
1872	1, 218, 000, 000	1913	18, 041, 000, 000
1873	1, 211, 000, 000	1914	18, 695, 000, 000
1874	1, 336, 000, 000	1915	20, 972, 000, 000
1875	1, 343, 000, 000	1916	25, 242, 000, 000
1876	1, 300, 000, 000	1917	28, 752, 000, 000
1877	1, 297, 000, 000	1918	30, 254, 000, 000
1878	1, 214, 000, 000	1919	35, 171, 000, 000
1879	1, 458, 000, 000	1920	37, 301, 000, 000
1880	1, 727, 000, 000	1921	34, 011, 000, 000
1881	2, 078, 000, 000	1922	35, 891, 000, 000
1882	2, 125, 000, 000	1923	38, 430, 000, 000
1883	2, 202, 000, 000	1924	41, 776, 000, 000
1884	2, 176, 000, 000	1925	44, 808, 000, 000
1885	2, 299, 000, 000	1926	46, 475, 000, 000
1886	2, 534, 000, 000	1927	48, 397, 000, 000
1887	2, 930, 000, 000	1928	50, 293, 000, 000
1888	3, 169, 000, 000	1929	50, 398, 000, 000
1889	3, 533, 000, 000	1930	49, 489, 000, 000
1890	3, 713, 000, 000	1931	44, 687, 000, 000
1891	3, 924, 000, 000	1932	36, 668, 000, 000
1892	4, 365, 000, 000	1933	33, 252, 000, 000
1893	4, 070, 000, 000	1934	37, 482, 000, 000
1894	4, 303, 000, 000	1935	42, 796, 000, 000
1895	4, 412, 000, 000	1936	48, 125, 000, 000
1896	4, 313, 000, 000	1937	48, 932, 000, 000
1897	4, 791, 000, 000	1938	49, 345, 000, 000
1898	5, 699, 000, 000	1939	54, 912, 000, 000
1899	6, 743, 000, 000	1940	61, 371, 000, 000
1900	7, 576, 000, 000	1941	68, 614, 000, 000
1901	8, 749, 000, 000	1942	77, 200, 000, 000
1902	9, 429, 000, 000	1943 [1]	99, 000, 000, 000
1903	9, 876, 000, 000	1944 [1]	122, 000, 000, 000
1904	10, 939, 000, 000	1945 [1]	147, 000, 000, 000
1905	12, 069, 000, 000	1945 [1 2]	160, 000, 000, 000

[1] Estimate.
[2] Year end.

Protection of depositors in closed insured banks.—From the beginning of deposit insurance to December 31, 1942, 393 insured banks were closed because of financial difficulties. Of these, 3 were subsequently reopened or taken over by other insured banks, and 390, having 1,266,000 depositors with total deposits of $485,000,000, were liquidated or merged with the aid of loans from the Corporation. Deposits amounting to $474,000,000, or 97.8 percent of the total deposits in the 390 banks, were made available promptly without loss to the depositors. Only 1,966 of the 1,266,000 depositors, or less than one-fifth of 1 percent, held accounts in excess of $5,000 and were not fully protected by insurance, offset, preferment,

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pledge of security, or terms of the merger agreements. It is estimated that these depositors will lose less than $3,000,000, or about three-fifths of 1 percent of the deposits in these banks. The Corporation's losses are estimated at slightly under $50,000,000.

Deposits and losses in closed insured banks, 1934–42, inclusive

	Total	Merged	Placed in receivership
Number of banks	$390	$150	$240
Number of depositors	1,266,000	902,000	364,000
Amount of deposits	484,800,000	382,300,000	102,500,000
Amount of protected deposits	474,100,000	382,300,000	91,800,000
Amount of Corporation disbursements	250,900,000	169,700.000	81,200,000
Amount of estimated losses to—			
Federal Deposit Insurance Corporation	48,600,000	27,500,000	21,100,000
Depositors	2,800,000	None	2,800,000

Condition of banks today.—The quality of the assets of the banks today is better than at any other time of record. Total assets of the banks were appriased by examiners at 99.8 percent of book value in 1942, compared with 99.4 percent in 1939 and probably not over 90 percent in 1933–34. Only 2.5 percent of the assets were considered to be substandard in 1942, compared with at least 25 percent in 1933–34. In 1942, more than 97 percent of the assets were not criticized; in 1933–34, less than two-thirds of the assets of the banks escaped criticism. The improvement has reflected in part the elimination of weak and insolvent banks, in part the charging off by operating banks of more than $4,000,000,000 of losses during the past 9 years, in part improvement in credit standing of debtors accompanying business recovery and rising incomes, and in part the acquisition by banks of a large volume of new assets consisting chiefly of United States Government obligations, cash and balances with other banks, and sound loans.

With assets in excellent shape generally and reserves ample and flexible, the banks are able to support whatever financial program may be necessary to win the war.

Post-war banking adjustments.—When this war is over we again will turn our energies to peacetime pursuits. A tremendous problem of conversion will then face us. Business will require financing in order to convert and reequip factories and plants, to reopen channels of distribution and, most important of all, to permit the small independent businessman to reestablish his business. This financial responsibility will fall chiefly upon the banks. If our banking system is to continue to justify its existence it must be ready to meet this responsibility. Business may have to be financed without reduction in bank holdings of United States Government obligations. Deposits may increase further. We do not know what adjustments will be called for after the war but we do know that they will be beyond any scale contemplated before this war. With deposits greatly above present levels and demands for business accommodation piled on top of that, the only protection which bank depositors will have will lie in the character of assets held by the bank, in the bank's capital cushions—and in deposit insurance.

I should like to present to this committee another chart (chart D) which compares the capital accounts of national banks with their assets. Data for national banks are used in this instance because they are the best figures available over a long period of time. If figures for all banks, National and State, were used the story would be about the same. The figures are given in table 4. The lower curve shows the amount of capital accounts for each $100 of assets held by the banks; the upper curve shows the amount of capital accounts for each $100 of assets held in the form of loans, securities other than United States Government, and fixed and miscellaneous assets. In other words, "cash and Governments" have been eliminated. The chart shows that even after the elimination of "cash and Governments," capital ratios are now lower than at any previous time except during the period 1916 to 1932. The sequel to that period of bank credit expansion was the closing during 1921–33 of more than 2,700 national banks because of financial difficulties, with losses to depositors estimated at $480,000,000. The dotted line represents our best estimates as to what the ratios will be in 1943, 1944, and 1945.

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Chart "D"

CAPITAL RATIOS OF NATIONAL BANKS 1865 – 1945

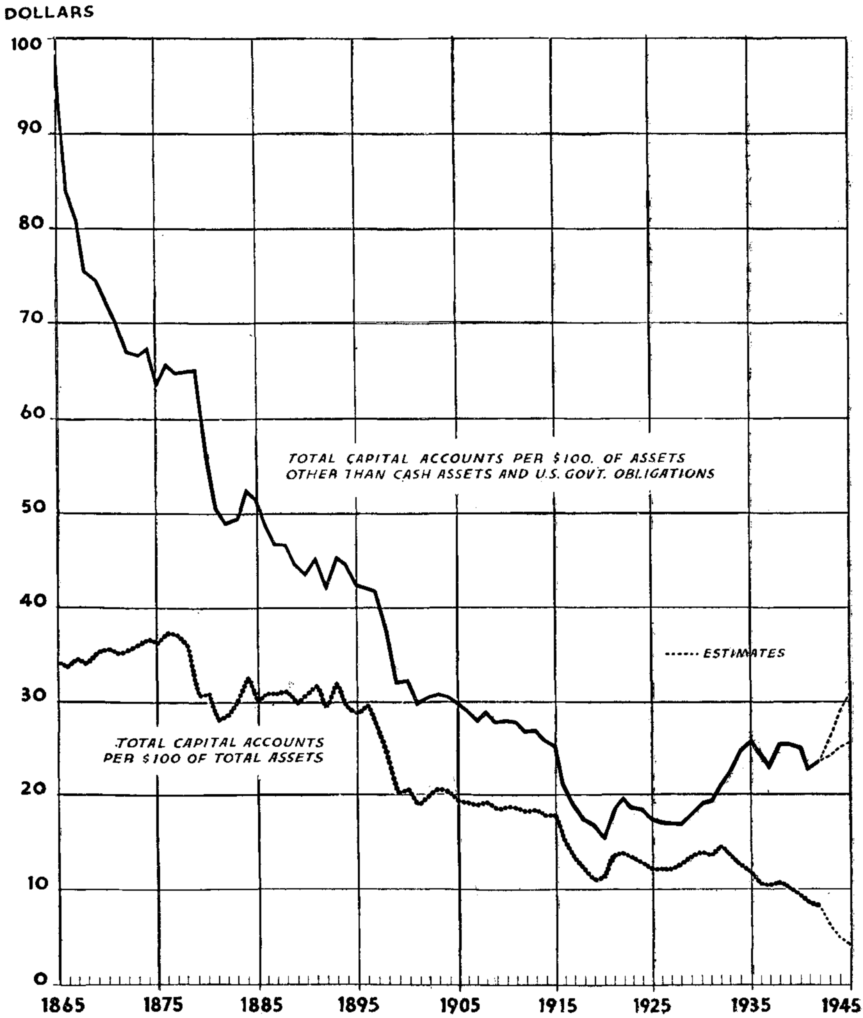

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TABLE 4.—*Total capital accounts per $100 of assets of national banks, 1865–1945*

June 30—	Total capital accounts per $100 of— Total assets	Selected assets [1]	June 30—	Total capital accounts per $100 of— Total assets	Selected assets [1]
1865	$33.76	$97.87	1906	$19.16	$28.96
1866	33.44	84.01	1907	18.92	27.99
1867	34.33	80.96	1908	19.14	28.91
1868	33.68	75.49	1909	18.41	27.87
1869	35.08	74.45	1910	18.70	27.90
1870	35.88	72.44	1911	18.62	27.72
1871	34.88	70.03	1912	18.27	26.81
1872	35.35	67.19	1913	18.53	26.83
1873	35.77	66.87	1914	17.85	25.79
1874	36.48	67.68	1915	17.85	25.22
1875	35.90	64.16	1916	15.10	21.31
1876	37.18	65.85	1917	13.50	19.11
1877	36.99	65.10	1918	12.26	17.64
1878	35.94	66.96	1919	11.13	17.01
1879	30.46	65.13	1920	11.27	15.76
1880	30.68	56.19	1921	13.65	18.61
1881	27.59	50.43	1922	13.80	19.74
1882	28.17	49.21	1923	13.40	18.99
1883	29.90	49.51	1924	12.94	18.66
1884	32.37	52.09	1925	12.24	17.51
1885	29.94	51.65	1926	12.25	17.21
1886	30.73	48.83	1927	12.24	17.05
1887	30.57	46.88	1928	12.63	17.19
1888	30.82	46.76	1929	13.47	18.20
1889	29.79	44.56	1930	13.77	19.21
1890	30.52	43.73	1931	13.67	19.54
1891	31.72	45.30	1932	14.67	21.13
1892	28.94	42.51	1933	13.70	22.48
1893	32.02	45.26	1934	12.56	24.60
1894	29.26	44.64	1935	11.85	25.69
1895	28.44	42.48	1936	10.66	24.60
1896	29.31	43.13	1937	10.59	23.39
1897	27.01	41.81	1938	10.78	25.30
1898	24.01	37.53	1939	10.22	25.42
1899	20.02	32.28	1940	9.43	25.02
1900	20.49	32.41	1941	8.71	22.98
1901	18.72	29.98	1942	8.23	23.78
1902	19.71	30.66	1943	[2] 6.10	[2 3] 26.00
1903	20.45	30.85	1944	[2] 5.10	[2 3] 29.00
1904	20.26	30.66	1945	[2] 4.30	[2 3] 31.00
1905	19.20	29.20			

[1] Loans, securities other than U. S. Government obligations, and fixed and miscellaneous assets.
[2] Estimated.
[3] These ratios assume a decline in the volume of loans, securities other than U. S. Government obligations, and fixed and miscellaneous assets. If these assets should not decline the ratios would be as follows: 1943, $24.80; 1944, $25.50; 1945, $26.20.

While many of the loans to industry for war purposes will be liquidated when the war is over, we may well expect many of them to be replaced by other loans with a consequent increase in the total volume of bank credit extended to private business. With their continually narrowing capital margins banks will be more vulnerable than formerly to shifts in economic fortunes. In that event, confidence in the banking system will depend almost wholly upon the integrity and soundness of the Federal Deposit Insurance Corporation.

Favorable outlook for bank earnings and profits.—The impact of the war has been felt in a very uneven number by the banks. Some have had an enormous growth of deposits and assets, some have had little growth, and some have even lost deposits. These disparities are the inevitable consequence of the profound adjustments required by war and impose difficult burdens upon some banks as well as on numerous other types of businesses.

Viewing the banks as a whole, however, earnings are increasing. While it is difficult to forecast all of the factors involved—such as the rate of return on Governments acquired, the changes in other sources of earnings, future expenses and charge-offs, recoveries, and taxes—we estimate that profits will increase sufficiently to cover increased taxes and that net profits after taxes for the banks as a whole will continue to range between $400,000,000 and $500,000,000. Thus the increased taxes of the banks will be paid for out of increased earnings rather than reduced profits.

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I have here another chart (chart E) which shows for national banks since 1890 and for insured commercial banks since 1934, the amount of profits, after taxes, earned on each $100 of total capital accounts, i. e., capital, surplus, undivided profits, and reserves. The figures for 1942 are estimates, while those for 1943, 1944, and 1945 probably should be called "guesstimates." Supporting figures are presented in table 5. The point of the chart is readily apparent. The banks can and, in the future, will be able to pay the present rate of assessment.

TABLE 5.—*Net profits per $100 of total capital accounts, national banks, 1890–1941,* [1] *insured commercial banks, 1934–45* [2]

NATIONAL BANKS

1890	$7.70	1909	$7.52	1928	$8.21
1891	7.68	1910	8.33	1929	7.78
1892	6.59	1911	8.12	1930	4.04
1893	6.69	1912	7.51	1931	−1.45
1894	4.19	1913	7.87	1932	−4.96
1895	4.75	1914	7.28	1933	−9.60
1896	5.06	1915	6.04	1934	−5.15
1897	4.60	1916	7.90	1935	5.14
1898	5.24	1917	9.12	1936	9.98
1899	5.73	1918	9.89	1937	7.11
1900	8.62	1919	10.44	1938	6.05
1901	7.70	1920	9.97	1939	7.44
1902	9.00	1921	6.48	1940	6.97
1903	8.55	1922	7.39	1941	7.49
1904	8.37	1923	6.73	1942	
1905	7.53	1924	7.36	1943	
1906	8.55	1925	8.22	1944	
1907	9.49	1926	7.96	1945	
1908	7.87	1927	7.91		

INSURED COMMERCIAL BANKS

1934	−$5.49	1938	$4.68	1942	[3] $5.87
1935	3.35	1939	5.99	1943	[3] 5.61
1936	8.35	1940	6.08	1944	[3] 6.12
1937	5.97	1941	6.72	1945	[3] 6.84

[1] For 1890–1915, net profits are for fiscal years and total capital accounts are as of June 30 or nearest available date; for 1916, net profits are for 18-month period ended December 31, 1916, adjusted to an annual basis, and total capital accounts are averages of figures for lune 30, 1915, June 30, 1916, and December 31, 1916; for 1917–41, net profits are for calendar years, and total capital accounts are averages of figures for call dates during the year.
[2] For 1934–41, net profits are for calendar years and total cpaital assounts are averages of figures for beginning, middle, and end of year.
[3] Estimated.

Summary and conclusion.—We support the proposal to exempt the War Loan Deposit from insurance assessment, solely as a war measure, in our desire to facilitate the Treasury's war financing. We consider inadvisable any other exemption, and any reduction in the rate of assessment at this time.

We face an unknown future. If past experience is any guide we can anticipate that in the post-war future American banking will face the most critical period of its entire existence. While there are comforting elements of strength in our situation we must not close our eyes to those elements of weakness which may arise.

One of the principal bulwarks of depositors' confidence is the deposit insurance system. Confidence in the banking system will be maintained so long as bank customers believe that the banks are kept sound through good management and supervision, and so long as they believe that the Federal Deposit Insurance Corporation is financially sound and properly administered. Loss of confidence would inevitably lead to hoarding on a scale greater than anything we have ever imagined, and to a deterioration in the banking structure of such a character as to require direct financial intervention of the Federal Government. Amid the popular outcry that would accompany such developments what would be the

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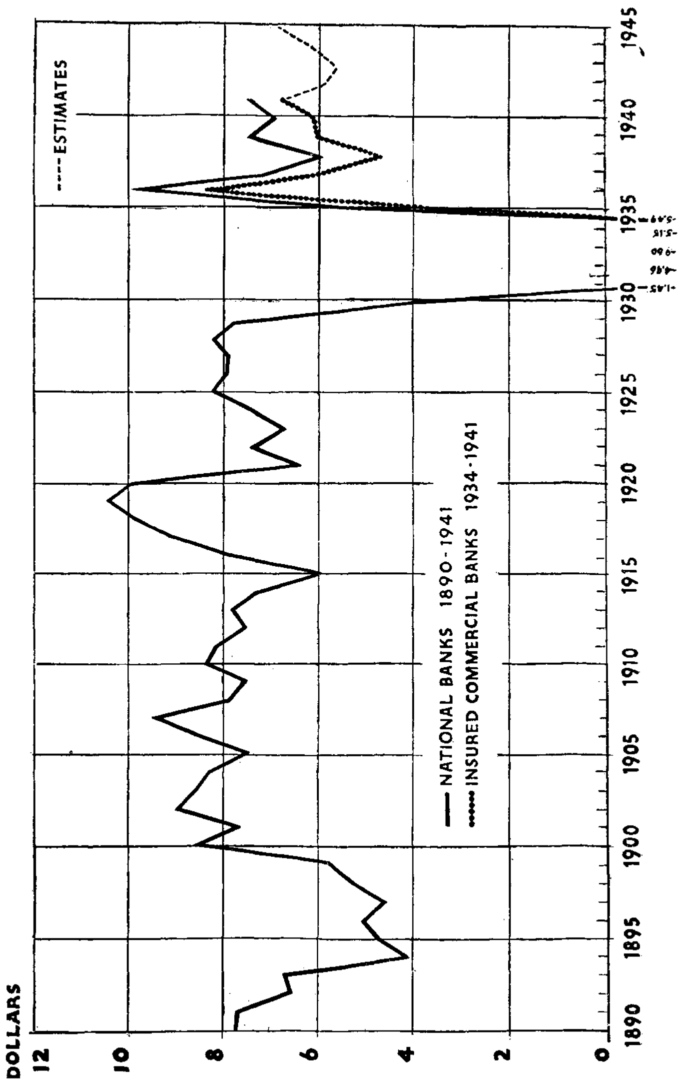
Chart "E"

PROFITS OF COMMERCIAL BANKS—PER $100 OF TOTAL CAPITAL ACCOUNTS



prospects for continuance of a system of privately owned banks which had claimed to be unable to support financially a deposit insurance system and had not made adequate provision for the risks of doing business although it had a record of sustained earnings and profits even after increased taxes?

Continuance of a system of privately owned banks is essential to the maintenance of the private business system which has contributed so much to the greatness of this country. The preservation of our banking system calls for wholehearted and intelligent participation in the war effort, for conservation of earnings and provision out of current earnings for losses, for strengthening of capital whenever possible, for farsightedness on the part of bankers and public officials concerned with banking, and for the maintenance of the Federal Deposit Insurance Corporation in as strong a financial position as possible. Not until we have completed our major post-war adjustments and have arrived at a comparatively stable post-war economy should we consider any reduction in the assessment rate or any further exemption of types of deposits from assessments.

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FEDERAL RESERVE ACT AMENDMENT

THURSDAY, APRIL 1, 1943

House of Representatives,
Committee on Banking and Currency,
Washington, D. C.

The committee met at 10:30 a. m., Hon. Henry B. Steagall (chairman) presiding.

The Chairman. The committee will please be in order. We will resume the hearings on H. R. 1699. We had not finished our discussions with Mr. Crowley.

STATEMENTS OF LEO T. CROWLEY, CHAIRMAN, FEDERAL DEPOSIT INSURANCE CORPORATION; AND DONALD S. THOMPSON, CHIEF, DIVISION OF RESEARCH AND STATISTICS—Con.

The Chairman. Mr. Crowley, I believe Mr. Wolcott desires to interrogate you further. Mr. Wolcott has not come in yet, but will be in soon.

I should like to ask you just what amount of insurance fees or assessments would you have to forego the collection of as a result of this bill?

Mr. Crowley. $2,500,000 to $3,500,000.

The Chairman. How do you arrive at those figures?

Mr. Crowley. Would you answer that, Mr. Thompson?

Mr. Thompson. We assumed that the war loan accounts would average about one-half of the average rate of borrowing of the Treasury. That is revealed by this chart which reflects the war loan accounts and the Treasury's monthly borrowings. The scale for the Treasury borrowings is double the scale for the war loan deposits, and that brings the two curves approximately together.

Assuming that the Treasury will run a deficit, as indicated in its budget, of approximately $60,000,000,000, we came out with a war-loan deposit account of around—I believe it was about three or four billion dollars. Of course, that account can vary by almost any amount, based on Treasury policy. The minimum below which the Treasury does not want to go, the frequency of Treasury borrowings, will all affect the amount in that account. But, on the basis of past experience, we assumed that it would run about $3,000,000,000 to $4,000,000,000, and that would make our assessments run anywhere from $2,500,000 to $3,000,000 or even $3,500,000.

The Chairman. If I understand the operations at present, the borrowings amount to approximately 50 percent of the funds raised?

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Mr. THOMPSON. I believe they have been around 40 to 50 percent; yes, sir.

The CHAIRMAN. Somewhere between 40 and 50 percent.

Mr. PATMAN. The last one was 45 percent, I believe.

The CHAIRMAN. And you base this calculation upon the assumption that this ratio will be maintained?

Mr. THOMPSON. No, sir. The payments may be made through the war loan account, if the Treasury so desires, whether or not the subscription is by the bank. If a customer goes to the bank and subscribes through the bank for an issue, the customer gives the bank the check, the bank charges the customer's account, and could then credit the Treasury war loan account. So that the amount in the war loan account would be determined, not solely by the amount that the bank loaned or borrowed, but by the amount of Treasury financing which the Treasury decided could be paid for through the war loan account device.

Mr. CROWLEY. What it does, Mr. Chairman, as I understand it, it makes this account a sort of an agency account in the purchase of this next issue that comes out. The funds from that will go into the war loan accounts, and until that money is put into the regular channels of the Treasury, that account is exempted from deposit insurance, whatever it may be.

The CHAIRMAN. But, does that cover subscriptions by individuals?

Mr. CROWLEY. That is right.

The CHAIRMAN. The same as by the bank?

Mr. CROWLEY. That is right.

The CHAIRMAN. That being the case, we are dealing here with the total borrowings of the Treasury rather than one-half of the borrowings?

Mr. CROWLEY. Let me put it to you this way. You are dealing with the total borrowings—it is a good deal as though we went down to the bank and we borrowed $100,000 to buy merchandise or to build a building, and check it out as the architect's certificate was issued. That account would be a dormant account for that particular purpose and would not be included in the assessment. It is an agency account that is not included. Just as soon as the Treasury checks out of that account, puts it into their general fund and spends it, then it becomes a part of our assessment.

The CHAIRMAN. Do you assume that the borrowings of the Treasury will remain on the same ratio in the future as it has up to this time?

Mr. CROWLEY. If they increase, this account will increase. On the other hand, while this account is increasing, as soon as they put it into trade, into the channels of defense, we will get some benefit when it is spent, by the increase in deposits.

The CHAIRMAN. Generally it will come back into the banks as regular deposits?

Mr. CROWLEY. That is right.

The CHAIRMAN. As a matter of fact, we do not have any right to assume that the borrowings of the Treasury will not be greater proportionately before this war is over, than they have been.

Mr. CROWLEY. We do not go on the theory but what they will be. But we do support the relief that is provided here because we think it will encourage many thousands of smaller banks to come in and take up a war loan account.

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The CHAIRMAN. As a matter of fact, we would not be safe in assuming that we know just to what extent the financing of this country may have to be done by borrowing?

Mr. CROWLEY. I think that is right.

The CHAIRMAN. Is not that a correct statement?

Mr. CROWLEY. That is right.

The CHAIRMAN. Of course, as the borrowings increase, and these Treasury accounts increase, the assessments upon those accounts for the benefit of the F. D. I. C. will be larger, under the operation of your proposed legislation than would be the amounts which you would have to forego?

Mr. CROWLEY. That is right.

The CHAIRMAN. For the benefit of the Corporation?

Mr. CROWLEY. That is right.

The CHAIRMAN. When it comes to that calculation, we do not have any very definite information?

Mr. CROWLEY. No. We took the Budget figures.

The CHAIRMAN. You took what?

Mr. CROWLEY. We took the Bureau of the Budget figures in determining what we thought this would relieve the banks.

The CHAIRMAN. What are the Budget figures? What do they figure?

Mr. THOMPSON. It is the estimates of the 1943 Budget, which ran to a deficit of $60,000,000,000 and on that basis we assumed that the war loan accounts would average between three and four billions. That is for the 1943 fiscal year.

The CHAIRMAN. The Budget does not go beyond 1943?

Mr. THOMPSON. That is right.

The CHAIRMAN. They have not any way of going beyond 1943, have they?

Mr. THOMPSON. No, sir. Our estimate is just for 1943.

The CHAIRMAN. Mr. Crowley, let me ask you this: What portion of the borrowings from the banks is taken care of by nonmember banks? Do you have those figures?

Mr. CROWLEY. You mean what are the loans of nonmember banks?

The CHAIRMAN. Yes.

Mr. CROWLEY. What are they, Mr. Thompson?

Mr. THOMPSON. Did you mean loans to businesses, the customers, or to the Federal Government?

The CHAIRMAN. I am talking about Government loans.

Mr. THOMPSON. Last June the nonmember insured banks held $1,650,000,000 of direct obligations. That has since increased, but I do not have the exact figures as yet.

The CHAIRMAN. That is June of last year?

Mr. THOMPSON. Yes, sir.

The CHAIRMAN. What were the total borrowings from banks at that time?

Mr. THOMPSON. $23,000,000,000. This is just insured banks.

The CHAIRMAN. Well, you do not have many banks that are not insured? Only about 1,000?

Mr. THOMPSON. Yes, sir.

Mr. SMITH. What were the indirect obligations held by the nonmember banks?

Mr. THOMPSON. $189,000,000.

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The CHAIRMAN. Have you any further break-down of these transactions with nonmember banks?

Mr. THOMPSON. Yes, sir. We have it broken down according to bills, certificates——

The CHAIRMAN. Let us have all those figures.

Mr. THOMPSON. The nonmember banks held $27,000,000 of Treasury bills; $1,375,000,000 of Treasury notes; $106,000,000 of certificates of indebtedness; and $186,000,000 of Treasury notes, and $1,330,000,000 of bonds.

The CHAIRMAN. Have you any further break-down of those figures?

Mr. THOMPSON. No, sir.

The CHAIRMAN. By districts, or otherwise?

Mr. THOMPSON. We have them by States.

The CHAIRMAN. Let us see how they run by States.

Mr. THOMPSON. Alabama: The direct obligations were——

The CHAIRMAN. Give us the total for Alabama; it is not necessary to break that down.

Mr. THOMPSON. $5,500,000 direct obligations.

The CHAIRMAN. Let us see what proportion goes to the money centers. That is really what I want to know.

Mr. THOMPSON. We are talking now just of nonmember banks, or did you want all banks?

The CHAIRMAN. Nonmember banks.

Mr. THOMPSON. In Illinois, the nonmember banks held $78,000,000. In New York, the nonmember banks held $180,000,000. Pennsylvania, $202,000,000; Ohio, $68,000,000; New Jersey, $111,000,000; Michigan, $46,000,000; Minnesota, $42,000,000; Missouri, $56,000,000.

Mr. SMITH. I wonder if they have the figures with respect to Federal Reserve districts?

The CHAIRMAN. I am coming to that in a moment. What about Massachusetts?

Mr. THOMPSON. $50,000,000.

The CHAIRMAN. And Connecticut?

Mr. THOMPSON. Maryland, $41,000,000.

Mr. CHAIRMAN. How about Connecticut?

Mr. THOMPSON. $63,000,000.

The CHAIRMAN. California?

Mr. THOMPSON. $137,000,000.

The CHAIRMAN. All the other borrowings are in Federal Reserve member banks. Give us the break-down of those figures by districts.

Mr. THOMPSON. In June the member banks held $21,413,000,000 of direct obligations.

The CHAIRMAN. Give us the break-down by districts.

Mr. THOMPSON. Boston, $1,114,000,000; New York, $8,746,000,000; Philadelphia, $1,064,000,000; Cleveland, $1,718,000,000; Richmond, $823,000,000; Atlanta, $594,000,000; Chicago, $3,414,000,000; St. Louis, $651,000,000; Minneapolis, $416,000,000; Kansas City, $509,000,000; Dallas, $441,000,000; and San Francisco, $1,923,000,000. Those are the direct obligations only.

The CHAIRMAN. The other obligations so far as proportions go correspond very well to that; do they not?

Mr. THOMPSON. Yes, sir.

The CHAIRMAN. Mr. Crowley, I do not know whether the members all fully understand the mechanics of these opreations between the

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Treasury and the banks. Tell us what they are, just how the transaction is conducted.

Mr. Thompson. With respect to the war loan account?

The Chairman. Yes.

Mr. Thompson. The bank subscribes to the new issue and upon receiving a notice of the allotment, credits the Treasury in a war loan account with the amount due on the allotment. The account remains in the bank until the Treasury withdraws it, which it does in accordance with a pretty generally understood schedule.

Then calls are made upon all banks proportionately. The Treasury will issue a call for 10 percent of the balance, or 9 percent of the balance, as the case may be, from time to time.

The Chairman. You say that these credits are placed to the Government account when the allotments are made known to the banks. Just how is that done?

Mr. Thompson. I am sorry, I do not know the precise mechanics.

The Chairman. Just what is the rule with respect to these allotments to the banks as to changes of allotments? What do you mean by that?

Mr. Thompson. I believe generally a certain minimum amount is always allotted in full and the rest is cut down proportionately in accordance with the amount of the issues available for the subscriptions that have been made. These issues are generally oversubscribed. That is handled by the Federal Reserve banks and so I imagine that Governor Eccles could probably detail that.

The Chairman. Mr. Crowley, let me ask you this question: You approve this bill?

Mr. Crowley. Yes, sir.

The Chairman. It has what you might call an interdepartmental support?

Mr. Crowley. That is right.

The Chairman. Consisting of the Treasury, the Federal Reserve, and the F. D. I. C.?

Mr. Crowley. That is right, sir.

The Chairman. Of course, you did not originate the legislation?

Mr. Crowley. No; the Treasury really originated it.

The Chairman. They regard it as helpful to the war program?

Mr. Crowley. That is correct.

The Chairman. Has the bill the approval of the President?

Mr. Crowley. No; I do not think a bill of this character necessarily is ever discussed with the President. I know I never discussed it with him.

Mr. Eccles. It cleared the Budget.

Mr. Crowley. Yes; it was cleared by the Budget.

The Chairman. You do not know whether the President approves it or not?

Mr. Crowley. No; because I do not think it is customary to take up this kind of legislation with him.

The Chairman. I was thinking about this in connection with another bill that was under consideration by this committee at one time, which the committee approved, and we found out later that it did not have the approval necessary at the time to pass the legislation. I am wondering if this interdepartmental comity that seems to exist at this time—and which I commend—obtains reciprocally among the three departments that have approved this legislation.

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Mr. Crowley. There is no disagreement at all on this legislation. I think it is fair to assume that we have all had our opinions on legislation in the past, and perhaps sometimes we had some things in our mind that the rest of them did not approve, and at other times some of the rest of them had some things in their minds we did not approve.

The Chairman. As a general thing, when one department determines upon a policy, or a course of action, and it relates solely to that department, the other departments as a matter of courtesy or comity acquiesce; it not that true?

Mr. Crowley. For instance, on this reduction in assessment, while the other agencies have an interest in the board principle, I think we are the ones that are affected by this reduction, just as the Federal Reserve are on the reserve requirements. My attitude on legislation that does not affect the general banking system, for instance—on Mr. Eccles' or Mr. Ransom's legislation pertaining to their own establishment—we have always kept our hands off. But where it affects the general banking system and is a general policy, then we have met and we have had our disagreements and, also, we have agreed lots of times

The Chairman. You remember the legislation to which I refer, that was approved at one time by this committee, which had to do with the reduction of assessments against depositors and authorization for a building.

Mr. Crowley. I think there was a little job done on us at that time, if that is what you refer to.

The Chairman. That had to do with deposit assessments solely and some other matters relating to the operations of the F. D. I. C.

Mr. Crowley. We have to be a little bit careful. We have accumulated a little fortune here, and when you get rich, everyone wants to visit you and the thing we have to be careful of is that we do not take on a lot of relatives while we have this capital surplus.

The Chairman. As a matter of fact, the other departments did not go along with you, with respect to the bill of which I am speaking.

Mr. Crowley. That is right, but let us be fair——

The Chairman. I am wondering, since this happy situation exists, if we might not expect in the future that the courtesies will be reciprocal.

Mr. Crowley. I assume that is right, but I do not think you can have characters such as you have in all three agencies without having opinions of their own.

The Chairman. Of course, this particular legislation is a matter of concern to all these departments.

Mr. Crowley. That is right. This is something that affects the general welfare.

The Chairman. I recognize that. That is undoubtedly true.

Mr. Crowley, I do not remember at the moment just how far you had gotten with your statement the other morning; we were in so much confusion here and going so fast that we did not get very far, as a matter of fact. So I am wondering if it would not be well for you to state now—it would not hurt to refresh our minds on it for the moment—what the condition of your account is at the moment, your assets and liabilities and losses.

Mr. Crowley. We have United States Government securities of $538,000,000. We have cash of $17,000,000. We have assets acquired through bank suspensions and mergers of $60,000,000.

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You asked the other day about those assets. They have been reduced down to what we consider a very sound market value. That makes a total of $615,000,000. So that our capital is $290,000,000 and our surplus is $325,000,000.

Our annual income from investments is running about $13,500,000 a year. The income from assessments last year was $56,500,000, making a total of $70,000,000 income.

The administrative expense was $3,600,000, and the deposit insurance losses were $3,400,000, making a total of $7,000,000.

The CHAIRMAN. What period do those losses cover?

Mr. CROWLEY. The $3,400,000 is for 1943. Our losses for the entire period are estimated at about $50,000,000.

The CHAIRMAN. That is what I want to make plain.

Mr. CROWLEY. The total assessments paid in from the beginning were $319,000,000. We have appreciation in our bond account of $15,000,000.

The CHAIRMAN. How much increase do you anticipate this year in your income as against last year?

Mr. CROWLEY. Up to $70,000,000 on assessments.

The CHAIRMAN. On assessments alone?

Mr. CROWLEY. That is right. Then our income from investments will go up to about $15,000,000 from $13,500,000.

The CHAIRMAN. So that your income will run up to about $85,000,000?

Mr. CROWLEY. That is right.

The CHAIRMAN. You still have the right to borrow of the Reconstruction Finance Corporation?

Mr. CROWLEY. And also from the Treasury.

The CHAIRMAN. And from the Treasury?

Mr. CROWLEY. That is right.

The CHAIRMAN. You have never exercised those rights, of course?

Mr. CROWLEY. Oh, no. We can borrow about $980,000,000; up to that.

The CHAIRMAN. The fact is, however, that while the right to borrow might become valuable in case of emergency, as a matter of fact, in case you borrowed, it would after all represent a liability of the Corporation?

Mr. CROWLEY. That is right.

The CHAIRMAN. How much do you think the Corporation should have to constitute such a dignified, practical sum as not only to command confidence—one that you would regard as sufficient reasonably to assure the public that any contingency that may reasonably be expected would be taken care of in the years that lie ahead?

Mr. CROWLEY. I do not think, Congressman, that anyone could answer that question definitely, because I think the longer the war goes on the greater the demand will be on the banking system when it is over. Consequently, there is no way of knowing what demands may be made on Federal deposit insurance. I would just like to go back a little bit on deposit-insurance assessment. When it was determined that we would have the right to assess up to one-twelfth of 1 percent, you will recall back in the Banking Act of 1933, there were certain changes made in the banking laws that were very beneficial to the banking system, such as interest on demand deposits and the regulation of interest on time deposits; and that more than offset to the banking system the cost of deposit insurance.

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It was always understood, according to the way I understood it, that that was done by the Congress to help to offset the assessment of deposit insurance, and that that assessment was not to be passed on to the depositors, but that was something that had to be paid by the banks themselves.

The CHAIRMAN. Let me ask you right there, what is the best estimate you can give of the amount that would represent the relief that was extended the banks because of the provision which prevented the payment of interest on deposits?

Mr. CROWLEY. You mean at the time the legislation was enacted? You see, new deposits have grown enormously since then, but the amount saved at that time was—how much was it, Mr. Thompson? We can get it and put it in the record.

Mr. PATMAN. About $250,000,000.

Mr. CROWLEY. My impression was it was $160,000,000 but we can look it up and put the right figure in.

Mr. PATMAN. The figures were put in the record at one time?

Mr. CROWLEY. That is right.

Mr. PATMAN. It was brought out that there were from $300,000,000 to $500,000,000 a year in reductions in time deposits, something like that.

Mr. CROWLEY. I realize that with the inflation of deposits, our income is going up. But I would be very reluctant to advocate any change in our assessment during this period. The banks are making money. These deposits are available to them to put into Governments and with our uncertainties I think it would be a great mistake, and the people might misunderstand, if we were to tinker with deposit-insurance income at this time. And certainly there is no better time to try to build your reserves for the future than now.

Mr. WRIGHT. Your contingent liabilities increase at the same time that your assets are increasing?

Mr. CROWLEY. That is correct, sir.

Mr. MONRONEY. How much have your deposit liabilities increased?

Mr. CROWLEY. Our deposits have gone up in a year from $69,000,000,000 to $88,000,000,000.

Mr. THOMPSON. They have gone up from $69,000,000,000 at the end of 1941 to $88,000,000,000 at the end of 1942.

The CHAIRMAN. Can we not bring that down a little closer? What are they now—approximately?

Mr. THOMPSON. They have increased, but I do not have an estimate.

The CHAIRMAN. What is the period covered in that increase from $69,000,000,000 to $88,000,000,000?

Mr. THOMPSON. 1942.

The CHAIRMAN. During the year 1942?

Mr. THOMPSON. Yes, sir.

The CHAIRMAN. What would those deposits amount to during 1943, would you say?

Mr. THOMPSON. I really do not know.

The CHAIRMAN. I know you do not know exactly, but you have a judgment about it?

Mr. THOMPSON. If I must hazard a guess, I would say probably about $2,000,000,000.

The CHAIRMAN. An increase of $2,000,000,000 during the year 1943?

Mr. THOMPSON. Yes, sir; so far.

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The CHAIRMAN. I am not talking about "so far." I am talking about the entire year. How much do you estimate will be the increase during this year?

Mr. THOMPSON. I would estimate between 20 and 25 billion; I am sorry, I misunderstood you.

The CHAIRMAN. So it would run considerably over $100,000,000,000 for this year?

Mr. THOMPSON. Yes, sir.

The CHAIRMAN. I thought the figure would be something like that. Mr. Wolcott suggests that I ask what portion of your liabilities would be reduced by reason of this legislation?

Mr. CROWLEY. What proportion of what?

The CHAIRMAN. Of your liabilities would be reduced by reason of this legislation.

Mr. CROWLEY. No reduction in liabilities at all.

The CHAIRMAN. That is what I understood to be the fact.

What about the earnings of banks? How much of an improvement have we had there? Give us the figures on that, please.

Mr. THOMPSON. The profits after income taxes for 1942 we estimate will be around $400,000,000. That compares with $455,000,000 in 1941.

The CHAIRMAN. How is that?

Mr. THOMPSON. In 1942 the net profits of banks will be around $400,000,000.

The CHAIRMAN. Which banks are you referring to?

Mr. THOMPSON. All insured banks.

The CHAIRMAN. I want to make that clear.

Mr. THOMPSON. All insured banks.

The CHAIRMAN. And what were they in 1941?

Mr. THOMPSON. $455,000,000. That is after taxes.

The CHAIRMAN. Net profits?

Mr. THOMPSON. Yes, sir.

The CHAIRMAN. How would you estimate those figures for 1943?

Mr. THOMPSON. At around $400,000,000, after taxes.

Mr. CRAWFORD. As of today's taxes you mean?

Mr. THOMPSON. Yes, sir.

The CHAIRMAN. Give us some figures that will show the change during recent years with respect to the earnings of banks.

Mr. THOMPSON. In 1935 net profits after taxes were $207,000,000 and in 1936, $524,000,000. That was due to a tremendous volume of profit-taking on bonds. You will recall that we had a rising bond market at that time.

In 1937 it was $381,000,000.

In 1938 the net profits after taxes were $300,000,000; in 1939, they were $388,000,000; and in 1940, they were $401,000,000.

Mr. CRAWFORD. Will you permit me to ask a question there?

The CHAIRMAN. Yes.

Mr. CRAWFORD. If you can do so, would you mind putting in the record at that point a break-down of two items; as to the profits from operations and the nonoperating profits—if I make myself clear?

Mr. THOMPSON. Yes, sir; we can do that.

(The matter referred to is as follows:)

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Earnings, expenses, and distribution of profits of insured commercial banks, 1934–45 (based on published figures for 1934–41; estimates for 1942–45)

[Amounts in millions of dollars]

	1934	1935	1936	1937	1938	1939	1940	1941	1942	1943	1944	1945
Income from loans	690	643	663	710	705	727	769	848	835	750	680	640
Interest on U. S. Government securities	550	548	574	572	532	522	[1] 284	[1] 304	404	666	925	1,178
Interest and dividends on other securities							[1] 216	[1] 205	205	195	189	180
Commissions, fees, collection, exchange, and service charges	76	90	105	111	115	121	129	140	149	160	170	180
Other current operating earnings	202	205	225	241	232	235	233	233	227	226	226	226
Total current operating earnings	1,518	1,486	1,567	1,634	1,584	1,605	1,631	1,730	1,820	1,997	2,190	2,404
Interest on time and savings deposits	303	262	237	235	230	215	201	190	173	165	157	157
Salaries, wages, and fees	402	411	437	463	473	484	498	527	566	622	652	684
Taxes other than on income [2]	74	74	86	97	93	95	100	103	103	103	103	103
Other current operating expenses	335	331	354	361	352	354	371	396	416	441	463	486
Total current operating expenses	1,114	1,078	1,114	1,156	1,148	1,148	1,170	1,216	1,258	1,331	1,375	1,430
Net current operating earnings (before income taxes) (operating profit before income taxes)	404	408	453	478	436	457	461	514	562	666	815	974
Profits on securities sold	(2)	(2)	268	117	173	215	178	145	44	20	20	20
Net charge-offs on assets	[3] 741	[3] 196	185	203	299	272	215	154	98	150	175	200
Net (nonoperating profit) [4]	−741	−196	83	−86	−126	−57	−37	−9	−54	−130	−155	−180
Profits before income taxes	−337	212	536	392	310	400	424	505	508	536	660	794
Taxes on net income (including surtax and excess profits tax) [2]	3	5	12	11	10	12	23	50	101	138	213	281
Net profits after income taxes but before dividends	−340	207	524	381	300	388	401	455	407	398	447	513
Cash dividends declared and interest paid on capital	188	207	223	226	222	232	237	238	232	230	240	250
Net additions to capital	−528	-----	301	155	78	156	164	217	175	168	207	263

[1] Break-down estimated.

[2] Taxes on net income are estimates for 1934–41. Figures of income taxes paid by national banks were obtained from the Source Book of the Bureau of Internal Revenue for 1934–37; in 1938 the classification was changed to include all "banks and trust companies"; figures of income taxes of nonmember banks have been reported separately since 1936. Normal income taxes paid by all banks and trust companies amounted to $4.1 million in 1934; $6.4 million in 1935; 14.9 million in 1936; $11.5 million in 1937; $12.1 million in 1938; $14.4 million in 1939; and $21.7 million in 1940.

[3] Profits on securities sold are not available separately except for nonmember banks in 1934 and 1935; they are included with recoveries on securities and thus deflate the figures of net charge-offs on assets for those years. Profits on securities sold of nonmember banks were $14.5 million in 1934 and $28.4 million in 1935; recoveries and profits on securities of member banks were $191.8 million in 1934 and $287.8 million in 1935.

[4] Minus (−) indicates nonoperating loss.

Mr. CRAWFORD. That will bring out very clearly what happened on the bond situation.

The CHAIRMAN. I want to ask one or two questions that are not of importance with respect to this bill, but for the record. Your total losses, you say, have been how much? I mean losses sustained by the corporation?

Mr. CROWLEY. About $50,000,000.

The CHAIRMAN. Could you tell us offhand where those losses occurred, and when?

Mr. CROWLEY. The largest part of them have been in New Jersey, New York, and Pennsylvania, in the order named. I would say that those three States were responsible for two-thirds of our losses, easily.

The CHAIRMAN. Those three States?

Mr. CROWLEY. Yes; the rest was spread throughout the country.

The CHAIRMAN. At one time I had the figures—because I happened to be speaking to the State association of bankers in New Jersey, many

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of whom had very vigorously opposed all proposals of legislation to insure bank deposits, and the figures at that time showed that losses down to that time by the Deposit Insurance Corporation, which had experienced its initial losses in straightening up the banking situation at that time—of the entire losses over half were sustained in the State of New Jersey.

Mr. CROWLEY. It is now about two-fifths due to an increase in our losses in New York and Pennsylvania. We went into New Jersey and did quite a wholesale job on quite a lot of banks. We consolidated a lot of banks there. That was the reason for that. The amount of money that was expended was a great deal more than that, but on account of conditions our liquidations have proved out a little better than anticipated.

Mr. SPENCE. In what year did those losses occur?

Mr. CROWLEY. It seems to me we must have gone into New York, Pennsylvania, and New Jersey about 1935, 1936, and 1937, along in there.

Mr. FORD. What were your losses in California?

Mr. CROWLEY. We have had only one or two in California; small losses.

Mr. KEAN. With reference to those losses in New Jersey, I think a large part of that was caused by the fact that they allowed a lot of banks to open that they never should have allowed to open.

Mr. CROWLEY. The banking situation in New Jersey was——

Mr. KEAN. Very bad.

Mr. CROWLEY. It was very bad; yes.

Mr. KEAN. They allowed a lot of banks to open that they never should have allowed to open.

Mr. CROWLEY. And the only way of correcting it was to do the kind of a job that we did.

Mr. WOLCOTT. In any of these cases, did the depositors lose anything?

Mr. CROWLEY. When we went into a State like New Jersey, we notified the depositors, as you know, that we were going to take care of these banks and that there would be no loss to depositors. If you are going to maintain confidence in your banking system, the depositors have got to understand that you are not going to run away from your liability. However, in one very important case we were unable to work out a satisfactory solution and the bank suspended. It was a large bank with a number of depositors with balances in excess of $5,000. Those depositors lost about $2,000,000.

Mr. WOLCOTT. What is the average interest paid on time deposits by the banks now?

Mr. THOMPSON. Less than 2 percent.

Mr. WOLCOTT. In most instances it is 1 percent or less, is it not?

Mr. THOMPSON. I can give you the figures for 1941, if you are interested in them. Interest paid on time deposits by all insured banks in 1941 averaged about 1.2 percent of average time deposits held.

Mr. WOLCOTT. I would like to find out how much of the earnings of the banks are reflected in a reduction of interest paid on time deposits, for this reason. I am not so sure that we are not approaching a situation that looks healthy at the present time, but might not be so healthy when people are given an opportunity to invest their money

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outside of the banks. I wonder if we are not creating a situation, perhaps without realizing it, where the banks are merely becoming warehouses of the people's money and fiscal agents of the Federal Government.

Mr. CROWLEY. I think, Congressman, there are a lot of savings accounts that are not really and truly savings accounts, if that is what you mean.

Mr. WOLCOTT. What you referred to the other day as perhaps liquidation accounts?

Mr. CROWLEY. That is right. They are awaiting some type of investment, such as you were talking about. I do not think by any means you could say that the amount of money we have in time deposits is really and truly a thrift account.

Mr. WOLCOTT. What would be the effect if the banks paid one-half percent more on time deposits?

Mr. CROWLEY. I do not think they could afford to, with what they can get for money now. You see, if they did that—how much would it cost them, Mr. Thompson?

Mr. THOMPSON. They have got $15,000,000,000 of time deposits. One-half percent would mean $75,000,000.

Mr. WOLCOTT. How does that $15 billion of time deposits compare with deposits in the banks during the period that you gave us, from 1936 on?

Mr. CROWLEY. The increase in time deposits is only about $2.5 billion or about 20 percent, as I understand it.

Mr. WOLCOTT. Much of that might be liquidation deposits?

Mr. CROWLEY. That is right.

Mr. WOLCOTT. You have not any way of knowing what percentage of those are thrift deposits?

Mr. CROWLEY. No; we have not.

Mr. PATMAN. I want to ask some questions, Mr. Chairman.

This bill deals with two questions, as I understand it. One is the reserves of the banks and the other is the assessment for the Federal Deposit Insurance Corporation; is that right?

Mr. CROWLEY. That is right.

Mr. PATMAN. The part about the assessments seems to be rather plain. For instance, take a bank in Texarkana, Tex., where I live; suppose that bank should buy $1,000,000 worth of bonds and the bank gives the Treasury credit on its books for $1,000,000. When that money is later transferred to the people, when the Government pays its debts to different people, such as when it pays the postmaster, the rural mail carriers, and other people in the community, the money will be transferred into their accounts, and very likely will remain in that bank, or other banks nearby. So this proposal is that during that period, from the time that credit is given on the books, by reason of the purchase of $1,000,000 worth of bonds, until it is transferred, there will be no assessment against it.

Mr. CROWLEY. That is correct.

Mr. PATMAN. Suppose that the bank owns a lot of bonds; that would not affect this at all?

Mr. CROWLEY. Not at all.

Mr. PATMAN. Now, about the reserves. Just how does this bill affect the reserves of the banks?

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Mr. CROWLEY. Would you allow Mr. Eccles to answer that, Mr. Patman, when his time comes?

Mr. PATMAN. Yes. But while you are on the witness stand, I want to ask you one or two questions. I have a bill here providing, that there shall be no more branch banks. It is what you might call an antibranch bank bill, H. R. 316. And since this subject relates to the whole subject of banking, I want to ask you something about your views on branch banks.

You are the head of the Federal Deposit Insurance Corporation, representing about 14,000 banks, and I should value your opinion highly, and I believe this committee and the Congress should. So if you do not mind stating your views on branch banks, I should personally appreciate it very much.

Mr. CROWLEY. Congressman, I think my position on branch banking throughout the banking system is generally pretty well known. I have always been an advocate of the independent banking system. I have always been opposed to the promotion of branch banking. The promoters of branch banking have always talked about putting branches in communities that could not support a bank. My experience is that they do not go into the communities where an independent bank cannot live. They go in and buy out the best independent bank and make that a branch, because it costs, practically speaking, as much money to operate a branch as it does to operate an independent bank.

I feel that we are taking backward steps in our banking system—we hear a lot of talk about trying to preserve the independent businessman, the small businessman, and yet we sit back here day after day and see a continual expansion of branch banking. I think it is a very unsound and a very unhealthy situation for the future of our banking system.

Every one knows where I have stood for years on that subject.

Does that answer your question?

Mr. PATMAN. Yes, sir. In other words, then, you would favor legislation along the lines proposed in H. R. 316?

Mr. CROWLEY. I would oppose any attempt to expand branch banking. I think the question of branch banking depends entirely upon State's rights and I think there should be something given to Federal corporations to protect against an expansion of that type of banking.

The CHAIRMAN. May I ask a question there?

Mr. PATMAN. Yes.

The CHAIRMAN. I wonder if you could give an estimate on this—how many banks were closed in the Uuited States that have not opened? You do not have to be exact in your figures.

Mr. CROWLEY. You mean since we started?

The CHAIRMAN. I mean during recent years from the peak in number.

Mr. CROWLEY. In 1920 you had approximately 30,000 banks. Now you have about half that number.

Mr. PATMAN. Less than half that number.

Mr. CROWLEY. That is right.

The CHAIRMAN. Of course, many of them were in very small communities, and in communities where there were more banks than there should have been.

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Is it not true that the franchise rights in various communities throughout the United States that were deprived entirely of banking facilities by reason of the closing of banks, would be of great value—billions and billions of dollars—during a period of 50 years?

Mr. CROWLEY. I think that unconsciously we have made a bank charter very valuable, because of our desire to restrict the expansion of banking. As I review the losses in the banking system since 1920, a lot of that was due to agricultural conditions, due to bad loaning policies, but also a lot of it was due to a forced liquidation that kept driving values down and down more all the time. I think that had we been able to keep the confidence of our depositors, the depression never would have gotten to the depth that it did; because you would not have had forced liquidation.

It is very evident to us, as we study many banks—Congressman Kean talked about the banks that were kept open in New Jersey—there were a lot of banks kept open in New Jersey that were in bad shape. On the other hand, I am fully convinced that there were many banks that closed that had a better chance of surviving, if they had had a chance to hold their assets for the enhancement in value that came along in the years to come, in the years that came after.

The CHAIRMAN. What you mean is that the closing of a bank did not reflect an exactly fair estimate of values.

Mr. CROWLEY. I think that is correct.

The CHAIRMAN. Of the assets?

Mr. CROWLEY. I think that is correct.

The CHAIRMAN. I want to ask one question, if Mr. Patman will permit me, while I am interrogating again. You did not have control of the reopening of the banks following the holiday?

Mr. CROWLEY. No.

The CHAIRMAN. They took 6 months' time after the examination and investigation for the deposit insurance to go into effect?

Mr. CROWLEY. That is right.

The CHAIRMAN. And it was limited to a temporary insurance of $2,500, before the permanent law was permitted to go into effect.

Mr. CROWLEY. I think there was a good job done on opening the banks.

The CHAIRMAN. I think that, too.

Mr. FORD. California has the greatest system of branch banks of any State in the Union. It has lost but one or two banks in the State. Our system is largely in the Federal Reserve. I would be unalterably opposed to any Federal law which undertook to tell us when we should have branch banks or any banks.

Mr. CROWLEY. Well, of course, that is the theory of States' rights that I subscribe to too, provided you follow that theory right straight on through and just don't use it in the case of branch banking. In other words, I think in this theory of States' rights we use it when it is to our advantage and throw it out the window when it is to our disadvantage.

Mr. FORD. That is human nature.

Mr. PATMAN. This bill I am speaking about provides no financial institution chartered by or pursuant to any law enacted by the Congress and any financial institutions, and their accounts, investment, or deposits are insured to any extent by the United States or any agency or instrumentality thereof shall hereafter establish any

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branch office provided, however—and then the bill exempts branches that are established at the time of the enactment of the law. But when the bill comes up, if we are able to get a hearing on the bill some time in the future——

The CHAIRMAN. We are hearing you on it right now.

Mr. PATMAN. I expect to propose the phrase "at the time of the enactment of this law" be changed to read "on or before January 5, 1943", the time of the introduction of the bill so as to put those out that will go in between that time and the enactment of the law. With reference to branch banks in California it is my understanding that the Bank of America covers several States. Is that right?

Mr. CROWLEY. Not the Bank of America. Transamerica does.

Mr. PATMAN. The Bank of Transamerica, that is just a holding company?

Mr. CROWLEY. Yes.

Mr. PATMAN. Transamerica owns the Bank of America?

Mr. CROWLEY. Yes; a portion of it.

Mr. PATMAN. Well, the control interest?

Mr. CROWLEY. Not the controlling interest but I think it is safe to say that Transamerica controls it.

Mr. PATMAN. Controls the Bank of America?

Mr. CROWLEY. Yes.

Mr. PATMAN. Now, how many other chain banking and branch banking institutions does this Transamerica control on the Pacific coast?

Mr. SULLIVAN. They have most of the banks in Nevada.

Mr. PATMAN. They have most of them in Nevada?

Mr. SULLIVAN. Yes.

Mr. PATMAN. They own them in Utah, do they not, and in Arizona?

Mr. CROWLEY. Not in Utah, so far as we know.

Miss SUMNER. Is it your fear if it is not stopped it will spread further?

Mr. PATMAN. Yes. If it is not stopped we do not know where it will go to.

Miss SUMNER. Yes.

Mr. WRIGHT. As you gentlemen know I am a new member of this committee and I am anxious to get a little information on the point of branch banking. Is there any control exercised over branch banking by the Federal Deposit Insurance Corporation in connection with branch banking?

Mr. CROWLEY. Yes, we have three agencies for the control of branch banks extending to banks under their supervision. We have no control over stopping a holding company from extending their ownership of corporate banks. We have no way to do that.

Mr. PATMAN. So indirectly you do not have sufficient force and effect to stop it?

Mr. CROWLEY. Not the expansion of a holding-company system.

Mr. PATMAN. I do not want to ask a lot of questions and take up a lot of time about something you can put in the record. You have a complete statement about the Transamerica Corporation, do you not, the holdings of this holding company?

Mr. CROWLEY. Yes; we have, insofar as information is available.

Mr. PATMAN. Will you place in the record a statement showing the bank holdings and all the different holdings of different types and character of the Transamerica Corporation? Can you do that?

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Mr. CROWLEY. Yes, sir; and if you hold the hearings open to give us a chance to confer with the Federal Reserve and get it ready?

Mr. PATMAN. Yes, sir; I presume it will be all right. And the Transamerica Corporation as I understand it is interested not only in banks but it is interested even in lumber yards and insurance companies and credit agencies?

Mr. CROWLEY. That is right.

Mr. PATMAN. And different types of business?

Mr. CROWLEY. That is right.

Mr. PATMAN. And many different kinds of business. That is right, isn't it?

Mr. CROWLEY. That is right.

Mr. PATMAN. It has been suggested they are even interested in restaurants. What all kinds of business are they interested in, Mr. Crowley, if you know?

Mr. CROWLEY. I believe they have an interest in a tobacco company, lumber mills, insurance companies, real-estate companies.

Mr. PATMAN. And distilleries and wineries?

Mr. CROWLEY. We will make up the chart for the record, Congressman.

(The matter referred to is as follows.)

Transamerica group as of close of business Dec. 31, 1942

Banks under control	Date control acquired	Percentage of stock owned by Trans-america	Total assets (thousands)
CALIFORNIA			
Bank of America National Trust and Savings Association, San Francisco		(1)	$2,143,203
Central Bank, Oakland	1930	99.72	59.849
First National Bank of Garden Grove	Dec. 23, 1938	82.60	1,474
Bank of Pinole, Crockett	Jan. 31, 1940	62.30	3,718
Central Bank of Calaveras, San Andreas	Oct. 10, 1940	90.83	1,417
Temple City National Bank	June 17, 1941	77.33	990
First National Bank of Fairfield	May 22, 1941	89.60	958
First National Bank of Weed	May 29, 1941	90.00	1,044
First Trust & Savings Bank, Pasadena	Dec. 11, 1941	65.30	18,666
OREGON			
First National Bank of Portland	1930	65.78	192,319
Clatsop County Bank, Seaside	Oct. 28, 1938	94.00	994
Coolidge and McClaine, Silverton	do	96.25	1,216
First National Bank, Forest Grove	do	90.00	1,068
Bank of Sellwood, Portland	Dec. 13, 1938	97.00	1,028
First National Bank of Cottage Grove	Jan. 5, 1940	90.00	2,168
First National Bank of Prineville	Apr. 2, 1941	90.00	1,377
Scio State Bank, Scio	Aug. 10, 1942	85.00	550
Bank of Sweet Home	Sept. 14, 1942	92.50	728
NEVADA			
First National Bank of Nevada, Reno	1934	99.26	52,765
Farmers Bank of Carson Valley, Minden	Oct. 26, 1938	84.00	1,326
Farmers & Merchants National Bank of Eureka	Mar. 22, 1939	80.00	677
Bank of Nevada, Las Vegas	May 17, 1941	88.00	1,041
ARIZONA			
First National Bank of Arizona, Phoenix	1939	77.79	24,576
Phoenix Savings Bank & Trust Co	1939	77.79	5,092
WASHINGTON			
National Bank of Washington, Tacoma	1936	72.03	45,081
FOREIGN			
Banca d'America e d'Italia Milan, Italy	1931	91.30	(?)

1 Indirect control.

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Transamerica group as of close of business Dec. 31, 1942—Continued

Other corporations under control	Date control acquired	Percentage of stock owned by Trans-america	Total assets
CALIFORNIA			
Corporation of America, San Francisco	1917	99.90	$127,555.48
Coast Service Co., San Francisco	1924	100.00	57,184.35
Capital Co., San Francisco	1923	100.00	51,994,964.88
Pacific National Fire Insurance Co., San Frnacisco	1928	92.00	10,237,879.56
Inter-America Corporation, San Francisco	1928	100.00	318,658.67
American Brokerage, Inc., San Francisco	1930	100.00	17,517.33
General Metals Corporation, Oakland	1930	55.90	4,777,694.37
Occidental Life Insurance Co., Los Angeles	1930	100.00	89,010,086.05
Timeplan, Inc., San Francisco	1941	100.00	16,829.67
Premier Insurance Co., San Francisco	1941	100.00	2,759,477.12
Pacific Finance Corporation of California, Los Angeles	1942	55.50	17,501,642.04
Enterprise Engine & Foundry, San Francisco	1942	100.00	7,007,283.45
Aerco Corporation, Los Angeles	1942	96.06	792,304.33
Adel Precision Products Corporation, Los Angeles	1942	95.31	5,455,947.26
KENTUCKY			
Axton-Fisher Tobacco Co., Louisville	1941	69.43	13,629,861.71

Proportion of banks and assets controlled by banks in Transamerica group

	California	Oregon	Washington	Arizona	Nevada	Total
Number of Transamerica banks	506	49	10	5	15	585
Number of independent banks	522	91	207	34	9	863
Number of all banks	1,028	140	217	39	24	1,448
Resources of Transamerica banks	$2,849,276,000	$284,150,000	$57,469,000	$39,655,000	$66,870,000	$3,297,420,000
Resources of independent banks	4,391,724,000	420,373,000	1,083,340,000	141,109,000	18,477,000	6,055,023,000
Resources of all banks	7,241,000,000	704,523,000	1,140,809,000	180,764,000	85,347,000	9,352,443,000
Percent of Transamerica banks	49.22	35.00	4.60	12.82	62.50	40.40
Percent of independent banks	50.78	65.00	95.40	87.18	37.50	59.60
Percent of all banks	100.00	100.00	100.00	100.00	100.00	100.00
Percent resources of Transamerica banks	39.35	40.33	5.04	21.94	78.35	35.26
Percent resources of independent banks	60.65	59.67	94.96	78.06	21.65	64.74
Percent resources of all banks	100.00	100.00	100.00	100.00	100.00	100.00

Mr. PATMAN. All right, sir. Do you look upon that as a healthy situation to have a holding company like that, to spread out over several States and grab up all these different kinds of institutions?

Mr. CROWLEY. I think, Congressman, that all the three agencies are in agreement about that situation.

Mr. PATMAN. That it should be corrected?

Mr. CROWLEY. That is right.

Mr. PATMAN. In that statement about the holdings of Transamerica I hope you make it full and complete and give the amount of interest that Transamerica owns, like say in the Bank of America it holds 91.3 percent of the stock.

Mr. CROWLEY. No, it is much less than that, Congressman. We will give it all.

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Mr. PATMAN. No, this is the Italian branch of it, I guess. It used to be the Bank of Italy. Take, for instance, the First National Bank of Nevada, it owns 99 percent of the stock.

Miss SUMNER. Fifty-one percent is enough to do all the damage.

Mr. PATMAN. Even less than that some times.

Mr. FORD. It has not done any damage, but the point is they have got a banking system in a State where they would not have it otherwise.

Mr. PATMAN. Is there any effort made to entice people or encourage people to borrow money from banks to buy Government bonds?

Mr. CROWLEY. No; I do not think so. I would prefer for the Federal Reserve to answer as to the bond policy.

Mr. PATMAN. Do you have anything to do with postal savings?

Mr. CROWLEY. No. In what way do you mean?

Mr. PATMAN. You do not have any control over it?

Mr. CROWLEY. No; that is entirely under the Treasury Department.

Mr. PATMAN. I notice in all this advertising where people are encouraged, and properly so, to buy all the Government bonds that they can to help out in the war effort and that no credit is ever given for the amount of money they invest in postal savings when the fact is that you help the Government just as much when you invest $100 in postal savings as when you buy a $100 bond.

Mr. CROWLEY. Except this, when you put the money into the postal savings you keep it more in a demand position and the Treasury needs to have money in longer maturities.

Mr. PATMAN. But the fact is, of course, every 60 or 90 days you can get your money on the bonds, can't you? And since all the money invested in postal savings is in turn invested in Government bonds anyhow it occurs to me it would be exactly the same thing and people should be given credit in these bond drives for the amount of money invested in postal savings. Don't you agree with that?

Mr. CROWLEY. I think that postal savings is making a contribution to the financing of the war.

Mr. PATMAN. Because a lot of people who will put money in the postal savings will not patronize a bank or any other financial institution.

Mr. CROWLEY. I would think this, Congressman, if there was a large growth in postal savings in lieu of buying War bonds that would be a weakness.

Mr. PATMAN. It would be a weakness?

Mr. CROWLEY. I think so.

Mr. PATMAN. But you will notice notwithstanding that fact that postal savings go into War bonds that there is no advertisement of postal savings at all and there is no effort made by the Government or by any person in the world to get people to invest in postal savings, notwithstanding the fact that postal-savings deposits are going up month by month and they are higher today than they have ever been in the history of this country. There is one other question I want to ask you.

Mr. CRAWFORD. Will the gentlemen yield at that point?

Mr. PATMAN. Yes, sir.

Mr. CRAWFORD. Where a person puts money in the postal savings and leaves it there it costs the Government considerably less money than if he buys a saving bond.

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Mr. PATMAN. That is true. It is 2 percent on postal savings and 2.9 percent on bonds.

Mr. CRAWFORD. Yes. Take the great majority of postal savings and you find many of them go back for 10 years or more beyond the duration of time a saving bond goes. For the period of years that they are deposited, I do not know what the Treasury does with it, but the point is the Government has the money.

Miss SUMNER. Do they put this back in the bank?

Mr. CROWLEY. That is true. Some is put back. About $50,000,000 is in the bank.

Mr. PATMAN. We passed a law here one time I know at least permitting the assets of insured banks that are not members of the Federal Reserve System to be used for rediscount purposes to the Federal Reserve bank in that district.

Mr. CROWLEY. That is my understanding.

Mr. PATMAN. I am not clear whether it was mandatory or permissive.

Mr. CROWLEY. It is permissive, as I understand it.

Mr. PATMAN. It is permissive?

Mr. CROWLEY. That is right.

Mr. PATMAN. In other words, "may." Well, has that privilege been permitted to be used to any extent, Mr. Crowley?

Mr. CROWLEY. Well, you see, since that law went into effect, Congressman, there has been no borrowing on the part of banks at all to speak of so there has been no use of it made at the present time.

Mr. PATMAN. There has been no use made? There has been no occasion at all? They did not need to borrow?

Mr. CROWLEY. That is right.

Mr. PATMAN. In fact, any bank with Government bonds, now all of them have Government bonds, can get money on them immediately if they want to?

Mr. CROWLEY. That is right.

Mr. PATMAN. Either through the open market or through the Federal Reserve bank in that district?

Mr. CROWLEY. That is right.

Mr. PATMAN. When you put the statement in the record about the amount of interest that has been saved, I hope you put it in up to date, if it is not too much of a job, and that you also include the same information on the reduction of interest on time deposits from the time the law was changed up to now. And I have another question I want to ask you. Do you know about bond sales to servicemen?

Mr. CROWLEY. No, I do not, Congressman.

(The statement referred to is as follows:)

FEDERAL DEPOSIT INSURANCE CORPORATION,
Washington, May 6, 1943.

The Honorable HENRY B. STEAGALL,
House of Representatives, Washington, D. C.

MY DEAR CONGRESSMAN: At the hearing on S. 700 before the House Banking and Currency Committee, The Honorable Wright Patman, of Texas, requested the Corporation to prepare a statement showing the estimated savings to the banks of the United States resulting from the acts passed by Congress in 1933 and 1935 prohibiting the payment of interest on demand deposits and providing for the regulation of the rates of interest on time deposits. We were also requested to compare the amount of this savings with the assessments which have been paid by insured banks into the Federal Deposit Insurance Fund.

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It is estimated that the prohibition of interest on demand deposits and the regulation of maximum rates of interest (at 3 percent) on time deposits resulted in initial savings to the insured banks in 1933 and 1934 at the rate of about $90,000,000 per annum or 0.25 percent of deposits.

The maximum rate of interest payable on time deposits was lowered to 2½ percent, effective February 1, 1936. This further reduction probably had little or no effect upon banks in central reserve and reserve cities since their rates were already below that level. However, for country banks this reduction resulted in further substantial savings for 1936 as compared with 1935 of from $15,000,000 to $20,000,000 or 0.24 percent of time deposits and 0.12 percent of total deposits in these country banks. The assessment rate is 0.083 percent of total deposits.

As a consequence of the easy money conditions which existed during the thirties, all interest rates declined substantially. It is not possible to estimate the extent to which the rate of interest on demand deposits would have declined, lacking prohibition of interest payments, nor the extent to which the rate of interest on time deposits would have declined, lacking regulation of maximum rates. It is reasonable to assume, however, that the low money rates would have brought about a substantial decline in rates of interest paid on deposits.

If, without the prohibition of the payment of interest on demand deposits other than interbank deposits, the rate had fallen to 15 cents per $100 of demand deposits other than interbank deposits in 1934–40, and to 14 and 13 cents, respectively, in 1941 and 1942, the total amount of assessments at one-twelfth of 1 percent of total deposits could be said to have been saved by the prohibition of interest. Similarly, if without the regulation of maximum rates on time deposits, the rate of interest on time deposits had declined by 25 to 40 cents less than it did per $100 of time deposits, the total amount of assessments could be said to have been saved. The two together would have saved double the assessments.

In the case of interbank deposits, assessments paid on total deposits at one-twelfth of 1 percent of total deposits equalled from 33 to 40 cents per $100 of interbank deposits for central reserve and reserve city banks which held all but 1 or 2 percent of interbank deposits during this period. Since these banks were actively bidding for interbank deposits during the period, it is probable that such deposits were profitable to them, and it is conceivable, therefore, that some interest would have been paid on interbank deposits if such payment had not been prohibited. If without the prohibition of the payment of interest on demand deposits the rate on interbank deposits had not remained as high as necessary to equal assessments, only a portion of the amount of assessments could be said to have been saved by the prohibition of the payment of interest on interbank deposits alone.

Our appraisal of these factors leads us to believe that the prohibition of payment of interest on demand deposits combined with the regulation of maximum rates of interest on time deposits have resulted in savings to the banks as a whole at least equal to the deposit insurance assessments paid. The amount of actual savings from these factors for the period 1934–42, inclusive, cannot be measured, however, and thus the conclusions are subject to debate.

Yours very truly,

FRANCIS C. BROWN, *Solicitor.*

Mr. PATMAN. That is all.

Mr. GIFFORD. The general result of this legislation is that the banks don't want to take money from people now who expect to leave it there on deposit for safekeeping for a while because they have to pay deposit insurance; is that right, the banks have to pay this?

Mr. CROWLEY. That is right. If it takes the deposit it has to pay the insurance assessments.

Mr. GIFFORD. To relieve the Government and the Treasury of this charge they hold a further preferential place, the Treasury does, over our own citizens, so that the banks will encourage them more. Do you think, I do not like to ask if you think that is fair to the general citizen of the country because the Treasury gets at all times a preferential place. They get money now at a very low rate of interest because they have to pay the deposit charges of this Federal Deposit Insurance Corporation charge. The bank can say to them,

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"We cannot lower the rate of our charge to you because we have to pay this on your business." The Treasury is relieved of that. I think you will find the Treasury has at all times a preferential position over our own citizens. That is not what I wanted to take up. I wanted to ask definitely this question. I have a bank close to a large camp. Their deposits are doubled. Their work is terribly increased. They have to pay now, do they, on their deposits?

Mr. CROWLEY. That is right.

Mr. GIFFORD. And this would relieve that bank greatly?

Mr. CROWLEY. On that particular war loan account.

Mr. GIFFORD. The war loan is deposited?

Mr. CROWLEY. This is in the Treasury or general account now.

Mr. GIFFORD. Well, it would not help my bank at all if the bank was willing to take the deposits of those people who are at the camp and who bring in twice the deposits the bank ever had before and have to handle?

Mr. CROWLEY. It does not help them, no.

Mr. GIFFORD. It does not help them at all?

Mr. CROWLEY. That is right.

Mr. GIFFORD. The third question: Tell me why there is this practice of one bank depositing in another bank and transferring deposits back and forth. Every bank is reporting a lot of money held in other banks. Why is that?

Mr. CROWLEY. That comes under my friend back here.

Mr. GIFFORD. I know, he is smiling there. I just had that questo ask you. You know banking and I do not. Why do banks transfer deposits back and forth? There has got to be some advantage there somewhere. I cannot understand it.

Mr. CROWLEY. There is a little advantage there, Congressman. There is an advantage there, all right.

The CHAIRMAN. As a matter of fact any reduction of the assessment of the banks regardless of the cause of that reduction on the class of funds that brought it about, would to that extent grant relief to the bank. And, of course, insofar as the assessment could be reflected in the banks' policy toward borrowers it would be just as much an inducement for loans as if the reductions were brought about by reason of any other class of deposits?

Mr. CROWLEY. That is right.

Mr. TALLE. Mr. Crowley, I had no opportunity the other day to pursue my questions as we were closing the meeting. Am I right in saying that in your introductory statement you said substantially this, that the banking system of the United States is in better shape now than ever before in its history?

Mr. CROWLEY. Yes; in my judgment.

Mr. TALLE. And what would you say would be the primary test in determining that liquidity?

Mr. CROWLEY. I think it is the quality of the assets other than the Government's, and then the liquidity that the banks have.

Mr. TALLE. In a serious depression nothing is liquid except cash.

Mr. CROWLEY. Except the right of discount on Government securities.

Mr. TALLE. What is the single type of asset, the one asset held in banks which overshadows all others in the banking system today?

Mr. CROWLEY. Of course, your Government securities overshadow everything else.

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Mr. TALLE. Liquidity then really rests on Government obligations; is that right?

Mr. CROWLEY. That is right.

Mr. TALLE. Other questions which I had in mind pertained to the investment of your funds and to income, but I will not take time to deal with those questions because they have been covered here, I think.

Mr. CROWLEY. Thank you very much.

Mr. PATMAN. In your statement I wish you would make a parallel column showing what the banks have received on demand deposits by reason of their not being required to pay interest on demand deposits. That is one column, and in another column, the amount of savings on time deposits, and third, the amount they have had to pay in assessments to the Federal Deposit Insurance Corporation. I believe you stated positively that the argument was made and accepted by Congress that the banks would be saved the interest on demand deposits in order to compensate them for the amount they would have to pay to the Federal Deposit Insurance Corporation.

Mr. CROWLEY. It was a compensating factor.

Mr. PATMAN. And we would profit greatly by it?

Mr. CROWLEY. That is right.

Mr. FORD. Another factor to be considered is, if I have $5,000 to put in a bank, if I put it in a Government bond I can get 2.5 percent interest.

Mr. CROWLEY. I think that is correct.

Mr. FORD. If there is no interest on the deposits they have a tendency to put more money in Government bonds.

The CHAIRMAN. It might be stated for the record that one of the considerations which entered into the provision preventing the payment of interest on demand deposits and regulating that on time deposits grew out of the practice that had been indulged in considerably where banks in need of cash instead of joining the Federal Reserve, or applying through the Federal Reserve if they were members, or through some bank, and arranging across the counter through somebody who knew what he was doing, in many instances banks that got in trouble they went out and borrowed from the public under the guise of deposits bearing interest.

Mr. CROWLEY. That is right.

The CHAIRMAN. And that was one of the evils we had and why we eliminated that practice.

Mr. GIFFORD. The banking system is, of course, in a much stronger position because it is filled with the IOU's of the Government and there is no security in back of that. The rest of it is borrowed by individuals. They have to put in doubtful securities. But the IOU of the Government has this backing, that we Congressmen are willing to tax the people enough to pay them. That is the soundness of the banking system today. It is depending on us.

Mr. CRAWFORD. I gather from your statement that this bill was originated by the Treasury Department?

Mr. CROWLEY. It is done at the request of the Treasury believing it would help their financing of the war.

Mr. CRAWFORD. I just want to read your statement here. You said:

> We have been told that many bankers have made representations to the Treasury they are loathe to participate in the handling of war loan deposits because of the assessment of one-twelfth of 1 percent.

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Are they actually loathe or do they actually refuse to participate?

Mr. CROWLEY. As I understand it between five and six thousand banks now have a war loan account and what the Federal Reserve and the Treasury want to do and would like to encourage is ten or twelve or thirteen thousand banks to have that account.

Mr. CRAWFORD. I see.

Mr. CROWLEY. This bill provides an incentive to do that.

Mr. CRAWFORD. You think it is necessary?

Mr. CROWLEY. That is right.

Mr. CRAWFORD. Mr. Crowley, a matter came up here which I am awfully anxious to further explore before any questions go out which had to do with Mr. Patman's bill which I think is a very important bill. If I understood you correctly I think this is awfully important to get into the record. If I understood you correctly in your defense of the independent unit banking system you do not want to go outside the confines of the State control. Here is what I mean by that. I want to be very specific. If State A has a State law which permits branch banking, if I understand you correctly you are willing to step aside and let that State handle its own affairs.

Mr. CROWLEY. I am willing to step aside and let that State pass State banking laws as it may, pertaining to branch banking, but I think your Federal authorities and especially the Federal Deposit Insurance must have some protection that some commissioner doesn't go out and expand branch banking all over the State and increase our liability to undue risk.

Mr. CRAWFORD. I have no argument with that at all. Another thing is this. Going back to the philosophy you have enunciated here so often in recent years and with which I am in full accord with reference to protecting the capital structure of the banks which you insure, can you state to us whether or not the earnings of the banks in smaller communities, by that I mean in towns of 15,000 population and less and right down to small villages of three and four thousand population, I am including the banks which you insure, are those capital structures being preserved through adequate earnings under the system which now prevails where Government agencies go out and make loans and where many of those banks are being forced into purchasing Government securities only to accommodate their excess funds?

Mr. CROWLEY. The capital ratio, Congressman, naturally is getting smaller all the time because of your increase in deposits. But we have tried to get the banks to conserve as much of their earnings as they possibly can to add to their capital structures, and with the quality of the assets they have and with the conservation of their earnings we feel they are doing the best they can. It would be unwise to go out and require the banks to increase this ratio by the sale of stock. As these deposits went up you would be doing it every 6 months.

Mr. CRAWFORD. Are those capital structures relatively as good in the banks doing business in towns and villages of 10,000 population or less, as they are in banks located in towns of above 10,000 population?

Mr. CROWLEY. Generally they are better. I think that our small banks are also making a little more money proportionately perhaps than your larger ones and I think they are handling their earnings just as judiciously as the large ones are. I think the small banking system

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has done a fine job during the last 10 years. I have some figures which I should like to insert into the record here.

(The matter referred to is as follows:)

Average net profits per $100 of total capital accounts of all insured commercial banks, 1939–41, and of insured commercial banks not members of the Federal Reserve System, 1939–42 [1]

[Banks grouped by amount of deposits]

	All insured commercial banks [2]			Insured commercial banks not members of the Federal Reserve System [3]			
	1939	1940	1941	1939	1940	1941	1942 [4] prelim.
All banks	$6.95	$7.02	$8.15	$5.20	$5.35	$6.93	$6.89
Banks with deposits of—							
$100,000 or less	3.62	3.99	4.74	3.48	4.26	4.57	2.88
$100,000 to $250,000	6.04	6.54	7.66	5.86	6.54	7.79	6.00
$250,000 to $500,000	7.64	7.89	9.14	7.35	8.18	9.33	7.71
$500,000 to $1,000,000	7.65	7.66	8.89	6.67	7.44	8.12	8.34
$1,000,000 to $2,000,000	7.18	6.91	8.00	5.65	6.34	7.72	7.60
$2,000,000 to $5,000,000	6.40	5.91	6.92	4.66	4.25	5.81	6.54
$5,000,000 to $10,000,000	6.44	6.30	6.49	3.70	6.03	4.31	4.13
$10,000,000 to $25,000,000	7.55	6.65	6.81	1.32	2.74	5.50	4.63
$25,000,000 to $50,000,000	7.36	7.11	8.15	5.17	−1.39		[5] 7.06
More than $50,000,000	6.36	6.84	6.82	4.76	5.58	6.06	[5] 7.39

[1] Excludes banks submitting reports covering less than the full year's operations or whose operations were materially affected by mergers during the year.
[2] Averages are based on ratios of individual banks.
[3] Averages are based on aggregates.
[4] Averages are based on aggregates of 3,195 banks—approximately one-half of the total number of insured commercial banks not members of the Federal Reserve System.
[5] Figures for 3 banks and 4 banks only and may not be representative.

Mr. Crawford. I am very glad to hear you say that. I am a little bit concerned about it and the reason I am concerned is because I am getting letters from small banks to the effect they are having a terrific job in maintaining their earnings. Letters come in in connection with the different agencies and if their earnings are holding up and if the ratios are proper I am delighted to know it.

Mr. Crowley. Banks in the Middle West, of course, have experienced considerable reductions in their loans. But banks generally have had to change their policies quite a lot in order to make money. They have had to reduce their overhead and levy a charge for services and charges for things like that which 10 years ago were almost unknown. They have been able to supplement their earnings by those factors. I think the banking system as a whole is getting along all right with its earnings.

Mr. Crawford. Now, going to the point raised by Mr. Ford to which you replied in substance that you could go along with that approach provided we did not use the States' rights to give us the excuse to do some things and then kick out States' rights on other matters. Where the Supreme Court holds that a certain type of operation is in interstate business it seems to me that is the thing that will largely have to govern. To make myself clear, suppose the Supreme Court later holds all banking is interstate business. Then that would erase, would it not, the States' rights approach with reference to branch banking.

Mr. Crowley. I think when you get into interstate rights I presume if you drew on your imagination sufficiently you could almost claim everything would come under Federal control.

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Mr. CRAWFORD. That is the reason I bring up this point, because I am drawing on my imagination and I think it is only a matter of a short time. I was just saying, drawing on my own imagination, I think it is only a matter of a short time until perhaps the Supreme Court will hold that all banking is interstate commerce.

Miss SUMNER. I don't see how they can.

Mr. CRAWFORD. Neither do I.

Mr. MONRONEY. They are on wages and hours now.

Mr. CRAWFORD. But until that time comes it seems to me that the Congress will be inclined to do this very thing which you pointed out awhile ago. But when that time does come then it appears that the Congress will have to function so far as banking is concerned under that decision.

Mr. CROWLEY. That is right.

Mr. CRAWFORD. Now, I wanted to come back to my original point, so long as the situation is as at present with reference to States' rights, that is, the States have control over the establishment of branch banks, if one or all of the States refuse to change the law so that State branch banking could not be, so long as the States refuse or a State legislature refuses to make a law which prohibits branch banking, then if I understand you correctly, to the effect that the Federal Deposit Insurance Corporation, so long as that branch banking does not interfere with its sound administration of the affairs of the Federal Deposit Insurance Corporation will take no position in the matter; isn't that a correct statement?

Mr. CROWLEY. That is correct.

Mr. WOLCOTT. Something came up on the floor of the House a few weeks ago which has been interesting me since then. I have a nephew at Camp Meade. He is a thrifty young fellow. He has been married a short time. And after giving his wife most of his salary what he has left over he wanted to go down to the bank at Laurel and deposit there. They would not take it. Which brings up this same question that Mr. Gifford raised about the bank in a camp district doing two million dollars of business every month in soldiers' accounts. Now, isn't there a law still on the statute books that a soldier can deposit out of his salary and have withheld from his salary for deposit a certain amount every month to be deposited in a Company account or a Regimental account?

Mr. CROWLEY. That is the Soldiers and Sailors.

Mr. WOLCOTT. What is that?

Mr. BROWN (of the Federal Deposit Insurance Corporation). That is a provision I think whereby finance officers take those deposits.

Mr. WOLCOTT. Regimental finance officers?

Mr. BROWN (of the Federal Deposit Insurance Corporation). The so-called soldiers and sailors deposit accounts.

Mr. WOLCOTT. Is that under the quartermaster department or the paymaster?

Mr. BROWN (of the Federal Deposit Insurance Corporation). It is handled by the finance officer.

Mr. WOLCOTT. As I understand it there is a set-up in the Army whereby a soldier can make an allotment of his salary to this account each month.

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Mr. Brown (of the Federal Deposit Insurance Corporation). I do not know whether it can be done on an allotment basis but he has the right to make it. It is a savings allotment.

Mr. Wolcott. Let me see if I understand how it is done. He has the right to make a deposit in this account and then it draws 4-percent interest from the day he makes the deposit.

Mr. Brown (of the Federal Deposit Insurance Corporation). I do not recall the interest rate. It draws interest. I can find out and let you know.

Mr. Wolcott. I am sure it is 4 percent. Is that a liquid account? Can he draw that out at anytime he wants to?

Mr. Brown (of the Federal Deposit Insurance Corporation). I looked into that sometime ago. I have an analysis in the office which I will be glad to put in the record or furnish to you. At one time, and I am not sure whether that has since been amended or not because it is over a year since I looked that up, at one time they could not.

Mr. Wolcott. I wish you would put it in the record. I have talked to a good many soldiers and sailors and marines, one was a major, one a lieutenant, the other a first sergeant, one a first-class private, and a private, and there wasn't one of them who knew anything about this account. I wonder if perhaps the banks in the locality of these camps would not be justified in calling the attention of the men to the fact they can deposit in these accounts and receive 4 percent interest and relieve themselves of the burden of carrying those accounts. I realize that the banks in the vicinity of the camps would have the burden of holding that account since, as in the case of my nephew which I used as an example, although I should not, he may be at Camp Meade 2 weeks and go somewhere else tomorrow. But I wish you would put in the record this set-up by which soldiers and marines, and this applies to the Navy Department as well as it does to the Army, can make deposits with the finance officers; and how much interest it draws; whether it is liquid or not and if they can draw on it entirely at will.

Mr. Brown (of the Federal Deposit Insurance Corporation). I will be glad to give you that analysis. As I recall it it was not an in-and-out account. At one time it had to be carried until the man's enlistment expired. I have the impression some legislation was considered to change that.

Mr. Spence. What is the actual amount of your liability on the limitation of $5,000?

Mr. Crowley. The last we had was about 27 billion, the last analysis that was made, in September 1941.

Mr. Spence. How does that run in proportion to all the deposits?

Mr. Crowley. At that time I think it was about 40 percent. At one time, September 1938, it was about 45 percent.

Mr. Spence. Is it much higher in smaller banks than larger banks?

Mr. Crowley. Yes, of course.

Mr. Spence. With reference to the banks you liquidate, what proportion of the deposits were insured?

Mr. Crowley. We cared for and protected about 98 percent of all the deposits in those banks.

Mr. Spence. As a rule than it is the smaller banks?

Mr. Crowley. No; the larger banks. But we did it under our authority to make purchases of assets for consolidation. I think that the time of a closed bank is almost a thing of the past. I think it is more economical for us to go in and consolidate an unsound bank

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with some other bank and take care of the deposit liability. It is very difficult to determine whether a person that has $6,000 should be paid only $5,000 or a person who had $5,000 paid all. And we find in liquidation we work out just as well and perhaps a little better by consolidating with another going bank and taking out all of the unsound assets.

Mr. SPENCE. And that to a certain extent wipes out the $5,000 provision?

Mr. CROWLEY. It gives 100-percent insurance for all practical purposes.

Mr. MONRONEY. You pay 100 percent of deposits or deposits up to $5,000?

Mr. CROWLEY. We pay 100 percent under the conditions I have just described.

Mr. MONRONEY. That gives you a cushion there for your consolidation.

Mr. CROWLEY. That is right.

The CHAIRMAN. The method that you employ, of course, prevents the losses that are incident to expeditious liquidation.

Mr. CROWLEY. That is right.

Mr. SPENCE. What proportion were consolidations?

Mr. CROWLEY. About two-fifths of the banks by number holding more than three-fourths of the deposits in the closed or merged insured banks. You see, we merged banks in New York that had deposits of 25, 30, and 40 million dollars. They had many deposits in those banks that were over $5,000. The net result to us was I think we made money, or rather, saved money, by the way we handled it.

The CHAIRMAN. I want to ask a practical question there. Since it is true we are practically protecting all deposits, don't you think it would be sensible for the law to recognize that and say so or at least increase the amount of individual deposits insured?

Mr. CROWLEY. I think it would cost no more money to insure the deposits 100 percent than it does to insure under the system we have now.

The CHAIRMAN. That statement covers what I had in mind.

Mr. PATMAN. This holding company law that Congress passed a few years ago, it did not affect the Trans-America Corporation?

Mr. CROWLEY. It did not restrict them from further expansion, Congressman. There was nothing in the law that gave anyone that authority to restrict their expansion.

Mr. PATMAN. Were they specifically exempt?

Mr. CROWLEY. No; I mean it did not stop the growth of any bank holding company.

Mr. PATMAN. You think that is a serious menace and should be dealt with by Congress?

Mr. CROWLEY. I do not think there is any doubt about it.

Mr. PATMAN. And on this Trans-America statement I hope you will include in there the percentage of the banks owned or controlled by the Trans-America Corporation in each State.

Mr. CROWLEY. We will.

The CHAIRMAN. The committee will adjourn to 10:30 a. m. tomorrow morning.

(Committee adjourned to Friday, April 2, 1943.)

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FEDERAL RESERVE ACT AMENDMENT

FRIDAY, APRIL 2, 1943

HOUSE OF REPRESENTATIVES,
COMMITTEE ON BANKING AND CURRENCY,
Washington, D. C.

The committee met at 11 a. m., Hon. Henry B. Steagall (chairman) presiding.

The CHAIRMAN. The committee will come to order. Governor Eccles, the committee has invited you to discuss this bill, H. R. 1699, and we will be glad to have you do so. If you desire to make a prepared statement without interruption, the committee will be glad to accord you that privilege and later the members may desire to interrogate you.

I am sure it is not necessary to say more than this. We are always glad to hear you. You may proceed.

STATEMENT OF M. S. ECCLES, CHAIRMAN OF THE BOARD OF GOVERNORS OF THE FEDERAL RESERVE SYSTEM

Mr. ECCLES. Mr. Chairman and members of the committee: I appreciate the opportunity to appear before you this morning and discuss what I consider a very necessary bill and one the passage of which is urgent. I feel that time is of the essence. I regret that the bill could have been acted upon sooner.

The bill is a war emergency bill, the life of which expires 6 months after the cessation of hostilities, as determined by the President or by Congress.

The Treasury, as you know, are undertaking a financing program to raise not less than $13,000,000,000 commencing Monday, April 12. It is desired, in fact it is very urgent, that this bill be gotten out, if possible, prior to that time so that as many banks as possible, or as many as can be persuaded to do so, will qualify for war loan deposit accounts and that those banks which have qualified for war loan deposit accounts can be persuaded to qualify for increased amounts.

There is considerable delay in getting banks to act, because the procedure is that they must get authorizations from their directors authorizing them to pledge securities with the Federal Reserve bank for the amounts they desire to qualify for and, after their applications are submitted to the Reserve bank showing proper authority, the Reserve banks are required to act upon their applications. The next financing drive opens on April 12, so that there is an element of time involved, and I merely wanted to say today that I hoped it would be possible for the committee to report the bill out this week and get it acted upon next week. Inasmuch as a similar bill has

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passed the Senate, it would seem to me that there should be little delay if this committee would report, say, the Senate bill out.

Mr. ROLPH. Has exactly the same bill passed the Senate?

Mr. ECCLES. Practically the same bill. I would assume that this committee might adopt the Senate bill with a House title and avoid any need of a conference on the bill.

Now, Mr. Chairman, I have a statement that I will read, if I may, without interruption, that explains the purposes and the operations of the bill.

The CHAIRMAN. The committee will be glad to have you do so.

Mr. ECCLES (reading):

This measure provides that for the duration of the war and 6 months thereafter so-called war-loans deposit accounts shall be relieved from Federal deposit insurance assessments and from reserve requirements. Its enactment will help to perfect the machinery for and thus facilitate and make smoother the Government's war-financing operations.

I should like to state as simply as I can what the bill does and why its enactment is important at this time. It is not a complex matter, and I see no reason why it should arouse controversy. The bill has the approval of the Treasury, the Federal Deposit Insurance Corporation, the Board of Governors of the Federal Reserve System, and the System's open-market committee. I might also say it has cleared the Budget.

As members of the committee will recall, war-loan accounts were originally authorized by the Liberty Loan Acts in the last war and are now authorized by the Second Liberty Loan Act as amended. This act provides that the Secretary of the Treasury may deposit "in such incorporated banks and trust companies as he may designate, the proceeds or any part thereof, arising from the sale of the bonds and certificates of indebtedness, Treasury bills and War Savings certificates authorized by this act * * *."

Incorporated banks and trust companies may qualify for war-loan accounts by applying to the Treasury through the Federal Reserve banks. Such accounts are fully secured by a pledge of assets for a stipulated amount, which is the maximum that may be on deposit in the account at any one time.

The Treasury has authorized the Federal Reserve banks to act upon these applications; it is not necessary to submit them to the Treasury for consideration—they have given that authority to the Reserve banks. The Reserve banks have the authority, without any limitation except as to the requirements of collateral security; as to the amount that any bank can qualify for, that is left up to the discretion of the Reserve banks without limitation [reading]:

When banks which have qualified for war-loan accounts subscribe to Government securities for their customers or themselves, they enter the amount of their allotted subscriptions in the war-loan accounts on the payment dates and subject to call by the Treasury. Subsequently, as the Treasury has need for funds, a call is issued; that is, notice is given to these banks to transfer to their respective Federal Reserve banks whatever percentage of the funds in the war-loan accounts is required by the Treasury to meet its current expenditures. Thus the war-loan accounts are drawn down gradually as Treasury needs arise, the money is checked out of the Reserve banks by the Treasury and ultimately flows back again to the banking system as deposits.

If there were no such mechanism—if all banks in subscribing to Government securities for their customers or themselves were to transfer the funds immediately to the Reserve banks—there would be periodic heavy drains on the deposit totals of the banking system, with seriously disruptive effects on the economy, particularly on the Government bond market. The larger the financing operation, the greater and more disruptive the drain would be. In peacetimes when the Government was not compelled to raise and expend such huge sums as are demanded by the war and when banks had superabundant reserves, the situation was very different. But today when the Treasury must go to the public and to the money market for large sums of money every few months, and when reserves

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are rapidly absorbed as currency in circulation expands and bank deposits increase, it is very important to extend the war loan deposit mechanism as widely as possible throughout the banking system.

If there were no such mechanism, it would be necessary to pump billions of reserves into the banking system to offset the heavy drains at financing periods and thus prevent widespread liquidation with the disturbance this would cause in the bond market. Then as the funds were spent by the Government and flowed back into bank deposits, the reserves that had been pumped in would be excessive relative to the current need. Any such alternating scarcity and redundancy of reserve funds would create difficult problems for the Treasury and the Reserve System.

To the extent that the war loan account mechanism exists throughout the banking system, such difficulties can be avoided and the flow of deposit resources into the war-loan accounts, then to the Reserve banks as the Treasury needs and calls for the money, then back into the banking system as the Treasury expends the money, is accomplished smoothly and without disruptive effects. There is a close adjustment and a minimum time lag between the drawing down of the money and its flow back into the deposit structure.

Because of these considerations, the Reserve System has made a special effort and a concerted drive through all of the Reserve banks to induce as many banks as possible to apply and qualify for war loan deposit accounts. The results so far have been gratifying, and a large number of banks, even though they may have felt that the war-loan accounts should not be subject to deposit-insurance assessments or to reserve requirements, have applied and qualified. There are still many thousands of banks which have not yet come in, and it is clear that the requirements of existing law, which this bill would suspend for the duration, are a real deterrent in many instances. Not only is a more widespread setting up of this convenient and necessary mechanism thus impeded, but banks that have war-loan accounts are discouraged from utilizing them as fully as would be the case if these statutory requirements were suspended. Neither requirement existed when war-loan accounts were originally authorized by Congress in the last war. We had no deposit insurance at that time and war loan accounts were not subject to reserve requirements before 1935.

I hope that this measure will be promptly enacted so that the mechanism, which I have tried to outline very simply, may be as widely set up and as generally utilized as possible to facilitate the large financing operations which are ahead of us as long as the heavy requirements of the war situation continue.

That concludes my formal statement, Mr. Chairman.

The CHAIRMAN. Governor Eccles, what is the procedure if a State bank, a nonmember bank, desires to extend a loan?

Mr. ECCLES. Desires to do what?

The CHAIRMAN. To make a loan to the Treasury.

Mr. ECCLES. If they have a war loan account, if they have qualified for it, they would put in their subscription or application through the Reserve bank of the district, and they then credit the Treasury through the war-loan account in their bank.

The CHAIRMAN. They would qualify for accounts through the Treasury?

Mr. ECCLES. They qualify through the Federal Reserve banks, who are the agents of the Treasury.

The CHAIRMAN. That is what I want to get.

Mr. ECCLES. That is right.

The CHAIRMAN. When a State nonmember bank wants to take a part of this loan, what is the process between the Treasury and that bank and between the Federal Reserve and that bank?

Mr. ECCLES. Well, the bank applies to the Federal Reserve bank for authority to establish a war loan deposit account. They deposit with the Federal Reserve bank the collateral or securities required.

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The securities must be in the minimum amount that must be put up, which will be the amount of the account. They must cover 100 percent with securities the amount of the war-loan account. In other words, they may qualify for a war-loan account equal to the capital and surplus, or may qualify for a war-loan account equal to twice the capital and surplus, or may want to qualify for one equal to three times their capital and surplus. Whatever amount they qualify for, they must deposit collateral with the Federal Reserve bank of that district in that amount.

The CHAIRMAN. And what is the application of that rule, if it does apply, to member banks?

Mr. ECCLES. The same thing.

The CHAIRMAN. That means, if I understand it, a bank that wants to make a loan to the Government has to give bond to the Government for the privilege of making the loan? Is not that about the way it works out?

Mr. ECCLES. Oh, no.

The CHAIRMAN. That is not quite a fair statement of it; but, as a matter of fact, they do have to make bond or give security to the Government?

Mr. ECCLES. If they want to establish an account for the Treasury in their bank, in other words, if they do not want the funds that they subscribe to leave the bank immediately, they must qualify. That is, if they do not want the funds to be paid out to the Reserve bank in payment for the Government securities, then they must qualify for a war loan deposit account, in which case they merely give credit to the Treasury in their bank for the amount of their subscription to Government securities, or the amount of the allotment of Government securities given to them as the result of their subscription.

The CHAIRMAN. What is the purpose of the securities that the bank puts up with the Federal Reserve in order to make a loan to the Government, or to the Treasury.

Mr. ECCLES. Of course what the bank does is the bank gets securities as the result of giving that credit, and the law requires that all Government deposits with any bank must be secured.

The CHAIRMAN. Of course, that is the purpose of it.

Mr. ECCLES. Otherwise, it is to protect the Government. The Government has an account with the bank; if that bank should close, the Government has securities to offset the amount of its credit in the bank.

The CHAIRMAN. The situation is really this: Any deposit that the Treasury leaves with a bank as a result of loans extended to the Treasury has to be secured by specific collateral pledged by the borrowing bank with the Federal Reserve System?

Mr. ECCLES. That is right.

The CHAIRMAN. That applies to nonmember banks?

Mr. ECCLES. And to member banks alike.

The CHAIRMAN. I understand.

Mr. ECCLES. That is right; it applies to all banks.

The CHAIRMAN. Well, is not that really the most of the difficulty that is likely to arise in financing the program of the Treasury?

Mr. ECCLES. What do you mean—you mean the difficulty of putting up collateral?

The CHAIRMAN. Yes.

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Mr. Eccles. No; that is no deterrent, because the collateral they put up is offset by the deposit that they give the Treasury credit for. In other words, it is a pure bookkeeping entry.

The Chairman. As I understand, the Treasury deposit account is an obligation of the bank?

Mr. Eccles. I did not get that question.

The Chairman. The deposit account in a bank creates an obligation on the part of the bank?

Mr. Eccles. It is an obligation; it is a liability of the bank. What the bank does is to credit the Treasury account with the amount of the Government securities which they purchase and that becomes a liability of the bank. On the other side of the ledger is an asset known as Government securities. So that they give the Treasury a credit for the purchase price of the securities which they purchase, and the offsetting asset, of course, is the amount of Government securities which they purchase.

The Chairman. What happens is the Government securities go to the bank and by the pledge of those obligations the bank, in keeping deposits, protects the deposits with specific collateral, or approved collateral?

Mr. Eccles. What these banks do is, to the extent that the banks buy Government securities, to that extent they create, through the operation of their purchase, that much money. And the banks as, for instance, will be the case commencing April 12 and running through April 14, will be given the privilege of buying $2,000,000,000 of seven-eighths certificates, and the banks will create $2,000,000,000 of funds. There will be $2,000,000,000 more funds as the result of that operation than there was before.

It is what we call bank money or bank credit. All of our bank credit, whether to the Government or whether to private parties, creates money. In other words, our money supply is largely composed of bank credit. That is why we hear so much about trying to do the financing outside of the banks; because, to the extent it is done through the banks, just to that extent it is inflationary in that it increases the volume of money.

During this coming drive, the banks are expected to take $5,000,000,000 of the $13,000,000,000 of securities, so that there will be $5,000,000,000 more money at the end of the drive than there was at the beginning of the drive, approximately.

Now, that covers the banks' subscription to Government and there are likewise subscriptions to Government securities in the community by individuals and corporations, which are expected to be $8,000,000,000 during this drive. The Treasury certainly won't spend the $8,000,000,000 during the period of the drive and, unless the banks keep on deposit the Treasury funds in the war loan account, then those funds would all come out of the communities' 13,000 or 14,000 banks. That $13,000,000,000 would all be immediately drawn out and deposited in the Federal Reserve banks to the credit of the Treasury.

Now, to draw $13,000,000,000 out of the banking system would simply eollapse the whole picture; that is all. There is only a billion and a half of excess reserves in the banks. To draw a billion and a half out would eliminate completely the excess reserves and would cause the banks to start selling heavily of Government securities to meet the withdrawal.

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Now, what we are trying to undertake to do here is to make this operation as smooth and as orderly as it is possible to make it, and we would like to see every dollar of that 13 billion—the 8 billion from the public and the 5 billion coming from the banks—credited to the Treasury in the war loan accounts in the communities where the 14,000 banks are located, and the Treasury then draw down those funds a few hundred million at a time as they spend them, and they flow back again into the communities.

So that your picture would be this: You would have, we will say, possibly $13,000,000,000 of credit to the Treasury in the War loan account. If that $13,000,000,000 were all raised at once, instead of over a period of several weeks, the Treasury would draw them down a few hundred millions at a time, possibly spending $200,000,000 to $250,000,000 a day, so that the money would go right back into the communities as fast as it was drawn out. That is, taking the country as a whole. So that when the entire $13,000,000,000 that was to the credit of the Treasury had been drawn down, there would be $13,000,000,000 back in the hands of the individuals and corporations. And, in that manner, the banks are not put under pressure to sell securities to get funds to take care of the withdrawals covering subscriptions to Government bonds.

That is why this thing is so urgent at this time, because the amount of excess reserves is getting very low and the size of the financing is getting very high. If the size of the financing were small, comparatively speaking, and the reserves were large, as has been the case up until 6 months ago, then the war loan account would not be necessary. If the Treasury were raising a couple billion dollars and drawing it all out at once and there were 4 or 5 billion of excess reserves in the banks, it would be a perfectly easy matter to draw out of the banks of the country a couple of billions if they had excess reserves in excess of that amount. But, as I explained, that is not the case today. The total excess reserves of all banks are about one and a half billion and here is a financing operation of 13 billion.

Mr. GIFFORD. How much of that will be conversion; how much of the 13 billion needed will be simply to pay off what is due—will be conversion?

Mr. ECCLES. None of it will be conversion; not a dollar of it will be used to pay off what is due.

Mr. SMITH. Is not part of it used in tax anticipation bills; is not that involved in that procedure; is not that part of it?

Mr. ECCLES. No, it does not cover tax anticipation notes, except one series, what is known as the two-purpose tax anticipation note, a 3-year note, and a very small part of those notes are used to pay taxes. The great bulk of them are just used as investments.

Mr. GIFFORD. One party told me yesterday when bonds become due they are simply going to convert them into other bonds.

Mr. ECCLES. That is true. There are some certificates coming due on May 1 that will be converted; but that is no part of the $13,000,000,000. The $13,000,000,000 is entirely new money. In addition to the $13,000,000,000 of new money, there is a conversion operation on May 1 covering some seven-eighths percent certificates that fall due on that date.

Mr. SMITH. Does that mean seven-eighths percent per year?

Mr. ECCLES. Per year.

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Mr. Smith. Less than 1 percent per year?

Mr. Eccles. It is a 1-year certificate; that is right. It is three-eighths for 90-day bills and seven-eighths for 1-year certificates.

Mr. Smith. Your alternative might be to lower the reserve requirements?

Mr. Eccles. Well, lowering the reserve requirements would only meet the thing part way. And, of course, if you lower your reserve requirements, that only meets it for this time, and what do you do in August? So it is not a way to meet the problem.

We could either lower the reserve requirements or we could buy billions of Governments—we could do it either way—in order to give the banks sufficient reserves to take care of the heavy withdrawals. But then, when the Treasury spent the money, you would have a large excess amount of reserves. So that it makes for instability, rather than for stability.

The Chairman. Let me ask you one or two other questions. What kind of security do you take from a bank that has a loan account with the Treasury, for the purpose of securing deposits of the United States?

Mr. Eccles. Well, the Governments themselves are largely used. Banks are permitted to put up other securities which are acceptable to the Reserve banks; but, as a practical matter, I think, as all banks have Governments, Governments are largely used—in fact are entirely used—as collateral. There may be some exception; I do not know of it. But if a bank had no Governments and wanted to put up other securities to secure the account, they are permitted to do so.

The Chairman. As a matter of fact they have no other securities in sufficient amounts to take care of the situation, have they?

Mr. Eccles. The banks would prefer to put up Governments rather than other securities, anyway.

The Chairman. But, as a matter of fact, they have no other securities in sufficient amount to take care of the situation, have they?

Mr. Eccles. I suppose if you took all of their loans and investments other than Governments, they could qualify for a sufficient amount; at least some banks could; perhaps some could not.

The Chairman. What happens is the bank buys the Government's obligation and gives the Government credit for it on its deposit account?

Mr. Eccles. That is right.

The Chairman. Then to secure the desposit account they turn around and deposit Government obligations with the Federal Reserve bank?

Mr. Eccles. That is right.

Mr. Gifford. How about the 8 billion that the individuals and corporations buy—will they take all that money out to buy the 8 billion of the 13 billion?

Mr. Eccles. Well, they would have to take that money out to buy them unless the bank has qualified for a sufficient amount in the war loan account to cover the subscriptions of their customers in the bank.

Mr. Gifford. How can you say there will be 13 billions of new money? If I buy a bond or a corporation buys a bond, we have to check it out of our account.

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Mr. ECCLES. You check it out of your account in the bank and it goes into the Treasury account in the same bank. So that, so far as the bank is concerned, so far as their deposits are concerned, it still has the money.

Mr. GIFFORD. But we do not have to deposit the bond to do that.

Mr. ECCLES. No; but if you buy a bond from the bank, you give the bank your check. All right. The bank charges your account with your check and credits the Treasury account right in the bank for the amount of your check, and the money never leaves the bank.

Mr. GIFFORD. That is true, but it takes that much money; that 8 billion as you call it would be subtracted from that?

Mr. ECCLES. No; it creates part of the 13 billion. To the extent you give the bank your check, or any other individual or corporation gives the bank a check for the Government securities that it wishes to purchase, the account of the individual or corporation would be charged for the amount of the subscription, and the war loan account in the bank would be credited with the amount of the subscription. So that there is no money that leaves the bank. That is why we are so anxious to get all the banks to qualify for war loan accounts, so as to avoid funds leaving the banks until the Treasury spends the money. Then, as it spends the money, the money will go back into the economy as a whole and each bank will get some of the money back. They may not get the amount back which was withdrawn, whereas some other bank may get more money back than was withdrawn. But the economy as a whole would get back just the amount that the Treasury withdrew and spent.

Mr. GIFFORD. Are you going to tell us there is 13 billion more money in the country by that process?

Mr. ECCLES. There would be 5 billion more.

Mr. GIFFORD. That is what I am trying to say.

Mr. ECCLES. So far as the 8 billion that individuals and corporations buy, that creates no new money.

Mr. GIFFORD. That is what I asked you.

Mr. ECCLES. That creates merely a velocity of use or turn-over. It merely means the transfer of funds from one ownership to another ownership. When the banks buy securities, it means the creation of new money.

Mr. GIFFORD. I understand that. So that there would be 5 billion more in our economy than there was before—permanently?

Mr. ECCLES. That is right, unless and until bank holdings of Government securities diminish.

Mr. BROWN. Governor, suppose under this bill you have a bank that has $500,000 of deposits and suppose the bank fails and $100,000 of those deposits is war fund money: Now, would the Government be treated any differently, or would the individual depositor be treated just like the Government?

Mr. ECCLES. The Government's $100,000 is secured with $100,000 of Government bonds. That is a preferred claim.

Mr. BROWN. In other words, this does not injure the individual deposits by reason of having this money deposited?

Mr. ECCLES. I would not think it would injure the individual depositors.

Mr. BROWN. I think that is one of the most important questions that we ought to consider. If we pass this bill, I certainly do not

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want to give the Government deposits an advantage over individual deposits.

Mr. ECCLES. Well, we have always had it. There is a statutory requirement that Government deposits with banks must be secured. That has always been the case. And there are many Government accounts outside of the war loan account.

Mr. BROWN. Well, does the bank then pay a premium on these other accounts you speak about; do they pay a premium for this Government money on deposit?

Mr. ECCLES. How do you mean, pay a premium?

Mr. BROWN. Well, would they have to pay one-twelfth of 1 percent on the Government deposit, because on all money they have now they have to pay that? Now, do they have to pay it on the Government funds they have?

Mr. ECCLES. They do. Banks whose deposits are insured by the Federal Deposit Insurance Corporation pay one-twelfth of 1 percent on all funds, including the war loan account, and what we are asking here is that the war loan deposit account, which is now subject to the F. D. I. C. assessment, be relieved of that assessment. We are not asking that other Government accounts be relieved of the assessment, but merely the war loan deposit account.

Mr. BROWN. What I am trying to get at is how that will affect the individual depositor. Would it injure him in any way if this bill were passed?

Mr. ECCLES. I do not think it would affect him at all.

The CHAIRMAN. Governor Eccles, we passed amendments to the Federal Reserve Act which authorized advances or loans to be made, secured by Government obligations, to nonmember banks. I mean loans to nonmember banks, partnerships, individuals, and so forth. What has ever been done about that; what has been the operation under that?

Mr. ECCLES. Well, it is still in effect, but very little use has been made of it by the banks.

The CHAIRMAN. Has the Federal Reserve put that provision of the law into effect in an effort to develop that type of business by Federal Reserve banks?

Mr. ECCLES. It is in effect.

The CHAIRMAN. I beg pardon?

Mr. ECCLES. The Federal Reserve, of course, is prepared, in accordance with statutory requirements, to make loans to nonmember banks as well as member banks; likewise to make loans to others as required by the statute; but there has been, so far as I know——

The CHAIRMAN. As a matter of fact, they have not made any such loans as that?

Mr. ECCLES. There may have been some; I could not say. If there are, they are isolated matters; because, if a customer wants to borrow on Governments, he can go to the bank and ordinarily borrow more cheaply then he can from the Federal Reserve bank.

Mr. GIFFORD. I want to have you explain about this transfer of funds from one bank to another and show the advantage to be gained by it. I brought that question up yesterday.

Mr. ECCLES. I do not understand.

Mr. GIFFORD. Where a bank has deposits in other banks which it can transfer or not.

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Mr. ECCLES. Yes.

Mr. GIFFORD. What is the advantage of it?

Mr. ECCLES. What you are speaking of is what we call interbank deposits?

Mr. GIFFORD. Yes.

Mr. ECCLES. The banks that are members of the Federal Reserve System, member banks, are required, of course, to carry certain percentages of their deposits with the Reserve bank of their district. Those banks do not necessarily have to carry balances with other banks, because they can effect all of their collection operations through the facilities of the Reserve bank. Nonmember banks, under the various State laws, are required to carry certain reserves. Those reserves can be carried with other banks—reserve city banks, central reserve city banks—as they are not members of the Reserve System they do not have all the rights and the privileges of the Reserve System.

If they should join the Reserve System, there would be no reason to carry balances with other banks; but they are required now to carry balances with other banks, or to carry cash in the vault, to meet the State reserve requirements—cash in the vault plus balances with other banks to meet the statutory reserve requirements applicable to State nonmember banks.

Mr. GIFFORD. Do they escape the one-twelfth assessment?

Mr. ECCLES. No.

Mr. GIFFORD. What advantage is there in doing that?

Mr. ECCLES. Well, they are required by statute to carry reserves and, if they are not members of the Reserve System, there is ordinarily only one place where they can carry them, that is, in other banks.

Mr. GIFFORD. They cannot hold them within their own bank and call them reserves?

Mr. ECCLES. Well, they could carry them in currency in their vaults. But, from the standpoint of facilitating their operations, it is necessary, in order to clear transactions, to have accounts either in the Reserve bank or in other banks. For instance, a customer of a country bank may want a draft on a New York bank or a Chicago bank, or may want a telegraphic transfer of funds; and there is the need of collecting checks that are deposited with the bank but are payable in other cities. It is necessary to clear those items through their correspondent banks, if they are not members of the Reserve System.

Mr. GIFFORD. I have one question more and then I am done. It is very important to the people at large, I am sure. What is that B–25 that a certain kind of notes can be discounted for only 3 months and at the end of that time must be reduced 25 percent. Whose order was that?

Mr. ECCLES. I could not tell you; I do not know to what you are referring.

Mr. GIFFORD. Where a note is sent in to a bank, they say they have orders in No. 25 that this note can be discounted for not longer than 3 months and, at that time, one quarter of it must be paid. I have it on my desk from my own bank.

Mr. ECCLES. Well, who is the order from?

Mr. GIFFORD. Well, it came from the Comptroller yesterday. I asked him and he said he did not know.

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Mr. ECCLES. I have not heard of it.

Miss SUMNER. It is not true in our State.

Mr. KUNKEL. Governor, why should you have this deposit insurance on any riskless deposits? You just called attention to the fact, where there are Government deposits in the banks aside from war loan accounts, they are completely protected, and the same is true of State funds in many instances.

Mr. ECCLES. Of course, if you raise the rate high enough on the risk deposits, then if you could determine what they were, you possibly could eliminate it on the riskless deposits. It is a question, it seems to me, of what funds the Federal Deposit Insurance Corporation requires to meet its contingent liabilities to the depositors in the banking system.

It would be rather difficult, it seems to me, to define a "risk" deposit and a "riskless" deposit. There is certainly a great variation of the definition of "risk," and what might be a riskless deposit now would, in a depression become a risk deposit.

Mr. KUNKLE. I mean a Government deposit secured by Government bonds would be a riskless deposit.

Mr. ECCLES. Well, I think that, of course, is correct, that no money was ever lost where Government bonds are involved. The only way you could lose money on a deposit secured by Government bonds, of course, would be to have to sell the Government bonds at a discount. If the bonds were carried through to maturity, of course they would pay out the amount of the deposit. But in most instances there is a big margin, even in the case where Government securities are put up as collateral on Government deposits.

Mr. KUNKEL. There is one extreme case. A bank at home carries an average deposit account of five to ten million dollars and, of course, the only liability of the Federal Deposit Insurance Corporation is up to $5,000. Yet they have to have Federal Deposit Insurance on that deposit and they also have to furnish security because the depositors are in Pennsylvania.

Mr. BALDWIN. Mr. Crowley suggested yesterday that without any additional risk he felt all demand deposits could be secured. I believe that was his statement; is not that correct?

The CHAIRMAN. That is right—without additional charges.

Mr. BALDWIN. Without additional charges, that all demand deposits could be secured.

Mr. SMITH. You mean exceeding $5,000?

Mr. BALDWIN. Yes; I mean full coverage.

The CHAIRMAN. As a matter of fact, what he undertook to say was that they are securing all deposits anyhow; that they won't let you say so under the law, but in practical effect that is what happens.

Now, I want to ask you about this provision authorizing loans by the Federal Reserve bank on Government securities to partnerships, corporations and State member banks. Would it not be helpful in financing the Treasury program for State banks to understand that they have this privilege of borrowing on Government securities from the Federal Reserve banks?

Mr. ECCLES. I think they all do understand that. We have certainly given it plenty of publicity, that they not only can borrow on Government securities, but the Reserve banks have given a special rate permitting all banks to borrow at par on Government securities

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at a rate of 1 percent; even though the bank might be getting 2 or 2½ percent on the security, it can still borrow at par at 1 percent.

The CHAIRMAN. I am just wondering if we are not losing their aid in the Treasury financing program. I am only asking for information.

Mr. ECCLES. No; I am sure all of the banks are well aware that they can borrow from the Federal Reserve bank of their district 100 percent, or can borrow the par value of the security, at the rate of 1 percent. They likewise know that in the case of Treasury bills which bear three-eighths of 1 percent, they can sell them to the Reserve bank of their district, at their option, on the basis of a discount rate of three-eighths and they can reserve the right to buy them back at any time at the three-eighths discount rate. So that, so far as Treasury bills are concerned, they are the equivalent of cash.

Mr. KEAN. In the Senate bill, it provides in the first clause "6 months after cessation of hostilities." In section 2 it remains the same day it is now—" 6 months after" the termination of the present war. Now, the chairman thought that was inadvertent by the Senate. I do not think it is. I think that is probably a good idea as loan deposits are going to continue for a while after the war, and if we provide "6 months after the end of hostilities," you are going to get an automatic increase in reserve requirements at a time when you might not want to do it.

Now, was that done deliberately?

Mr. ECCLES. I could not say.

Mr. KEAN. Would it not be a mistake to have an automatic increase in the reserve requirements 6 months after the end of hostilities; when we might still be trying to sell bonds, as we did after the last war—the Victory bonds—to clean up the slack of expenditures at the end of the war?

Mr. ECCLES. Well, I do not think that has anything to do with an automatic increase in reserve requirements.

Mr. KEAN. Well, it would, because you would automatically increase your reserve requirement if this thing suddenly expired.

Mr. ECCLES. That would increase the reserve requirements to the extent of the reserve requirements on the war loan account.

Mr. KEAN. Yes; that is right.

Mr. ECCLES. That is correct. But I would dislike very much to have to see this go to conference and get that delay. As I understand it, in the Senate bill that is uniform. It provides until 6 months after the cessation of hostilities.

Mr. KEAN. In section 1; but in section 2——

Mr. ECCLES. No, it is uniform; it is the same in both.

Mr. KEAN. It is uniform in both?

Mr. ECCLES. That is right.

Mr. KEAN. The chairman said it was not the other day—in the Senate bill.

Mr. ECCLES. The Senate bill is uniform.

Mr. BALDWIN. The House bill is not uniform.

Mr. ECCLES. It is the House bill that is not uniform.

The CHAIRMAN. The Senate changed it, then, did they?

Mr. KEAN. The Senate made it uniform in both cases.

Mr. ECCLES. The Senate made it uniform. It is the House bill that is not uniform.

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Mr. KEAN. Which one did they adopt?

Mr. ECCLES. You mean the Senate?

Mr. KEAN. Yes.

Mr. ECCLES. That "until 6 months after the cessation of hostilities in the present war," as determined by proclamation of the President, and so forth.

Mr. KEAN. That is the same in both cases?

Mr. ECCLES. That is the same in both cases in the Senate bill. It is in the House bill that it is not uniform.

Mr. WOLCOTT. The Senate bill says "until 6 months after the cessation of hostilities in the present war" as determined by proclamation of the President?

Mr. ECCLES. That is right, "as determined by proclamation of the President."

Mr. WOLCOTT. All of these other emergency measures say "cessation of hostilities, or by proclamation of the President, or by concurrent resolution of the Congress."

Mr. ECCLES. Well, I do not know why this is any different—"until 6 months after the cessation of hostilities in the present war as determined by proclamation of the President or concurrent resolution of the Congress," and so forth.

Mr. KEAN. "Concurrent resolution" is in there?

Mr. ECCLES. That is right.

The CHAIRMAN. This language where you provide for its being subject to termination upon the basis of a proclamation of the President, we say "upon a proclamation of the President declaring the termination of the war"; and just changing the language to declare "upon the termination of hostilities" is sort of mixing that up. But that is a technical matter which we can work out in the committee.

Mr. PATMAN. Mr. Chairman, there is a fundamental question involved in this bill. I am not convinced that it is meritorious; I am not convinced that it should become a law. I am going to seek information from Governor Eccles as to the effect of it and I would like to ask some questions about it without interruption, if the members will permit me to do so.

The CHAIRMAN. That will be entirely for you to decide, whether you wish to be interrupted or not.

Mr. PATMAN. Will the clerk of the committee distribute these booklets, please?

Before the Ways and Means Committee recently, to be exact, on February 14, I appeared and testified about many of the questions that will come up in connection with the consideration of this bill, and if the members will do me the kindness and the courtesy of turning to page 35 of the testimony which is now being given to each member, and will at their pleasure and convenience give it consideration, I would appreciate it very much. In connection with that testimony you will find the testimony of former United States Senator from Oklahoma, Robert L. Owen.

Senator Owen was chairman of the Committee on Banking and Currency of the Senate when the Federal Reserve Act was passed. I think he knows more about the monetary question than any man in the world, and I think he is one of the best-informed men in the world, and I believe that anything that Senator Owen says is certainly worthy of consideration by this Congress, and the questions

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discussed by Senator Owen are material and germane to a discussion of this bill—its merits or demerits.

Governor Eccles, I believe you said that you want this bill as an emergency measure indicating that the success of the next drive for funds will depend at least to some extent upon the passage of this bill.

Of course, if that is true to any major extent, we should pass the bill quickly and there should be no delay, but I am not convinced of that, and for that reason I want to ask you these questions.

Mr. ECCLES. Let me make this statement. I do not want to give this committee the impression that the Treasury financing would fail. Now, if this bill is not passed, we can reduce reserve requirements. We can buy billions of Government securities.

Mr. PATMAN. Certainly.

Mr. ECCLES. That, however, would create a terrific job on the part of the System to maintain stability in the market so that when the drive is over there would be billions of excess reserves again, and you would have an instability of the Government market. The difficulties of the job of the Reserve System in trying to maintain a stable market would be accentuated.

Mr. PATMAN. Your remarks would be frightening to me if I did not know that you can change these reserve requirements.

Mr. ECCLES. Yes; but you cannot change them overnight.

Mr. PATMAN. Why, you certainly can.

Mr. ECCLES. But as a practical matter, you cannot reduce them and increase them and reduce them and increase them weekly.

Mr. PATMAN. You would not want to do that. You would not have to do it, because the monetary market does not act so quickly as that, and react.

Mr. ECCLES. But our power to deal with the reserve requirements is limited. All that we can give, I think runs somewhere around perhaps $5,000,000,000, which would be the possible total, and we would then be down to the minimum statutory reserve of——

Mr. PATMAN. You can change the statute. Congress can change the statute.

Mr. ECCLES. Congress could, of course.

Mr. PATMAN. Congress has never failed when you wanted it done.

Mr. ECCLES. That might mean that there would be no reserve requirements.

Mr. PATMAN. You are asking for no reserves here.

Mr. ECCLES. Of course, I am only asking for no reserves against this particular——

Mr. PATMAN. I know it is a particular part.

Mr. ECCLES. Reserves were never required against war loan accounts during the last war, or at any time except after the enactment of the Banking Act of 1935, and that is when reserves were first required against these accounts.

Mr. PATMAN. If I understand you correctly, you are expecting to raise—at least the Treasury is—about $13,000,000,000 in this drive.

Mr. ECCLES. That is right.

Mr. PATMAN. And you are expecting to induce or persuade people who have money, individuals and corporations, to transfer $8,000,000,000 of money that is already existing for $8,000,000,000 worth of these bonds, but after you have done that, you anticipate,

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and you have reasons for that, that you will still need $5,000,000,000 that nobody has the money to furnish; therefore, you will have to deliver these bonds to the banking system and have them create that money by a flick of the pen—just out of thin air by a bookkeeping transaction—and for the creation of that money you expect to pay them interest.

All right. Now, on that $5,000,000,000, the two points involved, as I understand them, are:

First, that this $5,000,000,000, as a deposit in 13,500 banks in the country, there would have to be an assessment of one-twelfth of 1 percent paid to the F. D. I. C. under the existing law for a period of time until those funds are transferred to individuals or corporations that the Government will owe and will pay. That is one question, is it not, Governor Eccles?

Mr. ECCLES. That is right.

Mr. PATMAN. All right. Now then, how long do you anticipate it will take on an average for that $5,000,000,000 to be transferred from a deposit of the Government of the United States to individuals and corporations that will eventually get it on an average? What would you consider?

Mr. ECCLES. I would not be able to guess. It depends entirely on the total amount that the Government raises and upon the amount that the Government expends.

Mr. PATMAN. Would you say 3 months, or 6 months?

Mr. ECCLES. It depends entirely on what they get in taxes as well. It may run a month, 2 months, 3 months. It would simply depend upon the Treasury's policy whether they wanted to use up that $5,000,000,000 first, or whether they used other sources of income.

Mr. PATMAN. Well, you would say at least within 6 months?

Mr. ECCLES. Anywhere from 1 month to 3 months.

Mr. PATMAN. One to three. Do you think one-fourth of a year would be a reasonable time? Is that right?

Mr. ECCLES. That is right.

Mr. PATMAN. Now then, the net result of that is that if you sell these $5,000,000,000 in bonds to these banks and create the money to buy them, and you pay those banks a low rate of interest, seven-eighths of 1 percent, that means for the money they have created of that $5,000,000,000 for 1 year they will get $43,750,000 in interest.

Mr. ECCLES. For 1 year?

Mr. PATMAN. For 1 year. All right, now, then, for the 3 months that they would have to pay that one-twelfth of 1 percent, they would be saving $1,041,000. Now, that looks to me like it is a pretty small thing, if you allow them to create this money and give them an annual interest rate of $43,750,000 for this money which you admit is just created by a bookkeeping transaction, and now then you are trying to save them this little assessment of $1,021,000. It looks pretty small, Governor, pretty small.

Mr. ECCLES. Of course, in the first place, you are figuring $43,000,000 for a year.

Mr. PATMAN. That is right.

Mr. ECCLES. The difficulty is, when a bank sets up this deposit, the bank does not know whether that deposit is going to be there a day, 1 month, or 2 months.

Mr. PATMAN. That is right.

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Mr. ECCLES. As far as they are concerned, the banks hesitate. They say:

> Well, we do not want to open up those accounts because they are subject to immediate withdrawal. We know that the Treasury may draw on them at any time, and therefore we have to keep those funds that we set up here; we have to keep those funds idle in the Reserve banks.

Now, that is not the view of some of the larger banks who do have war loan accounts, and who have been, I think, convinced of the advantage of having those war-loan accounts.

The difficulty has been with a lot of the smaller banks primarily, who do have balances or reserves, and what they do, they would sooner buy and pay immediately for Government bonds than set up the war loan accounts. There are thousands of banks that, instead of opening a war loan account, would prefer to pay for the bonds at the time, by drawing against their reserves in the Reserve bank, or by drawing against their balances in a correspondent bank rather than qualify for a war loan account, and that means, of course, a transfer of funds. There is a good deal of merit to the point that you make, and I have made the same argument. I have argued with banks that even though they have to pay one-twelfth of 1 percent, they can still use this account profitably, and I think that there is considerable headway being made with the larger banks, but we have still had great difficulty in getting the thousands of smaller banks to open up accounts. They argue that they do not need these additional funds and that they do not want Government deposits upon which they have to pay one-twelfth of 1 percent. Whatever bonds they buy, they will pay for them in cash and they do not want the deposit account.

Mr. PATMAN. You are just as well off, and the Treasury is just as well off that way.

Mr. ECCLES. The Treasury?

Mr. PATMAN. Certainly it is.

Mr. ECCLES. Sure. They are just as well off. They are no better off and they are no worse off. They are as well off as far as they are concerned if the Federal Reserve will stabilize or maintain a market on those securities, but our responsibility in this size of an operation is one of maintaining a stable situation which will assure the success of the financing.

Where there is a huge volume of funds, that is, where there is an unknown volume of funds coming in from 14,000 banks all over the United States into the Federal Reserve banks, there could be created overnight a tight money situation that would be very difficult to meet. The difficulty is that in this country out here [indicating] they will say, "I have big balances over in Chicago and New York," and they can just draw down these balances, and transfer them to the Reserve banks, and that can create a tight money situation in the city banks where the balances have been carried. That is another aspect of the problem.

Mr. PATMAN. Would you not think that a tight money situation is improbable when our actual currency in circulation is increasing at the rate of $187,000,000 a week?

Mr. ECCLES. Temporarily tight, I mean, in the banking system. The amount of currency in the field has no influence whatever upon an immediate situation that could develop in the banking system.

Mr. PATMAN. I do not agree with you.

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Mr. ECCLES. The thing that affects the banking system is the amount of the reserves the banks have; the banks, if they do not have adequate reserves, immediately start selling their securities, and as they sell their securities the Federal Reserve has to buy those securities, and as we buy the securities, we, of course, supply the reserves which they lose.

Now, as the Government spends the money, the funds go back and the banks have then huge excess reserves again, and then it is a question of selling back the Government securities, so you would have a terrific volume of Government securities coming into the Reserve banks and going out of the Reserve banks, and that would create a situation which would be very difficult to handle.

Mr. PATMAN. You still do not frighten me, Governor, on that at all, because I know that you can work pretty fast. You have the power and the authority to work fast.

Mr. ECCLES. We cannot work fast at all, because there are 12 men who have to be brought into meetings from all over the United States here, and it is a question of agreement on the policy on the open market, in the first place. When it comes to the reserve requirements, it is not as though you have one person who can act. You have a Federal Reserve System. You have a Board, and it is not possible to act overnight as you have indicated.

Mr. PATMAN. And that Board operates through policies adopted by the Board, and it does not have to be in session every day for its policies to be carried out.

Mr. ECCLES. It has to be in session before it can increase or reduce reserve requirements.

Mr. PATMAN. That is unquestionably true.

Mr. ECCLES. It would be likely that it would take weeks of discussion before you would get action.

Mr. PATMAN. If there were a tight money situation, you could probably do it rather soon, Governor Eccles.

Mr. ECCLES. No; I do not believe we could do it soon at all. We would possibly buy a lot of securities. We would probably stand there. Instead of having $5,000,000,000 of securities as at present, we might have to buy $5,000,000,000 more in the market.

Mr. PATMAN. Suppose you did. Would that hurt?

Mr. ECCLES. It would not do any particular damage.

Mr. PATMAN. No harm at all.

Mr. ECCLES. No, except then as soon as the drive is over you would have to be in the market again and buy and sell.

Mr. PATMAN. You have got a whole army of people working on the thing right at the moment.

Mr. ECCLES. What harm would it do to adopt a program here that would make that unnecessary? That is the judgment of all those that have to do with this mechanism and with the operation. You say that it would not do any harm to have to buy a lot of securities and sell a lot of securities. I say that it would do far less harm to get these banks to open up war loan accounts, and, to the extent that waiving the reserve requirements and waiving the F. D. I. C. assessments would accomplish that, that is a very, very small concession to make in order to help facilitate financing. That is the way I feel about it.

Mr. PATMAN. Let me get to another point. We have covered the one-twelfth of 1 percent.

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The other is on the no reserve requirement, no reserve requirements for the $5,000,000,000. I am talking now in the light of this bond drive.

Under the existing law, when the banks buy these $5,000,000,000 in bonds, they will have to set aside a certain reserve, depending upon the reserve requirements at the time.

Now, you proposed and said that these banks that want to buy these bonds, they make application to the Federal Reserve banks, and the Federal Reserve banks can in advance certify that a certain bank can buy up to a certain amount of bonds and not have any reserves at all, and you anticipate, at least you contemplate, that you will have enough to absorb this $5,000,000,000, do you not, Mr. Eccles?

Mr. ECCLES. I don't——

Mr. PATMAN. Enough applications for extensions of this privilege without reserves to absorb the $5,000,000,000 in bonds.

Mr. ECCLES. I do not get your point.

Mr. PATMAN. Well, the point is, you take a bank in Texarkana, Tex., that buys $1,000,000 worth of bonds. As it is now, when that bank buys $1,000,000 worth of bonds, it creates the money on the books of the bank to buy the bonds, they give a deposit to the Government, and on this deposit they have to maintain a certain reserve.

Mr. ECCLES. That is right.

Mr. PATMAN. Depending on what the reserve requirements are in that town at that time.

Mr. ECCLES. The class of bank it is, what class bank it is.

Mr. PATMAN. What class bank. All right.

Now, then, you would change that so as to let this bank make application now for credit to get the benefit of this privilege up to, say, $5,000,000, and the Federal Reserve bank at Dallas would say, "That is all right, sufficient proof, O. K. it," and then this bank, when this drive comes on, would be able to buy up to $5,000,000 in bonds and give the Government credit on the books of the bank and not have to put up any bonds as they do now as security.

Mr. ECCLES. Oh, they would have to put up $5,000,000 of bonds.

Mr. PATMAN. Put up in the Federal Reserve bank in Dallas in advance?

Mr. ECCLES. Oh, yes, when the deposit account is opened.

Mr. PATMAN. That is right, but they would not have to maintain any reserves against this $5,000,000?

Mr. ECCLES. They would not have to maintain a statutory reserve which would, in the case of a reserve city bank, be 20 percent. In the case of a country bank it would be 14 percent.

Mr. PATMAN. Yes. Now, Governor Eccles, if you had the power yourself to raise or lower reserve requirements of banks in order to take care of any situation that might arise during war, you could handle this situation with this law, could you not?

Mr. ECCLES. I would not think so.

Mr. PATMAN. Do you mean to say you could not?

Mr. ECCLES. I do not think so. I think it would be very, very difficult.

Mr. PATMAN. You do not mean to say now that the success of this war depends upon this bill.

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Mr. ECCLES. I would not deal with the problem by changing reserve requirements. The instrument of changing reserve requirements is still too cumbersome, and it is not a flexible instrument at all. It gives reserves to all banks uniformly, or takes them away whether a bank needs them or does not need them. If one bank may have an excess reserve, and you reduce reserve requirements, you add to those excess reserves so that the difficulty with the reserve requirement instrument is that it is a shotgun method, and it is not an instrument that should be used frequently.

The increased reserve requirements were needed at the time of the Banking Act of 1935 in order to offset the large reserves that were being created by gold imports. The large gold imports and the silver purchases that were made in this country during the past 10 years were responsible for the large increase in excess reserves, and for the excessively easy money situation that developed.

It was felt that the Reserve System should have the authority to lock up, in effect, the large gold imports that came in, to sterilize, in effect, the gold imports by the right to increase the reserve requirements.

Now, that was done in part. The gold is still here. As I have said many times before, had this country owned the large amount of gold that it now has at the time the Federal Reserve Act was passed in 1913, very likely the statutory reserve requirements would have been placed very much higher than they were at that time, and I personally would dislike very much to meet this situation by the reduction of reserve requirements.

Mr. PATMAN. Let me suggest to you that the only inconvenience that could be caused, say, in Texarkana, in a Texarkana bank, would be if they needed more reserves, to either sell $1,000,000 of Government bonds to the open market committee, and thereby enable itself to buy $10,000,000 in Government bonds upon that reserve, or the Texarkana bank put up bonds that they own receiving upon which there is an interest charge of 2½ or 3 percent at the Federal Reserve bank at Dallas, and get that money at 1 percent, at all Federal Reserve banks.

Mr. ECCLES. There are no bonds purchased today that yield more than 2 percent.

Mr. PATMAN. That are purchased directly by the Government?

Mr. ECCLES. The Government is issuing no bonds available to banks that yield more than 2 percent.

Mr. PATMAN. You mean the Government is not selling them any bonds?

Mr. ECCLES. That is right.

Mr. PATMAN. But that does not keep them from buying bonds on the open market.

Mr. ECCLES. There are no bonds in the open market they can purchase except one long-term issue that would yield them, I think, more than about 2 percent. The bonds are already selling at substantial premiums.

Mr. PATMAN. I understand.

Mr. ECCLES. So that the average that the banks are possibly getting on their portfolios today, considering the bills, the certificates, the notes, and the bonds, would not be much more than 1 percent.

Mr. PATMAN. Well, suppose that these bonds are sold to the banks at seven-eighths of 1 percent.

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Mr. Eccles. One-year Treasury certificates?

Mr. Patman. One-year Treasury certificates. Now, you know that in all probability they will eventually become long-term bonds, will they not? I mean that long-term bonds would be sold to take them up. That is what usually happens.

Mr. Eccles. I do not know whether that would happen or not.

Mr. Patman. Can not you see, Governor Eccles, the possibility of a $300,000,000,000 national debt if this war lasts much longer?

Mr. Eccles. If Congress does not do a better job about taxation than they appear to be doing, I would hesitate to say where the debt may go, or what may happen in the inflationary picture.

Mr. Patman. And you do not think that Congress has been doing a good job on taxes?

Mr. Eccles. No, sir.

Mr. Patman. You do not think so?

Mr. Eccles. I do not.

Mr. Patman. They have been considering, and I think they have been giving sympathetic consideration to it. I want to pay every dollar we can through taxes.

Mr. Eccles. They have been considering without action too long, and they are just about a year late.

Mr. Patman. I think that we are raising a lot of money. The taxes that each individual pays, I think that he realizes that the war is on, and that Congress has actually placed the tax burden on the country.

Mr. Eccles. Well, we are doing the poorest job of any country in the world today on the picture that the Government is spending $250,000,000 a day, and getting one-third of it back in taxes, and the rest of it is just inflating the economy.

Mr. Patman. If we have a $300,000,000,000 debt, and we can maintain a 2½ percent interest charge, that is $7,500,000,000 a year interest. Do you believe that the people can pay that much interest burden every year and carry on the other normal expenses of the Government?

Mr. Eccles. I do not think that it makes any difference because the people will be getting $7,500,000,000 of interest.

Mr. Patman. You are assuming that the bonds will be equally distributed, are you not, Governor Eccles?

Mr. Eccles. They will possibly be distributed somewhere in relation to income. Income is not equally distributed, and neither are bonds, and taxes are not equally distributable. Taxes are supposed to be in relation to income, but so far as the economy as a whole is concerned, the economy will be $7,000,000,000 better able to pay taxes by getting the $7,000,000,000 of interest than it would be if they did not get the $7,000,000,000.

Mr. Patman. In other words, the interest burden will be a blessing.

Mr. Eccles. I would not say it is a blessing at all. It is a negative factor, taking the economy as a whole. So long as the debt is held internally, the debt is not destructive. The real problem is the way the financing is done. To the extent that we have to be financing this war through the inflationary route of bank borrowing, just to that extent you increase the total volume of your supply of money, and it accentuates greatly the inflationary nature.

Mr. Patman. Now, Mr. Chairman, it is about 25 minutes to 1 and it is going to take me a good deal more time to finish, and I

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would really like to ask some other questions. I regret to be compelled to make the request that Governor Eccles come back, but I do not see any other way out of it.

The CHAIRMAN. Let me ask the committee what about a meeting tomorrow.

Mr. BALDWIN. Do you expect to take action tomorrow?

The CHAIRMAN. We are not going to act tomorrow.

Mr. PATMAN. You would not want to interrogate a witness if the members know in advance that nothing will be done.

The CHAIRMAN. I just want to say this, we are not going to act tomorrow. I guess we might as well assume that we will not. I suppose we might as well come back Monday, and then we can probably conclude the examination, and act all on the same day, Monday.

Mr. FORD. May I interpose a question. Mr. Eccles, is not a reserve a kind of insurance?

Mr. ECCLES. What kind of reserve?

Mr. FORD. Why do you put reserves against deposits?

Mr. ECCLES. It is not insurance at all to my way of thinking.

Mr. FORD. What is it, then?

Mr. ECCLES. It is required for the purposes of national credit policy and for operating reasons. Most countries have no reserve requirements. Canada, I do not think, has a statutory reserve requirement. Great Britain has never had a statutory reserve requirement, but as a matter of operation the central bank has pumped funds into the banking system of sufficient amount to maintain a reserve that I think runs anywhere between 12 and 15 percent in England, but in both countries, you have huge central branch banking set-ups, and it becomes an easier matter to handle than would be the case in this country where 48 different States have different set-ups, with the national banking set-up, and with a set-up that calls for State member banks as well as State nonmember banks.

Mr. FORD. Why does an insurance company set up a reserve?

Mr. ECCLES. Well, its reserve is available to take care of losses. These reserves that a bank carries with a Federal Reserve bank are a required portion of its deposits, and not a part of the capital account at all. A bank can have a reserve set up as a part of its capital account—a reserve against losses or depreciation—and that is a form of insurance, but that is a very different kind of reserve than the reserve against deposits which must be carried in the central banks.

Mr. FORD. Why is it that so many people are advocating, at least a group are, 100 percent reserves? How would that affect deposits?

Mr. ECCLES. What they are advocating, 100 percent reserves, is to take away from the banks any discretion whatever as to the amount of money they will loan. That would be the effect of it.

Mr. FORD. What I was thinking of was this: The deposit account by the Government in the first place is insured 100 percent by a deposit of securities, is it not?

Mr. ECCLES. That is right.

Mr. FORD. Then, why should it not be necessary to impose any further tax on it for the purpose of insurance?

Mr. ECCLES. Well, of course, I do not think you should impose an F. I. D. C. assessment on that particular account. That is why we are proposing this bill.

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Mr. FORD. I realize that, but on any account which the Government has where it is insured 100 percent by the deposits.

Mr. ECCLES. I do not feel that the question of insurance was based upon the risk of the account at all. The F. I. D. C. insurance covers risk as well as nonrisk deposits. It is universally applied, and I think that is proper. I think if you begin to put different rates on different types of deposits, dependent upon risk, you would have certain deposits possibly bearing a very high rate. You would have other deposits bearing no assessment rate at all. I think that thing has all been debated a good many times, and I think that the conclusion that was arrived at, to apply a uniform low rate on all deposits, is the most simple and the most equitable way of getting at the problem. It is a question of the F. I. D. C. wanting so many funds, and they feel that one-twelfth of 1 percent is not excessive, and it does not give them more funds than they require.

I suppose if they felt it was not adequate they would want to raise the rate. If they felt it was giving them more money than they needed, they would want to reduce the rate.

Mr. KUNKEL. Is not the essence of insurance the amount of risk, and does not your rate always vary with the amount of risk?

Mr. ECCLES. Not this type of insurance. This is entirely different than a private insurance company, entirely different.

Mr. FORD. This is an over-all estimate?

Mr. ECCLES. That is right. Social Security is not that type of insurance at all. Old-age pension schemes, for instance, are not based upon the risks involved.

Mr. Chairman, let me say, I do not know whether it is directly in line with what is being said, in the original bill or law of 1933 the first deposit insurance law was passed, we set up a mutual insurance system with a definite charge, one-quarter of 1 percent, with a proviso that no further assessment would be levied except when necessary to restore the fund to an amount equal to one-quarter of 1 percent of the deposits of the participating banks. We were clubbed into backing off from that law and changing it requiring continuing assessments. Later on the banks came along and wanted us to reduce the assessments. The record shows that if they had permitted their original law to remain in effect, the banks would never have been assessed again down to this time in order to maintain the required fund.

Mr. KUNKEL. May I ask you a question at this point?

The CHAIRMAN. We offered them cheaper insurance, but they would not have it.

Mr. KUNKEL. Was it not understood at that time when the sum of $500,000,000 was reached, as a reserve for the Federal Deposit Insurance, that at that time the assessments would be reduced or limited?

The CHAIRMAN. Oh, no. When the original law was passed, it is just as I tell you, very definitely. The thought was that to make the fund sufficient they should have an amount equal to one-quarter of 1 percent of the deposits of the participating banks, and that there would be no further levy unless that fund was depleted. Then raise it only sufficiently to restore it.

Mr. KUNKEL. Was the sky the limit on the amount of reserves?

Mr. WOLCOTT. According to Mr. Patman's testimony before the Ways and Means Committee and citing, as he does, the Journal of the American Bankers' Association of February 1943, it is estimated

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that the Government securities held by the banks on June 30, 1944, would be $112,000,000,000. Their capital is $8,000,000,000. Their deposits amounts to $152,000,000,000. Can you break that down for me and tell me where these deposits are coming from, and whose deposits they are?

Mr. ECCLES. I do not think that is possible, Mr. Wolcott, and it would require a very extensive study that would spread over a period of months. You would have to have the cooperation of all the banks to do it for you. The only way you could find out who owns the deposits, whether corporations or individuals, farmers or laborers—it would require a terrific amount of work, and I do not think the banks would do it.

Mr. WOLCOTT. What I am trying to get at is, where are the banks going to get the money to buy $112,000,000,000 worth with only $8,000,000,000 capitalization?

Mr. ECCLES. The banks could buy all the securities they want on the capitalization. The capitalization has no relationship to the ability to buy securities.

Mr. WOLCOTT. Whose money buys the securities? Are they bought out of deposits?

Mr. ECCLES. Out of reserves.

Mr. WOLCOTT. How are those reserves created so that you can buy $112,000,000,000 of securities?

Mr. ECCLES. The capital has nothing to do with it.

Mr. WOLCOTT. Something has something to do with it.

Mr. ECCLES. It is the central bank——

Mr. WOLCOTT. What makes it possible for them to do it?

Mr. ECCLES. Well, that gets into the question that Mr. Patman has been raising that the banks create our money. If you give the banks the reserves, for every dollar of reserve you give them they can create $5 of money for you. The Federal Reserve System could buy $1,000,000,000 of securities and that would provide $1,000,000,000 of reserves. On the basis of these reserves the banking system could create $5,000,000,000 worth of credit. If we reduced the reserve requirements, correspondingly, they could buy $10,000,000,000.

Mr. WOLCOTT. If there is some arrangement whereby the banks can get a static income of $1,112,000,000 on an investment of $8,000,000,000, I think that we should know about it.

Mr. ECCLES. An income of what?

Mr. WOLCOTT. $1,112,000,000. That is only at 1 percent.

Mr. ECCLES. You are speaking of the interest on the amount?

Mr. WOLCOTT. Just guessing that the interest would be 1 percent.

Mr. ECCLES. What you have got to take a look at here, for the banks, is what are they actually earning on the capital that they have.

Mr. WOLCOTT. Are their earnings in addition to what we were told yesterday?

Mr. ECCLES. No. I have got some figures here. I will give them to you Monday. The earnings of the banks from 1941 to 1943 have gone down.

Mr. WOLCOTT. Will you discuss that for us Monday?

Mr. ECCLES. Yes. They have gone down $55,000,000 in 1942 over 1941.

(Whereupon the committee adjourned subject to the call of the chairman.)

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FEDERAL RESERVE ACT AMENDMENT

MONDAY, APRIL 5, 1943

House of Representatives,
Committee on Banking and Currency,
Washington, D. C.

The committee met at 11 a. m., Hon. Henry B. Steagall (chairman) presiding.

The Chairman. The committee will come to order.

Mr. Patman. Mr. Chairman, I had not finished my questions.

Governor Eccles, in this huge program we have, where we are spending so many hundreds of millions of dollars, that is, if this war continues much longer, of course a large part of that money will necessarily have to be obtained from the banks, the commercial banks, that receive deposits.

I think it is admitted that banks buying Government bonds create the money to buy them, and I just wonder if you have given consideration to the subject of possibly saving the Government, or the taxpayers, interest on any part of that national debt?

Mr. Eccles. You mean——

Mr. Patman. In other words, to the extent that you have even considered it, have you considered saving interest on any part of this national debt?

Mr. Eccles. I would like very much to save interest, but I would not favor robbing Peter to pay Paul.

Mr. Patman. Have you given consideration to any plan, or tried to devise or formulate any plan, that would enable the Government to do any part of its financing without the payment of interest?

Mr. Eccles. The Government can very easily do all of its financing without the payment of interest.

Mr. Patman. You have not answered my question. I asked you if you have given consideration to it.

Mr. Eccles. I have given a good deal of thought to the question of Government financing, but I have in connection with our own presentation of this subject had occasion to analyze very fully your point of view, and I have come to the conclusion that an attempt to finance the Government without interest would be a very inflationary procedure. It would be entirely contrary to the whole basis of our capitalistic system.

Mr. Patman. And you have not tried to devise or formulate a plan that would enable you to do that, or overcome the objections which you now see.

Mr. Eccles. I would not say that I have not tried. No; I have not undertaken to develop a plan that would, to my mind, destroy your whole credit-debtor system.

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Mr. PATMAN. You think that it would be inflationary. If you were convinced that that element could be removed and there would be no more danger than under the present system, would you then give consideration to it?

Mr. ECCLES. I would give consideration to any plan that would save interest if you offset the income which the banks get now from that interest with some other means of sustaining them.

Mr. PATMAN. Sustaining the banks?

Mr. ECCLES. That is right.

Mr. PATMAN. If I understand your theory you consider that interest should be paid on the bonds because you consider that the banks must be provided for more adequately, and that they are now rendering service at a price as low as they could be expected and for that reason this amount of interest should be paid as compensation to the banks for carrying and handling the amount of money, or credit, that is placed in circulation——

Mr. ECCLES. I think that credit extended by the banking system, whether to individuals, cities, counties, States, or Federal Government, should bear interest.

Mr. PATMAN. In other words, you make no distinction between the Government, which is sovereign and has the power to create money and does create money—you make no distinction of the United States Government, and a State, county, or political subdivision? You think that all should pay interest?

Mr. ECCLES. I make no distinction so far as they get their credit from the private banking system.

Mr. PATMAN. Under the present arrangement, if you sell bonds to a bank, a commercial bank receiving deposits, you admit that they do create money to buy those bonds, do you not?

Mr. ECCLES. I meant any loan a bank makes.

Mr. PATMAN. I am not talking about any loans; I am talking about Government bonds.

Mr. ECCLES. The bank creates the money, whether the loan be to the Government or to a private individual.

Mr. PATMAN. And the answer is—yes?

Mr. ECCLES. Well, I reserve the right, Mr. Congressman, to answer these questions as I see fit, and I do not expect that you are going to answer them for me. To simply say the answer is "yes" may well imply that the extension of credit by a bank to the Government has a different effect than the extension of credit by a bank to anybody else, which is not true.

Mr. PATMAN. Well, I was trying to shorten the inquiry, and of course if you want to insist on bringing in everything else, it is all right by me, but still I will ask you this question:

When a bank, a commercial bank, receives deposits by the United States Government bond, it creates the money to buy that bond, does it not?

Mr. ECCLES. It creates the money; that is right. Whether it creates the money to buy that bond, or whether it is using excess reserves that it already has depends upon the condition of the bank.

Any credit, whether to the Government or otherwise, by the banking system results in the creation of money; the money that is created in any capitalistic economy is created through credit extended by its banking system.

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Mr. PATMAN. The Federal Reserve banks now have the authority to buy directly from the United States Treasury bonds up to $5,000,000,000; that is right, is it not?

Mr. ECCLES. That is correct.

Mr. PATMAN. Now, those bonds under the present system provide for that interest charge; that is right, is it not?

Mr. ECCLES. That is right.

Mr. PATMAN. What would be the difference to the country insofar as inflation is concerned if those bonds were sold to the 12 Federal Reserve banks, the $5,000,000,000 worth, without interest? Would it be any more inflationary?

Mr. ECCLES. Yes; very much.

Mr. PATMAN. How would it be?

Mr. ECCLES. It would be inflationary to the extent that that money, when spent, would become a deposit in the hands of the private banking systems on one side of the balance sheet, and on the other side it would be excess reserves, and with those reserves, those idle funds, the banking system, in an attempt to use those funds might buy existing securities, whether public or private. To the extent that they had the reserves they would be under pressure to invest—to that extent they would inflate the total supply of money.

Mr. PATMAN. We are talking about the $5,000,000,000 loan now.

Mr. ECCLES. That $5,000,000,000 would give you possibly——

Mr. PATMAN. It has exactly the same effect, whether it is interest bearing or noninterest bearing.

Mr. ECCLES. It would give you the possible effect of a $25,000,000,000 credit expansion.

Mr. PATMAN. That is true. You do not get my point, or I have not made myself clear. But so far as the Government collecting interest on the $5,000,000,000 is concerned, means nothing in that if they sell $5,000,000,000 worth of bonds to the 12 Federal Reserve banks, and they are interest bearing, it has exactly the same effect on the country and the banking system as if they delivered to these Federal Reserve banks non-interest-bearing securities; is that not so?

Mr. ECCLES. That is right.

Mr. PATMAN. We admit that. We have gotten together on that.

Mr. ECCLES. That is correct.

Mr. PATMAN. All right. So there is no difference at all.

Mr. ECCLES. That is right.

Mr. PATMAN. How do you justify then requiring the Treasury to pay interest on that $5,000,000,000? It is created on the Government's credit, the $5,000,000,000 to buy these Government bonds. It is just an interchange or an exchange of Government obligations.

The Federal Reserve banks take one form of Government obligation and deliver them in return for another form of Government obligation, but the difference is the taxpayers have to pay that interest. How do you justify that?

Mr. ECCLES. It would make little difference whether the Treasury pays the Federal Reserve banks interest on that $5,000,000,000 that you refer to or not. The only advantage in having those bonds that the Federal Reserve takes as marketable obligations is so that the Reserve banks can sell those bonds in the market.

Mr. PATMAN. Eventually.

Mr. ECCLES. That is right.

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Now, the interest that is paid on those bonds to the Federal Reserve banks does not go to the stockholders of the Federal Reserve banks. That interest will help to pay for the operation, or the expense of the Federal Reserve Banking System. The earnings of the System in excess of the dividends which are fixed and run between $8,000,000 and $9,000,000, and of the expense, that is, the dividends and the expense of operating the System—what is left over above that—is added to the surplus of the Federal Reserve System which ultimately would go to the Government, and Congress at any time can appropriate the funds, any part of the surplus of the Reserve banks when they see fit, just as they did in 1933. At that time Congress appropriated $140,000,000 of the surplus of the Federal Reserve banks to set up the capital of the Federal Deposit Insurance Corporation, so, if the Federal Reserve banks do not get interest upon the Government bonds which they hold, then it would be up to Congress to appropriate such funds as would be required to operate the Federal Reserve System and to pay the dividends on their stock so long as that stock was held by the member banks.

Mr. PATMAN. I am familiar with the way the money is paid out, Mr. Eccles, and I am also familiar with the law which was at one time that all the surplus would go into the Treasury of the United States.

Mr. ECCLES. Right.

Mr. PATMAN. I am also familiar with the law which has never been carried out, that an interest charge would be granted the Federal Reserve banks under certain conditions when money was issued. That has never been carried out, but the point I am making is, that if you can sell $5,000,000,000 to the Federal Reserve banks, as you can, and as you have done, you can do that without the payment of interest, and the Federal Reserve banks do not necessarily have to have that interest because they have sufficient earnings in addition to that $5,000,000,000 to pay more than their operating expenses, and I am just giving that as an illustration of what can be done on a large part of the national debt.

Mr. ECCLES. The whole national debt?

Mr. PATMAN. I did not say the whole national debt—I said a large part of the national debt.

Mr. ECCLES. Why not finance it all without interest?

Mr. PATMAN. There is a good reason for that. I am opposed to that. I am in favor of selling all the bonds you can sell to the people that have the money to buy them, or the corporations. I am in favor of considering just as high a tax as possible to pay off as much of this debt as we can, but after we have sold all the bonds we can to people who have the actual money to buy them, and we have raised all the money through taxes that it is possible to raise, a lot of bonds will have to be sold at about 45 to 50 percent of the amount of money we use, and that will be obtained by letting the commercial banks create that money just by a flick of the pen, and we will be in this position of having a perpetual debt on our hands. If this debt gets to be $200,000,000,000, or $300,000,000,000, as many people think it will, the debt for interest alone will be from $5,000,000,000 to $7,500,000,000 a year just for interest. It occurs to me that this Congress will be falling down in its duty if it sits idly by and permits this money to be created in that way and obligates the people and the taxpayers to

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forever pay the interest. It just does not make sense to me. Maybe I am wrong about it, but I have studied it a long time, and I do not see any other way.

Mr. ECCLES. You have changed your views, have you not, Mr. Congressman?

Mr. PATMAN. Not to my knowledge.

Mr. ECCLES. Did you not favor several years ago the selling of noninterest-bearing securities to the banks only to finance the deficit? You favored that, did you not?

Mr. PATMAN. You mean the Federal Reserve banks?

Mr. ECCLES. Yes; and you now favor the public outside the banks buying interest-bearing securities.

Mr. PATMAN. Why, certainly I do, to keep down inflation. We would have inflation in this country if you did not do that.

Mr. ECCLES. How would you prevent the banks from purchasing those securities from the public?

Mr. PATMAN. Let the Federal Reserve banks buy them.

Mr. ECCLES. From the public?

Mr. PATMAN. Yes.

Mr. ECCLES. Why would you stop 15,000 banks? Would you prohibit them owning any Government securities?

Mr. PATMAN. Except a certain amount. The proposal I have sets a dead line, say, December 31, 1941, to permit the banks to always own the amount that they held at that time in Government bonds so as to help them out in their earnings. I would be willing for them to be helped out in their earnings, but let us not be in a position of paying the banks as much in interest each year as their entire capital stock. That time is coming if we do not do something to stop it.

Mr. ECCLES. I am glad to get that point, that you do favor then the banks owning enough Governments for them to have a reasonable——

Mr. PATMAN. Sure I do, because they render a public service.

Mr. ECCLES. Is this not what happens: That as the volume of money increases through the deficit financing operations, private held debt by the banks is rapidly diminishing, and therefore the earnings of the banks from loans and investments other than Government's is falling. But that is being offset, though not entirely, by the increase in the holdings of the Government, and I want to bring out here that the earnings of the banking system for the year 1942, in spite of the large increase in Government securities acquired by them in 1942, are less than in 1941, that the loss of interest through loans paid off by the banking system was not offset by the increase in the interest received by the banks from Government securities, so that the net operating profit from the banks of this country for the year 1942, in spite of an increase of $20,000,000,000 in their holdings of Government securities, was about $55,000,000 less in 1942 than in 1941.

I would like to give you some figures on the trend of bank earnings for 1942 as against 1941, which it seems to me will prove that to stop the banks as of the end of 1941 from acquiring further interest-bearing Government securities is not justified because, after acquiring $20,000,000 more Government securities, the earnings at the end of 1942 are still less than they were in 1941.

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Mr. PATMAN. Let us agree that a different base would be desirable, or a different amount.

Mr. ECCLES. There may be a point——

Mr. PATMAN. That is what I want you to get to. Will we ever reach a point?

Mr. ECCLES. There may be a point where the earnings of the banking system are more than adequate to take care of their increasing expenses, together with a reasonable return on capital. Now, banks, as you possibly know, are prevented from purchasing the 2½-percent Government securities that are being issued. They are allowed to invest in new offerings only up to 7–9 year maturities, which are the 2-percent bonds.

Mr. PATMAN. They are not prohibited from buying them in the open market, are they?

Mr. ECCLES. Yes, they are. They are prohibited from holding.

Mr. PATMAN. The 2½-percent bonds? Do not some banks hold 3- and 4-percent bonds?

Mr. ECCLES. Well, those are the old——

Mr. PATMAN. That is what I mean.

Mr. ECCLES. If they hold them, they are probably bonds that they bought at a very high premium.

Mr. PATMAN. They bought them years ago.

Mr. ECCLES. That is right. They are probably bonds which had been purchased before the period of restriction. Let me put it this say: There is no restriction against a bank's buying bonds already issued except bonds issued after a certain date of a certain type; that is, banks are not allowed to hold those bonds. As the debt increases, there will be increasing amounts of certain types of bonds which the banks are not permitted to take and hold. More 2½ percent bonds probably will be issued in the future and War Saving bonds series E, F, and G, which likewise bear 2½ percent or better and have been issued in large amounts, are likely to be continued.

Mr. PATMAN. They can take them as collateral; can they not?

Mr. ECCLES. That is right, except the E, F, and G bonds, which are not assignable. The 2½-percent bonds, I think, are, but there is a way, of course, of keeping banks from what we may term "profiteering" out of interest paid by the Government. They are a long way from approaching that position.

Mr. CRAWFORD. Will you let me ask a question?

Have you, in your general approach, thought about putting an accelerator or a sliding rule in this provision that has to do with the banks holding enough bonds to cover the operating expenses in the event other types of income do not prove adequate? In other words, suppose as we move on into this war effort the investment of private funds dries up,we might say, and yet we release more and more money to the people with which they can buy something, and, if they do not buy, the Government goes to the commercial banks to do its financing primarily, or if we put in an enforced purchase of Government bonds, or Government securities by the people so as to avoid going to the banks, we may have a situation where the banks will lose, say, 50 or 75 percent of the present papers they have in their portfolios which create earnings for the banks, so we may have a situation instead of using 1941 as a yardstick you will have to move on upward to accommodate your operating expenses of the bank.

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Mr. PATMAN. I agree with you. That is the reason I told Mr. Eccles we could agree that possibly a different or different amount would be desirable. I accept that as logical and reasonable and possibly desirable.

Mr. CRAWFORD. My thought goes into this international phase that is now being so actively discussed between Mr. White, of the Embassy, and some British authorities, and Mr. Morgenthau.

Mr. PATMAN. The reason I make that suggestion is that if we could finance part of this national debt through the Federal Reserve banks, which we can—possibly half of it, at least—the part that we would normally get from commercial banks, that each year we could pay 2½ percent to the Federal Reserve banks on the amount we have financed that way and, in 40 years, that entire amount will be paid. Whereas, if we go ahead and let the private banking system create this money on the Government's credit and we pay them--and eventually we know the rate will be raised—2½ percent each year for 40 years, we will still owe the entire amount. And what I am getting at, Mr. Crawford, is that if something is not done, you are going to have a perpetual debt on the taxpayers of this country and they will never be able to pay any more than the normal interest charges and operating expenses of the Government. And I think that the Federal Reserve bank officials—and I am disappointed that Mr. Eccles refuses to give consideration to it; he insists on closing his eyes and not trying to solve the problem at all—should and I cannot understand why they do not give some consideration and try to save a large part of that interest. I think if you would exercise the same diligence that you insisted Congress should use the other day on raising taxes, you could find some way to do that, Mr. Eccles.

Mr. ECCLES. Well Congressman, when the problem of excess profits of the banks begins to appear, you will find me just as diligent about attempting to avoid profiteering on the part of the banks as we have been to prevent profiteering by anyone else. But that development is in the very opposite direction to what you are referring to. Your discussion is purely academic.

Mr. PATMAN. But you are not thinking about the taxpayers.

Mr. ECCLES. It is a practical question that is before you. The trend of bank earnings is in the opposite direction from what you undertake to indicate here. For instance, I will give you the figures for banks outside New York City in the New York district. The net profits of banks with less than $500,000 deposits—that is the small banks—in 1941 were 4.8 percent of their capital accounts; in 1942, their net profits were 2 percent. The net profits of banks with deposits between $500,000 and $2,000,000 in 1941 were 5.7 percent of their capital accounts; in 1942 they were 4.3 percent. The net profits of banks with deposits from $2,000,000 to $5,000,000 were 5.2 percent for 1942 and 4.7 percent for 1941. Only the larger banks of over $20,000,000 increased their earnings from 4.5 percent on capital accounts to 5.4 percent.

Mr. PATMAN. But in that class of banks there are more than 100 people who receive very high salaries, some up to $175,000 a year, and it is hardly fair, to my way of thinking, to take money out of the Treasury to pay such huge salaries.

Mr. ECCLES. There is only one banker, I think, who has received such a salary; the salaries generally in banks nowhere approach the figure you name.

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Mr. PATMAN. There are 140 that receive $25,000 to $175,000.

Mr. ECCLES. The banks for which I gave the figures are outside of New York City, with deposits of over $20,000,000. The net profits of New York City banks with deposits over $100,000,000, dropped from 6 percent on their capital accounts in 1941 to 5.6 percent in 1942. The Minneapolis district shows a similar trend. The small banks, under $500,000 deposits, dropped from 9.7 percent in 1942 to 7.6 percent in 1941. The banks of from $500,000 to $2,000,000 deposits dropped from 11 percent to 9.3 percent.

I submit for your record the table of bank profits for the New York and Minneapolis districts which contains the figures which I have read.

(The table referred to is as follows:)

Bank profits, 1941 and 1942, selected groups of member banks

	Ratios of: Net profits to total capital accounts		Ratios of: Interest on loans to total earnings	
	1942	1941	1942	1941
New York City banks with deposits of—				
Over $100,000,000	5.6	6.0	32	34
Under $100,000,000	3.9	4.9	49	54
New York district banks outside New York City with deposits of—				
Over $20,000,000	5.4	4.5	40	44
$5,000,000 to $20,000,000	4.6	6.1	45	48
$2,000,000 to $5,000,000	4.9	5.2	47	51
$500,000 to $2,000,000	4.3	5.7	50	55
Under $500,000	2.0	4.8	55	61
Minneapolis district banks with deposits of—				
Over $10,000,000	8.1	8.3	43	44
$5,000,000 to $10,000,000	7.5	9.4	45	50
$2,000,000 to $5,000,000	7.9	8.6	44	48
$500,000 to $2,000,000	9.3	11.1	53	55
Under $500,000	7.6	9.7	57	60

NOTE.—Figures are averages of ratios for individual banks in each group. The averages are affected to some extent by shifts in some banks from the smaller to the larger groups between 1941 and 1942.

And I was looking this morning at the figures for the banks in Mr. Steagall's district, the Atlanta district. The smaller banks, as a rule, suffered a greater proportionate decline in net earnings than did the larger banks. The seven very small banks in the group having deposits up to $250,000, reported a decline of 52 percent in profits in 1942 as compared with 1941. The 42 banks that had deposits of over $10,000,000 reported a decrease of 13 percent in their profits for the same periods.

Now, it seems to me that the record of bank earnings for 1942 as compared with 1941 is not such that the Federal Reserve need to be concerned about profiteering on the part of the banking system. And your approach to this thing seems to me at the moment to be rather academic, and you will find me just as ready as anyone to stop profiteering by the banks when that time comes.

Mr. PATMAN. Is it very academic when we see facing us a 200 billion or 300 billion dollar debt?

Mr. ECCLES. You are assuming that the banks are going to own the greater part of that debt. It would be unfortunate if the banks should own the greater part of that debt, or a very substantial part of that debt. You will have such an inflation of bank costs and they will

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go up so high that it will take the increased interest from that debt to offset the increased cost.

What I would like to see considered is a much greater effort on the part of the Congress to provide revenue through taxation which will more nearly offset the sums that they appropriate to pay for the expenses. I would like to see this deficit cut to the bone and, what is left over, I would like to see the funds raised from the public. So far as I am concerned, I would like to avoid selling the banks $1 worth of Government securities and hold the situation as it is at the present time, insofar as the volume of funds already created by the banking system is concerned. So that I am not anxious to see the banks own a large part of the Government debt.

Mr. CRAWFORD. May I join you in that statement?

Mr. ECCLES. But we will have the banks creating money by the purchase of Government securities and, to the extent they have to, to that extent they are going to have to have the interest on the securities to offset the increased expense due to the inflationary development.

Mr. PATMAN. But you are getting the wrong people to pay the bill under the present system. When the banks buy bonds, this $5,000,000,000 worth of bonds you state they will have to buy in this coming campaign, they will of course receive interest on those bonds. Then when the amount is transferred to the individuals and corporations that the Government will pay the money to, the banks will continue to get the interest on the bonds. And if you are looking at it strictly from the standpoint of compensating the banks because that amount of currency or credit has been put in circulation, why should not the people who own it pay the cost of servicing it rather than the Government continuing to pay it for the next 100 years?

Mr. ECCLES. It involves the question of service charges.

Mr. PATMAN. They are going to be paid the service charges on it anyway.

Mr. ECCLES. Yes.

Mr. PATMAN. And now they are paid twice; they are paid one way by getting the Government interest, and paid the other way by getting the service charge.

Mr. ECCLES. Well, it would appear that the interest and service charges are not putting the banks in the class of profiteers.

Mr. PATMAN. Well, the fact remains that the entire capital stock of all the 13,500 banks amounts to about 3½ billion dollars.

Mr. ECCLES. Is that with surplus?

Mr. PATMAN. I concede that the surplus and undivided profits will run it up to about 6 billion 7 or 8 hundred million.

Mr. ECCLES. Better than 8 billion.

Mr. PATMAN. Anyway, the entire capital stock is 3½ billion. Now, you already have the Government in this position, which I consider is a position that cannot be justified, of encouraging the sale of bonds to the banks to the extent that by the end of the next fiscal year these banks that have a capital stock investment of 3½ billion dollars will be receiving from 1 to 2 billion dollars a year interest on the Government obligations they will then hold. Now that does not seem to make sense to me. I recall the Stevens Hotel was taken over by the Government recently because they said the rent charged would amount very soon to enough to pay for it, and it would be

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better for the Government to buy the hotel and pay for it in cash, rather than to have to pay such high interest charges.

So I am apprehensive that one of these days the banks will have so many Government bonds upon which they receive interest that there will be a clamor in this country, "Why pay the banks 3½ billion dollars a year interest when they only have 3½ billion invested in capital stock; why not take all of the banks over and save that 3½ billion a year interest?" I am in favor of the private banking system, of free enterprise, and I think the banks are doing something against themselves when they place themselves in that vulnerable position.

Mr. ECCLES. What would you suggest to take the place of the interest that these banks now receive on Government securities?

Mr. PATMAN. I would permit them to receive a certain amount that is reasonable, but I would have the date fixed and, if that was not satisfactory, I would fix another date.

Mr. ECCLES. Do you think the banks hold a reasonable amount of bonds at the present time, based upon this earning picture?

Mr. PATMAN. I have not examined the picture lately. I presume it runs from forty-five to fifty billion dollars—the amount of Government securities held by the banks; but I do not know; I have not looked into it.

Mr. ECCLES. The banks, including mutual savings banks——

Mr. PATMAN. Of course, they would not come in the category of the banks I have been discussing.

Mr. ECCLES. All right; just the member banks have 37 billion. This is as of the end of the year, the last figures, as of December 31, $37,546,000,000 direct and guaranteed securities of the Government. People all get the impression that the securities held by the banks all bear a rate of interest higher than is the fact——

Mr. PATMAN. Well, they have some bonds that bear rather high interest. Of course, I know the amount is limited.

Mr. ECCLES. Of that $37,000,000,000, a very large portion is represented by three-eighths of 1 percent Treasury bills, seven-eighths of 1 percent certificates, and Treasury notes that carry rates from 1 to 1¼ percent, or maybe some 1½. So that the amount of return to the banks on the Government debt is certainly not excessive.

Mr. PATMAN. You are talking about the short-term debt, but you know there will be a refinancing and these certificates will be refunded probably with long-term bonds drawing a much higher rate of interest.

Mr. ECCLES. I would not think that would be true unless there was an opportunity to place such refunded issues with the public. I think it is very desirable to have in the banks the short-term debt and not the long-term debt. The British development is a very interesting one. They agreed to pay the banks 1⅛ percent on a 9 months' security, and the British banks finance on that basis the British borrowing to the extent that it cannot be financed by taxes and by selling to the public, and that basis was arrived at or that rate was arrived at, so Mr. Keynes who was over here last year told me, because the banks needed about that much return to pay them for the services which they were rendering.

Mr. PATMAN. I want to ask you now about something else. It seems like we will not be in agreement on this thing, and I think I know your views and you know mine.

Mr. SMITH. May I get some more figures in here just on this point?

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Mr. PATMAN. I will be through in just a minute, if Mr. Eccles won't take so much time to answer questions that do not require such extended answers. I think I will give up at this point in the record any further questioning along that line with this understanding, Mr. Chairman, that I may place in these hearings my testimony and Senator Owens' testimony and Congressman Voorhis' testimony before the Ways and Means Committee, also some other excerpts, and I ask unanimous consent that I may do that.

Mr. SPENCE (presiding). Without objection, that may be done.

Mr. PATMAN. Mr. Chairman, I am inserting herewith my testimony, the testimony of the Honorable Robert L. Owen, and the testimony of the Honorable Jerry Voorhis before the Ways and Means Committee of the House of Representatives, February 13, 1943, on H. R. 1470, a bill to increase the debt limit of the United States.

This testimony, I believe, is convincing that billions of dollars a year can be saved the taxpayers if Congress will prevent the payment of unearned interest to finance the war. Further, that if the debt is financed like we advocate, the entire national debt can be paid in 40 years.

The testimony is as follows:

STATEMENT OF HON. WRIGHT PATMAN, A REPRESENTATIVE IN CONGRESS FROM THE STATE OF TEXAS BEFORE THE COMMITTEE ON WAYS AND MEANS, HOUSE OF REPRESENTATIVES, FEBRUARY 13, 1943

Mr. PATMAN. My name is Wright Patman, Member of Congress from the First Congressional District, Texas.

In the beginning I want to express my appreciation to this committee for giving consideration to this subject. I know it is a controversial subject, but I have studied it for 25 years, 10 years before I ever made any public declaration on it. I was very anxious to seek the best advice from the best experts in this Nation before I ever made any public declaration on this subject.

Our public debt by the end of the next fiscal year will be about $210,000,000,000. A large part of this debt, if present plans are not changed, will be owned by the 14,000 commercial banks in the Nation. The interest burden on this debt will be between four and five billion dollars per annum. The interest burden this fiscal year will be $3,000,000,000, which is provided for in the Budget message submitted by the President at the beginning of this session of Congress.

The net increase in the public debt for the year ending June 30, 1944, will be $75,500,000,000.

HOW LARGE PART OF INTEREST CAN BE SAVED

The occasion of my appearance before this committee is to make a suggestion about how billions of dollars a year can be saved by the Government on this huge national debt. Our interest burden after the next fiscal year will be much larger than the entire expenditures of our Government in 1933 and more than four times as large as the total expenditures of our Government in 1914. The question of interest, therefore, becomes one of our major problems. If a substantial part of this interest can be saved it will be of great help to the already over-burdened taxpayers. If the plan had been in effect in

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the past our Government would have been saved at least one-half the interest burden, which would have amounted, over a period of years, to billions of dollars.

It is my considered opinion that not only can a large part—in fact, the greater part—of this interest burden be saved but the method pursued in saving it will enable our Government to pay the entire national debt in 40 years even if it should reach $300,000,000,000 before this was is over. In addition, the plan proposed will retire a definite amount of the debt each year, thereby reducing annually any inflationary condition that has been brought about because of the war, and more effectively retard inflation than the present system.

Inflation is our greatest danger. Monetary controls cannot stop it; only adequate price control can retard or prevent it. It must be prevented or our country will suffer a shock almost equal to losing the war to the dictators.

My plan is no different from present plans and methods except that no interest will be paid by the Government for a large part of its credit used to finance the war.

I am opposed to the Government owning the commercial banks. Those banks render a good service and are entitled to a fair profit. My advocacy of this proposal is in favor of the private banks and to help them remain private. This is no fight against bankers. They are doing a splendid, patriotic job in the war effort and they are among the finest and best citizens in every community. If it is necessary for the Government to assist the private banks in order to keep them performing efficiently, I am in favor of it.

For the first 125 years of our country's existence the question of interest paid by our Government was of only minor importance. For the past 25 years, however, our Government's interest burden has exceeded on an average more than a billion dollars a year.

Anyone is entitled to pay for hire of his money. When people dug gold and silver out of the earth, it was right, if they loaned it to the Government to get interest on it.

ROAD TO RUIN

We should not permit the war burden to be doubled and trebled through the payment of unnecessary interest. It will be traveling the road to ruin.

The Treasury is spending monthly:[1]

Currently: $6,000,000,000 for a war, a half billion for other purposes.

End of 1943: $8,000,000,000 for war, a half billion for other purposes.

End of 1943: $8,000,000,000 for a war, a half billion for other purposes.

Fiscal yearly total spending:[1]

Ending June 30, 1943: $74,000,000,000 for war, $6,500,000,000 for other purposes.

Ending June 30, 1944: $97,000,000,000 for war, $7,000,000,000 for other purposes.

Gross public debt[1]

Dec. 31, 1941	$57,900,000,000
Dec. 31, 1942	108,200,000,000
June 30, 1943	134,800,000,000
June 30, 1944	210,500,000,000

[1] Information from Banking. Journal of the American Bankers Association for February 1943, p. 24.

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Possible banking-system balance—sheet as of June 30, 1944[1]

Resources:	
Cash and reserves	$20,000,000
Government securities, direct and guaranteed	112,000,000,000
Other investments	8,000,000,000
War loans	8,000,000,000
Other loans	12,000,000,000
Total	160,000,000,000
Liabilities:	
Deposits	152,000,000,000
Capital	8,000,000,000
Total	160,000,000,000

[1] Information from Banking, Journal of the American Bankers Association for February 1943, p. 24.

It will be noticed that the banks are expecting to hold $112,000,000,000 of the Government's securities by the end of 1944, which will be more than one-half of the entire public debt. The annual interest on this amount, which must be paid by the taxpayer, will be approximately $2,500,000,000. The Stevens Hotel in Chicago was purchased by the Goveriment because the annual rent to be paid would soon equal the purchase price.

In connection with the question of how much of the increased debt for this year will have to be purchased by the banks, I desire to quote the chairman of the board of directors of the Chase National Bank of New York, Winthrop W. Aldrich, in a speech he made Thursday, January 21, 1943, in which he stated:

> Through 1943, it is estimated that the commercial banking system, that is, all commercial banks plus the 12 Federal Reserve banks, may have to absorb $40,000,000,000 of Government obligations, an amount equal to about 60 percent of the estimated increase in the total Federal debt.

BANKS IN VULNERABLE ATTITUDE

The Bank of America statement of condition, December 31, 1942, discloses that it owns $1,043,000,000 of the United States Government's securities and has a capital stock of $50,000,000. In other words, this bank will collect as much in interest on these bonds in 2 years as the amount of the entire capital stock of the bank.

The statement of one bank of New York for December 31, 1942, discloses that it had in its portfolio Government obligations amounting to $1,988,096,539.18. The capital stock of this bank is $77,500,000. The interest received on the Government obligations in 2 years would be much more than the capital stock of the bank.

The statement of another New York bank for December 31, 1942, discloses that it had in Government obligations at that time $1,692,372,867.88. The capital stock of the bank is $90,000,000.

ONE-HALF ALL FEDERAL SOCIAL SECURITY BENEFITS

January 9, 1943, it was reported that the 12 largest banks in New York City, as of December 31, 1942, held $11,182,594,000 worth of United States Government interest-bearing securities. These 12 New York banks will therefore collect approximately a quarter of a billion dollars a year interest each year from the Government on these securities. This amount is equal to about half of the Federal Government's total expenditures for social security. Ten times as much

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as the cost of the legislative department of our Government in a year.

It was reported January 20, 1943, that the 20 largest banks in the United States, 12 of them being in New York City, held Government bonds at the end of 1942 amounting to $16,407,197,000. The interest that the Government will pay to these 20 banks will be between three hundred and four hundred million dollars per year.

The total capital stock of all the commercial banks amounts to $3,500,000,000, although their surpluses and undivided profits amount to about $5,000,000,000 more. When these banks own enough Government bonds to entitle them to $3,500,000,000 a year, what do you think will happen?

ALL RIGHT TO PAY INTEREST ON ACTUAL MONEY HIRED

In the beginning, may I make it plain that I am not opposed to interest being paid by individuals or corporations for the use of other people's money that they have hired. Neither am I opposed to the payment of interest by States, counties, and political subdivisions for money that they hire. I am opposed to the United States Government, which possesses the sovereign and exclusive privilege of creating money, paying private bankers for the use of its own money. These private bankers do not hire their own money to the Government; they hire only the Government's money to the Government, and collect an interest charge annually.

What I am telling you I can prove by the highest authorities in the world. Over a period of years I have interrogated Mr. Eccles, Mr. Morgenthau, Mr. Bell, and the biggest bankers in this country and I know what their claims and contentions are, and what I say is there is no dispute or contention about it, or controversy; it is admitted. And, furthermore, I have, I believe, the best authority in the world on financial matters to support this statement. I don't want to take too much time, because I want you to hear from him. There are more words of Senator Robert L. Owen in the Federal Reserve Bank Act than the words of any other person, living or dead. Senator Owen is one of the most highly cultured men in the world. I feel like he knows more about this problem than any other person living. I know he is a modest man; he has not tried to put himself forward, but I feel, because of his attitude back in 1913, when the Federal Reserve Act was being written, his attitude was not favorable to certain powerful interests and it is the same today as it was then, and by reason of that unfavorable attitude on the part of some of the biggest fellows in the country they have submerged the part this great man had in the writing of that history-making legislation. Few men in the world have had the ripe experience and the successful experience that Senator Owen has had. He is a successful national banker himself. He organized a bank in 1890, owns a substantial part of the stock, was president for a long time, has been an official or director ever since, and he knows what this is all about.

Incidentally, it is a coincidence that Senator Owen, who was chairman of the Banking and Currency Committee in the Senate at the time of the passage of the Federal Reserve Act, and Senator Glass, who was chairman of the Committee on Banking and Currency in the House, when the Federal Reserve Act was passed, were both born about the same time within two blocks of each other, in Lynchburg, Va.

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The CHAIRMAN. May I interrupt to ask a question there?

Mr. PATMAN. Yes, sir.

The CHAIRMAN. You know that Senator Owen and Senator Glass were the authors of the Federal Reserve System?

Mr. PATMAN. Yes, sir.

The CHAIRMAN. Both played a conspicuous part in the writing of that act.

Mr. PATMAN. Yes.

The CHAIRMAN. Did you get Senator Glass' reaction to this proposal?

Mr. PATMAN. I only know how Senator Glass stood when the Federal Reserve Act passed, and his views were contrary, in many substantial respects, to Senator Owen's. I know his views since that time, and I would consider he would definitely be very much against it.

The CHAIRMAN. He would?

Mr. PATMAN. Yes, sir. I know his views. I am not arguing with him, or criticizing him or condemning him. I am just telling you I believe that would be his views. I know how he stood in the past on these difficult questions.

INTEREST CAN BE SAVED ON PART OF WAR DEBT

Furthermore, in this emergency it is necessary that we sell all the interest-bearing bonds that we can to the public, including corporations who have the money to buy them. This is necessary to retard inflation and it is very helpful to that end. I favor the levying and collection of all the taxes it is possible for the people to pay in order to reduce the national debt as much as possible each year. After the Government has collected all the taxes it can collect and has sold all the bonds to the public that can be sold, there will remain 50 percent or more of the funds to be raised which must be obtained from the Federal Reserve banks or the privately owned 14,000 commercial banks of the country, that accept deposits, or from both.

It is this money that must be obtained from the Federal Reserve banks and the commercial banks that I insist can be secured by the Government without an annual interest charge.

Mr. DISNEY. Congressman, if you will restate your proposal in just a word, it would help me.

Mr. PATMAN. The point is this; we want to sell all the bonds we can to the public and corporations that have the money to buy them. And I am not opposed to that. We want to collect all the taxes we can to pay on this war. But after we do that, we will still have to have a large sum of money each year, and that money must be obtained through creation; it has got to be created. And my point is that the money, if it has got to be created on the Government's credit, that the people should not have to pay interest on that money that is so created. That is it in a nutshell, Mr. Disney.

H. R. 1 GERMANE TO BILL TO RAISE DEBT LIMIT—THAT IT PROVIDES

I have before this Congress the bill H. R. 1. It is germane in the consideration of this bill to raise the debt limit to $210,000,000,000. The bill provides for the issuance of non-interest-bearing, non-negotiable bonds by the 12 Federal Reserve banks to finance the part of

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the war that would otherwise be financed by the commercial banks and the 12 Federal Reserve banks on interest-bearing bonds.

The bill would prohibit the Treasury from issuing any further interest-bearing bonds to the banks receiving deposits, and would restrict the amount of United States bonds held by any bank to the amount held by such bank on December 31, 1941. The date is an arbitrary one. Any other fair date or fair adjustment of the amount of bonds any bank could hold would be satisfactory.

FEDERAL RESERVE BANKS DISTINGUISHED FROM COMMERCIAL BANKS

First, let us get our definition straight as to the kind of banks that I speak of. The 12 Federal Reserve banks are owned by the private commercial banks of the country. Not one penny of stock in these 12 banks is owned by the United States Government or by the people. The total stock in these 12 banks is about $150,000,000.

The 14,000 commercial banks include not only the national banks and the State banks that belong to the Federal Reserve System, but also the other banks which accept deposits which are State banks and do not belong to the Federal Reserve System, but practically all of them are insured by the Federal Deposit Insurance Corporation.

NO INTEREST SHOULD BE PAID ON LARGE PART

The money that must be secured by our Government after all the bonds have been sold to the public that can be sold, and all the taxes have been paid that can be collected without injuring our domestic economy, can be secured without an interest charge through the use of the 12 Federal Reserve banks. It is right that the Government use the banks for this purpose, because these 12 banks, although privately owned, operate exclusively upon Government credit. These 12 banks have the power to create the money that is placed in circulation and used by the people. Congress has farmed out to them this great privilege. It is the most valuable privilege any government on earth ever delegated or conveyed to an individual group or corporation.

POWER NOT DISPUTED

The sovereign power of Congress to authorize the program that is proposed in the bill I am discussing is beyond question. No one questions the power of Congress to do what I propose.

SIMPLICITY AND SOUNDNESS OF PLAN

In order to demonstrate the simplicity, desirability, and soundness of the plan, I desire to first analyze the status of the present national debt. It will not be my purpose to quote exact figures since exactness is not required for the purpose of this illustration. Let us assume that the national debt now is a round number—$100,000,000,000 which is very close to the actual amount. One-half of the amount is held by individuals and corporations, including mutual-savings banks and life-insurance companies which had the money to lend to the Government in exchange for interest-bearing bonds. The other $50,000,000,000 is held as follows:

Forty-four billion by the private commercial banks which created the money by a flick of the pen to purchase interest-bearing bonds from the Government and which they now hold.

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Six billion has been purchased by the 12 Federal Reserve banks by creating it by a flick of the pen, and is now held by these 12 Federal Reserve banks, and the Government will continue to pay interest on it just the same as if the bonds had not been purchased through the use of the Government's credit.

CREATING MONEY IS ACKNOWLEDGED

For fear that someone will think that I am using a very radical and unorthodox word when I say "create" in connection with the banks' creating money with which to buy Government bonds, I want you to know that the highest and best authorities in our Government and in the United States agree that the commercial banks and the Federal Reserve banks actually create money on the Government's credit in order to buy United States Government bonds. There is no dispute about that question. The Honorable Henry Morgenthau, Secretary of the Treasury, admits it. So does the Honorable Marriner S. Eccles, Chairman of the Board of Governors of the Federal Reserve System, and all other informed people.

Therefore, the main point for consideration by this committee is whether or not the 12 Federal Reserve banks and the private commercial banks that create money on the Government's credit, should continue this policy and thereby cause the taxpayers to pay interest on it for generations to come.

HOW GOVERNMENT OBTAINS MONEY NOW

Under the present system if the Government desires more money and it is necessary to borrow the money from the banks, the following procedure is adopted:

First. If it desires, the Treasury can deliver bonds to the 12 Federal Reserve banks directly and receive credit for the amount of the bonds on the books of the 12 Federal Reserve banks. Then as the Treasury pays its debts, checks are given on these 12 Federal Reserve banks and the funds are transferred from the Treasury to the ones receiving the checks. In this way the Government is paying interest to the Federal Reserve banks just the same as it pays interest to the private banks and to individuals, although the Federal Reserve banks operate on the Government's credit. If the receiver of a Treasury check in a case like this desires the money instead of credit in his local bank, he is given Federal Reserve notes. These notes are not obligations of the Federal Reserve banks, they are obligations of the United States Government. Therefore, the Government and Congress, particularly, finds itself in the idiotic position of permitting the Treasury to deliver one form of Government obligation—interest-bearing notes—to the privately owned Federal Reserve banks and receiving credit therefor, and then when the Federal Reserve banks are called upon for the money they issue another form of Government obligation, Federal Reserve notes, to satisfy the demand. In each case Government obligations are used. The net result is that the taxpayers are paying for the use of their own credit.

This power of selling bonds directly to the Federal Reserve banks by the Treasury is authorized by the Second War Powers Act which became a law March 27, 1942, and can only be used to the extent of $5,000,000,000. The question is, if it is good money up to $5,000,000,000 why is it not good money up to $100,000,000,000? However, this

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does not stop the Federal Reserve banks from buying $100,000,000,000 or $200,000,000,000 of Government bonds in the open market through the Open Market Committee in New York. The restriction of $5,000,000,000 is only on a direct sale from the Treasury to the Federal Reserve banks.

Second. The other way the Treasury would obtain the money would be to sell interest-bearing bonds of the Government to the 14,000 commercial banks. In a sale of that kind a commercial bank receives the Government bond and gives the Treasury credit upon its books for the amount of the bond. Then when the Government pays its bills it gives checks upon this fund in the local commercial bank. The money has been created by a bookkeeping transaction and it is seldom that the one receiving a check from the Government wants the actual money but desires instead credit at the bank. In that way the money is created on the books of the bank but the actual money is not paid out except to a very limited extent. If the one receiving the check, however, desires the actual money and the local bank does not have the money to pay the check, the local bank can obtain it from the nearest Federal Reserve bank by depositing Government bonds as collateral security. The bank will pay the Federal Reserve bank one-half of 1 percent interest on this money. The Federal Reserve bank will pay the Government 30 cents per $1,000 for the money. The net result is that the Government has not gotten anything for the sale of bonds to the public and the collection of taxes, that the United States Treasury deliver to the Federal Reserve banks non-interest-bearing, nonnegotiable Government securities or certificates of indebtedness and obtain from the 12 Federal Reserve banks credit for the amount of the bonds or certificates. Then as the Treasury pays its debts checks will be given on these 12 Federal Reserve banks in the same way and manner as if the bonds were interest-bearing. The ones receiving the checks will receive their money and the same kind of money and in the same way and manner as if the bonds were interest-bearing. The result will be, however, that the Government will be saved interest. In this way the Government can pay each year 2½ percent to the Federal Reserve banks on these bonds or certificates and in 40 years the entire debt will be liquidated, whereas under the present plan our Government can pay 2½ percent each year for 40 years as interest and none of the principal of the debt will be paid but all of the debt will still be due at the end of the 40 years.

Mr. DEWEY. May I query the witness at that point on just that use of currency?

The CHAIRMAN. Yes; go ahead.

Mr. DEWEY. Why did not the Government do that in 1907 and 1912, when there was a money panic, before the organization of the Federal Reserve System, and the country went to clearing-house certificates and there wasn't any currency to go around? They had to go to the only thing that existed at that time, which was the clearing house, and they issued real fiat money to take care of the requirements of trade and industry. As the result of that we put in a system known as the Federal Reserve System, which would supply cash and take it off the market when not needed. The Bureau of Engraving and Printing was in existence then. Why didn't the Government go to the Bureau and buy some of this 30-cents-a-thousand currency and just put it out in the country?

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Mr. PATMAN. Of course, the gentleman would not seriously insist that I attempt to answer that question. I was only 14 years old at that time.

Mr. DEWEY. Well, that is what you want to have done now, Mr. Patman.

Mr. PATMAN. I don't know what was in the minds of the people who were in charge of our Government at that time. Of course, I know about the clearing-house certificates from reading the history of the 1907 panic, and I well remember it, because it hit us awfully hard in Texas, and we all suffered from the depression down there. I know they used the certificates, but as to why they didn't resort to other means—there are other means that could have been resorted to. This would not be the only one.

Mr. DEWEY. They did resort to other means, by organizing the Federal Reserve System.

Mr. PATMAN. And remember this, Mr. Dewey, that up until 1917 we had never paid any interest hardly on our national debt, only two or three million a year over a period of 125 years.

Mr. DEWEY. We didn't have any national debt.

Mr. PATMAN. Our interest burden has really not been sufficient to attract our attention except during the last 25 years, and for that reason only should a plan like this be considered.

Mr. DEWEY. We didn't have any national debt.

Mr. PATMAN. That is right; we didn't have any national debt. It was very small. But I cannot answer the question as to why people, 35 years ago, did not do so and so, because I have no way of determining it. But I know one thing; their failure to do it is not sufficient to justify us in ignoring it. I am not willing to ignore a good proposition now because it was not adopted 35 years ago.

The CHAIRMAN. One question right there. You mentioned this money that the Bureau of Engraving and Printing gets out, and all the Government gets for it is the cost of the printing.

Mr. PATMAN. Yes, sir.

The CHAIRMAN. You say the Government gets nothing for its credit. The Government isn't out anything.

Mr. PATMAN. It is out its credit. It signed a mortgage; it is behind it. It has pledged all the resources of this Nation to back it up.

The CHAIRMAN. Doesn't it give what Senator Owen and Senator Glass were after, a sound system of banking?

Mr. PATMAN. Certainly.

The CHAIRMAN. That is getting something.

Mr. PATMAN. Certainly; it is a sound system of banking.

The CHAIRMAN. It is put on a national basis.

Mr. PATMAN. That is right.

The CHAIRMAN. And, of course, that was the trouble before. The banks could not get the money. There was no Federal agency, and no means by which they could get money. This provides a sound system of banking; isn't that right?

Mr. PATMAN. Sure; it is a very fine system. I am not opposed to it; I am for it, but in an unusual case like this, why should we burden the taxpayers on a $300,000,000,000 debt, when we know they will never be able to pay more than just the interest on it? That means a perpetual debt of $300,000,000,000. That means that any inflation

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that we have in that $300,000,000,000 will remain indefinitely, whereas if you adopt a plan of saving the interest on a substantial part of that money, you can reduce it each year by as much at least as you would pay in interest, and then you reduce the inflationary condition each year instead of having it remain the same each year.

The CHAIRMAN. I haven't any disposition to argue with you. I may agree with you when you get through; I don't know. But if the banks were not to get any interest on this money that the Government borrows, how would you get the banks to lend the money? They say, "It is the money of our depositors; we are responsible for it, and if we don't get anything for the use of it we will just not buy the bonds."

Mr. PATMAN. I don't think that question is involved in this at all.

The CHAIRMAN. I don't know why it wouldn't be involved. They won't furnish the money if they're not going to get any interest on it.

Mr. PATMAN. I am not proposing that. I am proposing that the 12 Federal Reserve banks furnish it, not the commercial banks.

The CHAIRMAN. Suppose the Federal Reserve banks balk?

Mr. PATMAN. They can't balk. They are an agency of the Congress. They have to do what Congress says.

The CHAIRMAN. These bonds can't all be held by the Federal Reserve banks; they have to be scattered throughout the country.

Mr. PATMAN. I am afraid we are talking about different things. I am afraid you are talking about the usual industrial or commercial transaction, and I am talking about the Government finances.

The CHAIRMAN. I beg your pardon. I am sorry; I didn't follow you.

Mr. DISNEY. As I understand it, these banks are heavily loaded with Government bonds, so heavily loaded that a sharp decrease in the value of Government bonds would wipe out their capital stock.

Mr. PATMAN. Two or three points decrease would wipe out their capital stock, but there is no danger of that.

Mr. DISNEY. Suppose there was a sharp decrease in the value of Government bonds, that would have a tendency to wipe out a part of the capital stock of the banks, or some of them, and if any sizeable number of them should get in that position, they would be liable to be in trouble and go broke and take the rest of the banks with them. How could we prevent that?

Mr. PATMAN. That is already provided for, Mr. Disney. The Open Markets Committee, which, by the way, has been moved from Washington to New York, has already arranged that any bank in distress can get a hundred cents on the dollar on its bonds any time. There is where the Government's credit comes into play again. They just issue more Federal Reserve notes to buy those bonds, and they are not going to let the banks suffer. They have already told them they will not let them suffer. There is no danger of that at all.

Mr. DISNEY. No danger of Government bonds——

Mr. PATMAN. Declining; absolutely not. It is, in effect, guaranteed by the United States, and there is no danger in the world. In fact, I think it is a good thing, although it is the Government's credit being used again, free. It is perfectly all right.

Mr. KNUTSON. Right at that point, why did Government bonds drop to 82, along in the fall of 1921?

Mr. PATMAN. Becase of a situation you gentlemen had vision enough to guard against when this war started. In 1914, when the war started

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in Europe, and in 1917, when we became engaged in the war, we did not make any provision to protect the people who bought United States Government bonds. They had to sell them in the open market. Consequently, when the war was over, and every one wanted to sell their bonds, naturally the market went down and down, and some of them sold as low as 75 cents on the dollar. It was the crime of the age to permit that to be done. Men in the armed services had paid for their bonds a few dollars a month over a period of time. And when they came out of the service they saw these bond manipulators force the price down to 75. It was absolutely a crime. But you gentlemen provided—and if you will remember, I appeared before this committee in connection with that and invited your attention to it, and asked you, for God's sake, to prevent any such thing happening in the future. Not necessarily because of my testimony did you do it, but you provided, anyway, that now they can get their money 100 cents on the dollar, and the people of this Nation should appreciate what this committee did to initiate that type of legislation which will protect them against that awful crime that happened after the other war.

There is one objection to this plan. Mr. Chairman, not a serious objection, not one that you cannot correct, but it is, I am afraid, an objection.

The CHAIRMAN. Which plan are you talking about?

Mr. PATMAN. This plan I am proposing now.

OBJECTION WORTHY OF CONSIDERATION

One objection is urged against this plan which I think is worthy of the greatest consideration. It is that if the commercial banks buy the bonds a part of the excess reserves of the bank will be used in the transaction, but if the Federal Reserve banks buy the bonds and the money is paid out into the country, it is deposited in the local banks and the excess reserves of the local banks are increased by that much, which will be more inflationary than the sale of the bonds to the local banks.

This objection can be overcome completely by permitting the Board of Governors of the Federal Reserve banks to change the reserve requirements of the local banks. In other words, use the same system to contract the reserves of the local banks that is now being used to expand the reserves of the local banks. Mr. Eccles has testified that the objection can be cured that way.

That is the only real objection that has ever been urged to this plan and upon analysis it becomes an excuse rather than a reason for not approving the plan that will save the taxpayers such enormous sums of money annually.

The CHAIRMAN. Where would the banks get the additional reserve? They can't call in their loans very well. If they did, they would wreck the country. It would embarrass the parties to whom they made loans. Where would they get this extra reserve? I am not trying to argue. If they have to increase their reserves, where would they get the increase?

Mr. PATMAN. I will be glad to answer the gentleman's question. If this plan is adopted and we sell a million dollars' worth of bonds, it will require the Federal Reserve to take a million dollars of bonds

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that are not interest bearing, and nobody doubts the power of Congress to do that. They all admit it. Raleigh, I guess, is your Federal Reserve bank, is it not?

The CHAIRMAN. No; Charlotte.

Mr. PATMAN. All right; at Charlotte there is a credit of $1,000,000. When they pay the Postmaster and the rural carriers and the Honorable Bob Doughton their salaries, they will take their checks to the local bank, a commercial bank, and deposit them, and the local commercial bank can use those deposits as excess reserves and purchase any kind of paper, 5, 8, or 10 times as much as that, depending on what the reserve requirements are at that time. I will admit that that will cause an inflationary condition, but you can correct it by changing the reserve requirements of that bank so that it could not lend more than 2 to 1, or 3 to 1, or more than $1 for one—100 percent reserves. Mr. Eccles suggested that before the Banking and Currency Committee. That would completely stop the inflationary condition and save interest.

The CHAIRMAN. Do you think a bank could live and pay its stockholders any dividends if it were forced to keep such large reserves? They couldn't make any money.

Mr. PATMAN. Oh, they would make money. I provide in this bill that they shall be allowed to take and hold a reasonable amount of bonds. Let them have enough bonds to live and render the fine service they are now rendering, but not let them have unlimited bonds on the Government credit in an unusual critical situation like we are in now, where the war debt must be increased by hundreds of billions. That is just going too far. But I provide in this bill, Mr. Doughton, that they may have as many bonds as they had December 31, 1941, and they had a pretty good supply of bonds.

The CHAIRMAN. How would they get those bonds?

Mr. PATMAN. They could buy them in the open market, or directly from the Treasury.

The CHAIRMAN. Wouldn't they have to draw on their reserves to buy them?

Mr. PATMAN. That would be all right.

The CHAIRMAN. Wouldn't that cut their reserves down? How could you go on the market and buy bonds, and at the same time hold up your reserves?

Mr. PATMAN. I respectfully submit that is no problem in this plan.

The CHAIRMAN. That is not the question I asked. You say they have to have a reserve, and they go into the open market and buy bonds. I say they can't go into the market without reserves.

Mr. PATMAN. They have the money.

The CHAIRMAN. They can't have the bonds and the reserves both. You know that.

Mr. PATMAN. They have plenty of reserves, Mr. Doughton, and I would be in favor of having plenty of reserves. If they want more reserves, they could sell a million dollars' worth of bonds to the open-market committee and get a million dollars in Federal Reserve notes, and then buy $10,000,000 of United States Government bonds. They will have no trouble in getting reserves.

The CHAIRMAN. Would they be interest-bearing or non-interest-bearing?

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Mr. PATMAN. They would be interest-bearing. There is no trouble about reserves. That could be changed up or down, and I am presenting in my testimony here, which I will not take the time to read, evidence along that line.

The CHAIRMAN. Let me see if I understand it. The bonds that the Federal Reserve banks hold would bear no interest, but the bonds that the commercial banks hold would bear interest.

Mr. PATMAN. Yes; you see the commercial banks are entitled to a profit.

The CHAIRMAN. What percentage of the total loan now outstanding would the Federal Reserve have and what percentage would the commercial banks have?

Mr. PATMAN. That depends on how much we spend in the war and on how much the public will buy and the insurance companies and other corporations that have money to buy the bonds with; and, in addition, how much money can be collected in taxes to retire part of it.

The CHAIRMAN. If they bought them all, then you wouldn't have to get any loans from the Federal Reserve?

Mr. PATMAN. I would love to see it that way. If the public and the life-insurance companies and the other people having money would buy it, that is the way to do it. But it will not work, Mr. Chairman; we know it will not work. They don't have the money. It has to be created; so, since it has to be created, should we always pay interest on that part?

The CHAIRMAN. How much do you save—say on $200,000,000,000, how much do you estimate the Federal Reserve banks would hold on which there would be no interest paid?

Mr. PATMAN. I estimate 50 billion, something like that.

The CHAIRMAN. That is one-quarter.

Mr. PATMAN. Yes; but if you save a quarter of $4,000,000,000 a year and you have saved $1,000,000,000, and after this war is over, my dear sir, and when we have industrial activity then the banks will want to unload these bonds, individuals will want to sell their bonds, and money will have to be created in order to take care of them. Then the Federal Reserve could save more money—I am not trying to hurt the commercial banks, but the chairman of this committee knows——

The CHAIRMAN. How would this money to take up all these bonds be created?

Mr. PATMAN. In the same way and manner it is now created, by just a flick of the pen, if you want to call it that. That is the power of the Federal Reserve banks, to create money. They are doing it to the amount of $5,000,000,000 now by direct purchases.

The CHAIRMAN. Would it be logical to just create money that way now?

Mr. PATMAN. No, because you would have unlimited inflation, ruinous inflation. I don't want to do that. I would love to sell all the bonds to the public and the corporations having the money to buy, but we cannot sell the bonds that way. The people do not have the money and we have got to create it. I don't want the taxpayers of this Nation to pay interest for the next two or three hundred years. That is the point I am trying to make—just the part that must be created anyway, on the credit of the Government.

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The CHAIRMAN. Why not create that independent of the Federal Reserve banks; just leave them entirely out of it?

Mr. PATMAN. Well, that is the best way to do it, I think. You wouldn't have any control otherwise. You have got to have a simple, desirable plan that is sound. I think that is the soundest way to buy them. But it is impossible to sell enough bonds to the public.

Mr. DISNEY. You mean through the Federal Reserve?

Mr. PATMAN. The Federal Reserve. All the bankers tell you that they shouldn't buy these bonds. They know it is highly inflationary. The bankers are patriotic people; they spend their own money to get the public to buy them and they are doing their best to get the public to buy them. But it is impossible to sell enough bonds to the public to finance this war, and a large part of it must be created, and I say the part that must be created on the Government's credit, the Government should not pay interest on.

Let me read you just a few questions and answers, from Mr. Eccles's testimony in 1941, before the Banking and Currency Committee. I am interrogating:

> Mr. PATMAN. The stock is less than $140,000,000 and you do several hundred billion dollars' worth of business a year sometimes, and furthermore, when you actually hold and claim now over $2,000,000,000 in Government securities which you claim you bought. How did you get the money to buy those $2,000,000,000 of Government securities?
>
> Mr. ECCLES. We created it.
>
> Mr. PATMAN. Out of what?
>
> Mr. ECCLES. Out of the right to issue credit, money.
>
> Mr. PATMAN. And there is nothing behind it, is there, except the Government's credit?
>
> Mr. ECCLES. We have the Government bonds.
>
> Mr. PATMAN. That's right, the Government's credit.
>
> Mr. ECCLES. That is what your money system is.

There is the highest authority in the Federal Reserve bank. There is no question about this, gentlemen. There is no dispute about what I am saying. You will not find a witness who will deny what I say. It is undisputed. There is no controversy about it.

Mr. KNUTSON. Does Mr. Eccles endorse your plan?

Mr. PATMAN. Oh, I am sure he wouldn't, because he believes there should be interest paid on all Government bonds. He is opposed to starting any other system. He don't want a change. Ordinarily, that may be right, but when you have such an unusual condition, when our national debt will be 10 times as high as it has ever been in the history of our country, don't you think we should consider any plan that might save the taxpayers money?

Mr. DEWEY. Mr. Patman, you want to create some more money, or funds for the Government in these wartimes. We have been hearing a great deal about this inflationary gap.

Mr. PATMAN. Yes, sir.

Mr. DEWEY. Which is the excess funds in the hands of the public which may come into competition for a large amount of commodities.

Mr. PATMAN. Yes, sir.

Mr. DEWEY. For that reason we are considering increasing the tax bill and enforced savings.

Mr. PATMAN. That is right.

Mr. DEWEY. You want to create more.

Mr. PATMAN. No.

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Mr. DEWEY. Why not exhaust that excess spending power of the public before creating new money?

Mr. PATMAN. That is perfectly all right, my dear sir. If you could get the money to finance this war by selling bonds to the public who have the money to buy them, and through the collection of taxes, such as you propose, or in any other way, I am for it. But——

Mr. DEWEY (interposing). It is understood——

Mr. PATMAN. Let me finish. But we have demonstrated we cannot sell enough bonds to the public, we cannot levy enough taxes to balance our expenditures in this war and the difference, my dear sir, has got to be created money on the Government's credit, and my point is what we create on the Government's credit we should not pay interest on for the next two or three hundred years.

Mr. DEWEY. What percentage of the debt was carried by the banks during the last war?

Mr. PATMAN. I don't know, but the last war was merely a fist fight compared to this one, so far as expenditures are concerned.

Mr. DEWEY. In proportion to the national income, the Government bonds sold in the last war was a very small percentage. We sold most of the bonds to the public and I don't see why we couldn't do it this time.

Mr. PATMAN. Well, we can't do it, because the Government knows the people do not have the money.

Mr. DEWEY. We just agreed that the public is in possession of that inflationary gap. That has been brought out by every person that has testified here, from Treasury officials on down.

Mr. PATMAN. Let me read a little more of the testimony of Mr. Eccles, in answer to questions asked him by Mr. Dewey. I have had an awful time getting these things, Mr. Chairman. The witnesses have shown irritation, sometimes, in being compelled to answer questions, but over a period of years I have gotten the Secretary of the Treasury, Mr. Morgenthau, the Under Secretary, Mr. Bell, and Mr. Eccles and other high officials of the Government to prove every statement that I make concerning this. I mean not my own opinions or conclusions, but statements of fact. I have other testimony to prove it. Let me read Mr. Eccles' testimony when he was interrogated by Mr. Dewey on June 17, 1942 (reading):

Mr. ECCLES. No; the Federal Reserve would buy in the open market. If the Federal Reserve then bought a billion dollars of securities in the open market that would be new Treasury issues. The banks would still hold them, and the Federal Reserve would put into the banks another billion of excess reserves. If they used that billion they could buy 5 billion more of Governments, and you could keep the price up. For every billion of the Federal Reserve banks put in the open market operations, the private banks could buy 5 billion.

Mr. DEWEY. That comes pretty close to some other ideas I have heard.

Mr. ECCLES. I mean they could buy 10 billion. I mean the Federal Reserve when it carries out an open market operation, that is, if it purchases Government securities in the open market, it puts new money into the banks which creates idle deposits.

Mr. DEWEY. There are no excess reserves to use for this purpose.

Mr. ECCLES. Whenever the Federal Reserve System buys Government securities in the open market or buys them direct from the Treasury, either one, that is what it does——

Mr. DEWEY. What are you going to use to buy them with?

Mr. ECCLES. What is who going to use?

Mr. DEWEY. The Federal Reserve to make these purchases.

Mr. ECCLES. What do they always use?

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Mr. DEWEY. You are going to create credit?

Mr. ECCLES. That is all we have ever done. That is the way the Federal Reserve System operates. The Federal Reserve System creates money. It is a bank of issue.

What better evidence do you want than that, gentlemen? There is no dispute about what I say, and I insist it is absolutely wrong for this committee to permit this condition to continue and saddle the taxpayers of this Nation with a burden of debt that they will not be able to liquidate in a hundred years or two hundred years.

Do you know that we are carrying a million dollars' worth of bonds that were issued during the War between the States and we have paid 4 billions in interest for every $1 that was borrowed? We are still paying on them and still owe them. Do you know that on the Panama Canal convertible 3's, we have already paid more than $50,000,000 in interest and we will soon have paid $75,000,000 in interest and still owe the $50,000,000 principal on those bonds? If you judge the future by the past, the people will be compelled to pay a dollar, $2, and $5 in interest for every $1 they borrow. Does any man, then, say that we shouldn't seriously consider any plan that will enable the taxpayers of this Nation to make that payment on the principal of the debt and not on the interest? Two and a half million each year, and in 40 years liquidating the entire debt, and removing that inflationary condition that we will have by reason of the expenditures during this war.

W. L. Hemingway, president of the American Bankers' Association and of the Mercantile-Commerce Bank & Trust Co., St. Louis, in a speech on our national debt before the Chamber of Commerce of the State of New York, in New York City, said:

The war must and will be financed. It can be done in one of three ways—first, by printing paper money, Uncle Sam's demand I O U's. Fortunately this generation has seen the evils of that route and will have none of it. The second is by borrowing from the Federal Reserve banks directly, but that is but little removed from the paper money way because the Reserve banks would issue the money against the Government's notes or give credit on their books to the Government, which would pay it out for war purposes. It would then flow into the commercial banks increasing their legal reserves, thus inviting further inflation. So we come to the third and least objectionable way, and that is by borrowing from the public and the banks.

Both the Treasury and the banks want to see the banks buy as small a part of the succeeding issues as possible, because both understand that when the banks buy the bonds new bank credit or money is created and remains in circulation until their bonds are paid or taken by the public—an inflationary act to be avoided as much as possible. The banks should be only underwriters and distributors and not permanent investors.

I invite your attention to the following with reference to Mr. Hemingway's statement:

First, he says that banks should not be permanent investors of United States Government bonds.

Second, that it is highly inflationary for banks to buy United States Government bonds.

Third, in the second way, he says the war can be financed by borrowing from the Federal Reserve banks directly, he also says that is but little removed from the paper-money way because the Reserve banks would issue money against the Government's notes or give credit on their books to the Government, which would pay it out for war purposes. He could have very well added that the sale of Government bonds to commercial banks is no further removed from

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paper money than the sale to Federal Reserve banks if the excess reserves of banks are properly handled.

Reasons why commercial banks should not purchase bonds are contained in a statement of the Secretary of the Treasury issued April 25, 1942. It is as follows:

If the Government is compelled to go to the commercial banks for the bulk of these funds, the result will be to increase inflationary tendencies which are already serious. This is true because when commercial banks buy Government bonds they do not pay for them with actual cash taken from their vaults, but by placing on their books newly created deposits to the credit of their Government. When the Government draws upon those deposits to pay for the goods and services it buys, the purchasing power of those to whom these payments are made is increased without any decrease in the purchasing power of those from whom the money is borrowed.

When Mr. Eccles, chairman of the Board of Governors of the Federal Reserve System was before the Banking and Currency Committee, September 30, 1941, I interrogated him at length about the banks creating money on the Government's credit.

When Mr. Morgenthau, Secretary of the Treasury, and Mr. Bell, his Under Secretary, were before the Banking and Currency Committee on September 24, 1941, testifying on the price-control bill, I interrogated Mr. Morgenthau about banks creating money. He suggested that Mr. Bell, his Under Secretary, answer the questions. Mr. Bell was sitting by Mr. Morgenthau's side and the following questions were asked and the following answers were given, as disclosed on page 1132, volume 2, of the printed hearings on that bill:

Mr. PATMAN. In other words, when you sell a Government bond to a commercial bank, you allow the bank then to create the money.

Under Secretary BELL. That is right. We want to avoid that, as far as we can.

Mr. PATMAN. By a bookkeeping transaction?

Under Secretary BELL. Yes, sir; in the first instance.

Mr. PATMAN. And that increases the supply of money, just as much as if the country issued greenbacks directly?

Under Secretary BELL. It increases the supply of money, but I would not say it has the same effect.

Mr. PATMAN. It increases the supply of money to exactly the same amount as if the Government issued the credit directly?

Under Secretary BELL. That is probably right.

I doubt that anyone would want any higher authority on the question of commercial banks creating money to buy Government bonds than the testimony just quoted.

When Mr. Marriner S. Eccles, chairman of the Board of Governors of the Federal Reserve System, testified before the Banking and Currency Committee of the House, June 24, 1941, the following questions were asked and the following answers given, at page 68 of the printed hearings on S. 1471, a bill to amend the Federal Reserve Act.

Mr. PATMAN. Going back to this issue as to the Government's credit, is it a fact that the $20,000,000,000 that the commercial banks of the country hold today in United States Government bonds were purchased with created money?

Mr. ECCLES. Is it not a fact that what?

Mr. PATMAN. The $20,000,000,000 of Government bonds, approximately, that they purchased these bonds with created money.

Mr. ECCLES. What 20 billion of bonds?

Mr. PATMAN. That the banks hold today; approximately—between 19 and 20 billion dollars.

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Mr. ECCLES. I do not know exactly what the banks hold.

Mr. PATMAN. Well, that is not the main point. In other words, the bonds that the banks hold today—they created the money to buy those bonds, did they not?

Mr. ECCLES. The banking system as a whole creates and extinguishes the deposits as they make loans and investments, whether they buy Government bonds or whether they buy utility bonds, or whether they make farmers' loans.

Mr. PATMAN. I am thoroughly in accord with what you say, Governor, but the fact remains that they created the money, did they not?

Mr. ECCLES. Well, the banks create money when they make loans and investments.

Mr. PATMAN. All right; and these Government bonds were one of the investments.

Mr. ECCLES. That is correct.

Mr. PATMAN. Now we are back to where we were. The banks created the money to buy $20,000,000,000 or whatever it was in Government bonds. Therefore it has increased the available money supply by $20,000,000,000 did it not?

Mr. ECCLES. Yes; that is true, if those are the figures representing the increase in commercial banks. I think those figures are excessive.

Mr. PATMAN. It is over 19 billion, anyway?

Mr. ECCLES. I think those figures represent a large investment of savings funds.

Mr. PATMAN. I believe they do. Anyway, the commercial banks when they buy bonds or anything else, create the money, so to speak, to buy them with?

Mr. ECCLES. That is right.

Mr. Eccles testified before the Banking and Currency Committee June 17, 1942, on a bill to amend the Federal Reserve Act. His testimony which appears at page 15 of the hearings, discloses that commercial banks can buy all the bonds they desire to buy and if they are called on for money to pay their depositors the nearest Federal Reserve bank can always furnish them the money they need. His testimony is as follows:

Mr. PATMAN. Is it not a fact that you did send out letters to the banks which made the statement that the Federal Open Market Committee was ready to buy all the bonds at par?

Mr. ECCLES. No, sir; not buy, but we adopted a policy, each bank did, that would loan par on them.

Mr. PATMAN. That would loan par on Government securities?

Mr. ECCLES. Yes.

Mr. PATMAN. Do you charge the interest rate that is effective in that particular Federal Reserve district?

Mr. ECCLES. One percent.

Mr. PATMAN. One percent?

Mr. ECCLES. Yes.

Mr. PATMAN. Have you ever told all the banks that you stand ready to make loans at par at a 1 percent interest rate?

Mr. ECCLES. Each Federal Reserve bank has done that.

Since Mr. Eccles testified, the interest rate has been reduced to one-half of 1 percent. It is doubtful that the banks will need the money, but if they do the Government, through the Bureau of Engraving and Printing, will furnish it to them. The Federal Reserve banks will pay 30 cents per $1,000 approximately, for the currency, and the commercial banks will pay $50 per $1,000 interest per year, but will continue to receive interest on the bonds that they deposit with the Federal Reserve banks to obtain the money at one-half of 1 percent.

Mr. Eccles' testimony before the Banking and Currency Committee, June 17, 1942, commencing at page 16 of the hearings on the bill to amend the Federal Reserve Act, is as follows:

Mr. PATMAN. What are the excess reserves on the money market at the present time?

Mr. ECCLES. They are running around two billion five hundred million.

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Mr. PATMAN. How much could they buy in Government bonds if they were to use the excess reserves to the limit?

Mr. ECCLES. About $12,000,000,000.

Mr. PATMAN. $12,000,000,000?

Mr. ECCLES. Yes, sir; that is, assuming that the deposit structure and the present structure does not change.

Mr. PATMAN. It would be about $12,000,000,000.

Mr. ECCLES. Yes; you see, the Federal Reserve requirement is about 20 percent.

Mr. PATMAN. Yes, sir.

Mr. ECCLES. For the country it is 14, and for the central Reserve cities it is 20, and for the Reserve cities it is 26, so that we figure in about a 20-percent reserve requirement, so that on the basis of $2,250,000,000, if that were all fully utilized on the fractional reserve basis, I would estimate that they could buy about $12,000,000,000 worth of Governments, that is, if it were utilized fully and completely through the entire reserve, all the banks.

Mr. PATMAN. Suppose today they bought those $12,000,000,000 of bonds, what would they have back of those bonds to support them in addition to what they have now? In other words, what increased assets would the bank have except the Government bonds?

Mr. ECCLES. They would have the Government bonds themselves, which would be an asset, and they would have a liability, however, in the form of a deposit.

Mr. PATMAN. That is right.

Then further:

Mr. PATMAN. Let us suppose that the banks are called upon to buy $12,000,000,000 of Government bonds today. That consumes all their excess reserves. If you wanted to increase their excess reserves in order to buy another $12,000,000,000 of Government bonds, how would you do that, through the Federal Open Market Committee?

Mr. ECCLES. We might decrease the reserve requirements.

Mr. PATMAN. How would you decrease them?

Mr. ECCLES. I think it runs between $5,000,000,000 and $6,000,000,000.

Mr. PATMAN. Between $5,000,000,000 and $6,000,000,000?

Mr. ECCLES. Yes; somewhere between $5,000,000,000 and $6,000,000,000.

Mr. PATMAN. If it were decreased as you suggest, that would enable you to buy how many bonds?

Mr. ECCLES. If we decreased it to the full amount, then the reserve requirements are 10 percent instead of 20 percent, and you can buy about 10 to 1.

Mr. KEAN. What does change it from 5 to 1 to 10 to 1? Would you explain that again?

Mr. ECCLES. As it is, the requirements of the Federal Reserve Bank System of the country as a whole are about 20 percent. If we changed the reserve requirements to the full amount we could then say the reserve requirements are only 10 percent instead of 20 percent, and you can get about 10 to 1, and that would be about $50,000,000,000.

Mr. PATMAN. After you have already reduced the reserve requirements of the banks and have bought these $50,000,000,000 in bonds, if you need to buy still more, how would you handle the others? Suppose you wanted to call upon them to buy $25,000,000,000 more in bonds?

Mr. ECCLES. We would carry it on then, if it were necessary, by an open-market operation.

Mr. PATMAN. In other words, you would buy a billion dollars' worth of bonds. What would be the effect of that billion dollars on the banks?

Mr. ECCLES. If they could get a billion dollars they could buy up about $10,000,000 in bonds.

June 19, 1942, Mr. Eccles testified before the Banking and Currency Committee of the House on the amount of Government bonds that any bank could purchase. His testimony is as follows, at page 41 of the hearings on the bill to amend the Federal Reserve Act.

Mr. PATMAN. In the bill we passed here a few days ago, creating the Smaller War Plants Corporation, there was an amendment offered by the gentlewoman from Illinois, which was adopted and it is now a part of the law, providing that there should be no limitation on the amount of a loan to any person or corporation by any bank, providing, of course, that the loan is guaranteed by the Government, or some agency of the Government.

Have you given consideration to that amendment, Mr. Eccles?

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Mr. ECCLES. Are you referring to the technical aspects of it?

Mr. PATMAN. No; I am talking about—suppose a bank had a capital stock of $250,000, should they, under this amendment, negotiate a loan for say $5,000,000 if it is guaranteed by the Government or some agency of the Government?

Mr. ECCLES. It would take the limit off. There is no limit to the amount of Government bonds, for instance, that a bank can buy. Its only limit is its supply of funds.

Mr. PATMAN. You mean there is no limit now?

Mr. ECCLES. That is right.

Mr. PATMAN. This amendment did not cause that—it was already that way.

Mr. ECCLES. No; the difference is—there has been no question about direct obligations of Governments. This was simply a case of recognizing the loans which were guaranteed as having the same status as a direct Government obligation.

On the same day Mr. Eccles testified, at page 25 of the hearings:

Mr. PATMAN. Mr. Eccles, the day before yesterday I had gotten down to the point where, if we needed more money, one way to give the banks extra reserves to purchase Government bonds would be for the Open Market Committee to buy Government bonds in the open market, and I suggested if you bought for the Federal Reserve bank one billion dollars' worth of bonds, that would automatically create a billion dollars of reserves in the banks, and, after the reserves had been reduced to 50 percent, the maximum that would enable the banks to purchase $50,000,000,000 worth of bonds. Now, let us assume that has happened——

Mr. ECCLES. $10,000,000,000 worth by the purchase of a billion dollars' worth of bonds in the market?

Mr. PATMAN. I got the two mixed up. The purchase of a billion dollars' worth of bonds in the market, after the excess reserves had been reduced, will enable the banks to buy ten billion?

Mr. ECCLES. That is right.

Mr. PATMAN. Where the fifty billion came in was if you would automatically reduce the reserves now, which you have a right to do, that would give them $5,000,000,000 of excess reserves, which they could use to purchase $50,000,000,000 worth of bonds.

Mr. ECCLES. That is right.

Mr. PATMAN. Now let us assume that we not increase the reserves in the banks, and you go into the market and buy a billion dollars' worth of bonds; you buy them with Federal Reserve money, do you not?

Mr. ECCLES. Well, we buy them with Federal Reserve credit.

Mr. PATMAN. I know; but suppose the banks call for the money, you issue Federal Reserve notes, do you not?

Mr. ECCLES. What we do, if we purchase Government securities in the market, is we credit the account of the bank that turns them in. They usually come through the banks.

Mr. PATMAN. That is right.

Mr. ECCLES. Even though they may be individuals who are selling the securities; and we debit the bond purchase account, showing that the Federal Reserve has a liability to the banks to the extent of $1,000,000,000, which represents their reserves on the one hand, and that they own $1,000,000,000 of bonds in what we call the portfolio, on the other hand.

Mr. PATMAN. I know in practice that is exactly the way it is done, Mr. Eccles, but suppose the banks want the billion dollars in currency, you would pay it in Federal Reserve notes, would you not?

Mr. ECCLES. That is right.

Mr. PATMAN. Those Federal Reserve notes, as we have often discussed, are obligations of the United States Government?

Mr. ECCLES. That is right.

Mr. PATMAN. Then you use those Government obligations to buy interest-bearing Government obligations and you place them with the Federal Reserve banks—12 of them?

Mr. ECCLES. That is right.

Mr. PATMAN. And they would continue to receive interest on those Government obligations as long as they were outstanding?

Mr. ECCLES. That is right.

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On June 17, before the same committee, at page 21 of the hearings on the bill to amend the Federal Reserve Act, Mr. Eccles testified:

Mr. ECCLES. No; the Federal Reserve would buy in the open market. If the Federal Reserve then bought a billion dollars of securities in the open market that would be new Treasury issues. The banks would still hold them, and the Federal Reserve would put into the banks another billion of excess reserves. If they used that billion they could buy five billion more of Governments, and you could keep the price up. For every billion of the Federal Reserve banks put in the open market operations, the private banks could buy five billion.

Mr. DEWEY. That comes pretty close to some other ideas I have heard.

Mr. ECCLES. I mean they could buy ten billion. I mean the Federal Reserve when it carries out an open-market operation, that is, if it purchases Government securities in the open market it puts new money into the banks which creates idle deposits.

Mr. DEWEY. There are no excess reserves to use for this purpose.

Mr. ECCLES. Whenever the Federal Reserve System buys Government securities in the open market or buys them direct from the Treasury, either one, that is what it does——

Mr. DEWEY. What are you going to use to buy them with?

Mr. ECCLES. What is who going to use?

Mr. DEWEY. The Federal Reserve bank to make these purchases.

Mr. ECCLES. What do they always use?

Mr. DEWEY. You are going to create credit?

Mr. ECCLES. That is all we have ever done. That is the way the Federal Reserve System operates. The Federal Reserve System creates money. It is a bank of issue.

Mr. Allan Sproul is president of the New York Federal Reserve Bank, which is manager of the open-market system for the Federal Reserve System. On January 18, 1943, he addressed the bankers of the State of New York and stated:

Reserve banks are backing the commercial banks in investing to the limit in war financing.

Further it was said in his speech:

President of New York bank tells bankers of New York State that the Federals are here to save them from embarrassment if withdrawals reduce reserves.

In other words, the Federal Reserve System will continue to furnish all the money that the private banks need to pay their depositors in the event that it is needed and then they can purchase all the bonds they want to purchase with the assurance that the Government printing presses will protect them.

The Federal Reserve Bank of New York is acting as the manager of the Federal Reserve's open market system. This system is the most powerful factor in the money market in the United States. Washington authorities often do not know of important rules and regulations that the New York bank has put into effect until long afterward.

In connection with the question of how excess reserves are manipulated in order to permit commercial banks to buy additional bonds, the following is quoted from the bulletin published by the National City Bank of New York, October 1942.

In order to provide the additional funds required, the Federal Reserve banks have bought over $1,000,000,000 of Government securities in the open market since April, and have twice reduced the percentages of required reserve against deposits of member banks in the central reserve cities of New York and Chicago. The latter action followed enactment of legislation in July authorizing the Reserve Board to reduce reserve requirements for the rest of the country; and the reductions were confined to New York and Chicago by reason of the drain imposed upon these centers by the steady flow of funds to areas where war industries are located.

The first reduction, from 26 to 24 percent against net demand deposits, came on August 20, and released approximately $345,000,000 of reserves in New York City

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and $70,000,000 in Chicago. Within less than a month—on September 14—the second reduction, from 24 to 22 percent, was ordered, adding about the same amounts to excess reserves, on September 23, the "excess" totals in the two main financial centers were again approaching their earlier lows, while the total of slightly over $2,000,000,000 reported for all member banks was the lowest since 1938.

When Dr. E. A. Goldenweiser, Director of Research and Statistics for the Board of Governors of the Federal Reserve System, testified before the Banking and Currency Committee of the House on October 1, on the price-control bill, the following questions were asked and the following answers given, page 1538, volume 2, of the hearings.

Dr. GOLDENWEISER. The total reserves of the Federal Reserve are about 20½ billion, not 23 billion.

Mr. PATMAN. I am talking about the total gold supply that is either owned by the United States Government or claimed by the Federal Reserve banks through the——

Dr. GOLDENWEISER. The amount of the stabilization fund is not available to the Federal Reserve.

Mr. PATMAN. No; but I am presuming that it will be available. That will be 23 billions?

Dr. GOLDENWEISER. All right.

Mr. PATMAN. That leaves 16 billions unattached?

Dr. GOLDENWEISER. Yes.

Mr. PATMAN. How much bonds could the Federal Reserve Open Market Committee buy in the United States, Government bonds, based upon that?

Dr. GOLDENWEISER. It depends on how much of it will be in deposits and how much in notes. But, roughly speaking, about three to three and a half times.

Mr. PATMAN. Three and a half times?

Dr. GOLDENWEISER. No; not three and a half times. From two and a half to three times.

Mr. PATMAN. That would be about $40,000,000,000?

Dr. GOLDENWEISER. That is right.

Mr. PATMAN. When that money is paid out, suppose they pay it to the commercial banks, they could expand about five to seven to one on that, couldn't they?

Dr. GOLDENWEISER. If they paid that much assessment.

Mr. PATMAN. Yes; they would have the power to under the existing law?

Dr. GOLDENWEISER. That is right.

Mr. PATMAN. That means that, say, an average of six times—that is about right now, isn't it—about six?

Dr. GOLDENWEISER. Approximately.

Mr. PATMAN. That means that they could inflate about $240,000,000,000 more?

Dr. GOLDENWEISER. That is right.

It will be noted that the Federal Reserve banks and the commercial banks could expand their deposits sufficiently to purchase $240,000,000,000 worth of Government bonds at the time Dr. Goldenweiser testified. When the reserves are reduced to the limit that they can be reduced, these banks may purchase as much as $480,000,000,000 of Government bonds without having any more capital stock or assets than they now have except, of course, as Mr. Eccles always adds, that they will have the Government bonds.

The taxpayers have paid at least $4 for every dollar that was borrowed on the $1,000,000 now outstanding on the debt created during the War between the States. It is possible that the taxpayers will pay several dollars for each dollar borrowed before the debt is fully liquidated.

In the hearings on the price control bill, in 1941, volume 2, commencing on page 1354, the following testimony appears:

Mr. Chairman, I desire to insert in the record two questions that I have submitted to Mr. Morgenthau, under date of February 4, 1941, and his answers under date of February 15, 1941.

The CHAIRMAN. They will be incorporated in the record.

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Mr. PATMAN. I asked Secretary Morgenthau the following question:

"Your annual report for the year ending June 30, 1940, on page 730 discloses that there are outstanding now $758,945,800 in Treasury bonds that were issued October 16, 1922, and bearing 4½ percent interest. Please advise how much interest the Government will have paid on these bonds by October 15, 1947, and also by October 15, 1952."

Mr. Morgenthau's answer was as follows:

"The annual interest charge on the 759.9 million dollars of 4¼ percent Treasury bonds of 1947-52 outstanding on June 30, 1940, is 32.3 million dollars. For the 25-year period from their date of issue to their first call date, October 15, 1947, the total interest payments with respect to the amount of bonds outstanding on June 30, 1940, would be about 806.4 million dollars; and for the 30-year period from date of issue to final maturity on October 15, 1952, would be about 967.7 million dollars."

Mr. PATMAN. Then I asked this question:

"On the same page of the same report it is disclosed that there are $49,800,000 of Panama Canal loan bonds outstanding, which were issued June 1, 1911, and are redeemable or payable June 1, 1961, with a rate of interest of 3 percent. Please advise how much interest has been paid on these bonds to date and how much will have been paid by June 1, 1961."

And his answer was:

"The annual interest charge on these 49.8 million dollars of 3 percent Panama Canal bonds of 1961 outstanding on June 30, 1940, is about 1.5 million dollars. For the 29½-year period from their date of issue to December 1, 1940, the total interest payments with respect to the amount of bonds outstanding on June 30, 1940, would be about $44,000,000; and for the 50-year period from date of issue to maturity on June 1, 1961, would be about $75,000,000."

It will be noticed that in each of the cases inquired about the interest charges will be considerably in excess of the principal amount borrowed. This is typical of long-term bonds. Almost invariably the taxpayers are compelled to pay more interest than the amount of the principal on all long-term bonds, not only Federal, but also States and cities. In the case of the Panama Canal bonds, the taxpayers will be required to pay $75,000,000,000 in interest by the time the bonds are due and will then still owe the $49,800,000 originally borrowed. Other similar instances could be cited.

Mr. ROBERTSON. Mr. Chairman, I would like to ask a question. Mr. Patman, as you probably know, some have been unkind enough to refer to your plan as the issuance of printing-press money. Now, in order to get the difference between your plan and printing-press money, will you give us a plain and concise definition of printing-press money?

Mr. PATMAN. That depends on which plan you are talking about. You know, you couldn't have any more printing-press money than you are using today. If you think we are slipping into greenbackism, you can say we have already slipped, because that is what we are using now for money. It is just one of those obnoxious terms that people are wont to use against any plan they do not favor.

Mr. KNUTSON. Mr. Patman, I have heard it charged—I don't know but what I have heard you say it, that up to 1862 some similar plan to what you propose was before the Treasury Department in this country.

Mr. PATMAN. No, I don't think so, Mr. Knutson, but I will say this; that in 1861–65 there were $356,000,000 of money issued, and on a 5-percent annual-interest basis, more than $11,000,000,000 of interest on that money has been saved and the money is still outstanding, and that is just an example of what can be saved if you adopt this plan instead of committing the taxpayers to forever paying interest on this debt.

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Mr. KNUTSON. I am asking for information. What was the market history of that money?

Mr. PATMAN. You mean the United States notes?

Mr. KNUTSON. Yes; the greenbacks.

Mr. PATMAN. Well, they went down when they had no support behind them at all, and when they could be used only for a limited purpose.

Mr. KNUTSON. How far down did they go?

Mr. PATMAN. I don't know. They went down——

Mr. KNUTSON. Thirty-five cents?

Mr. PATMAN. Then the Government made them good for all purposes and placed some gold behind them. Of course, there is no danger on earth of any money outstanding. Take Federal Reserve notes, there is some criticism about those. There is no danger of those notes going below par. They will always be worth a hundred cents on the dollar. Those notes happened to be issued because they had them printed over there—I am giving you my opinion only. They may have had a different reason for it—and it is true they are obligations of the Federal Reserve banks. The Government permits the Federal Reserve banks to issue notes on the Government credit to the extent of tens of billions of dollars, so why should the Federal Reserve banks object to these notes being in circulation, which are obligations of the Federal Reserve banks to the extent of two-thirds of a billion dollars?

Mr. KNUTSON. It is my recollection those notes went down to thirty-five cents, around 1864.

Mr. PATMAN. I am sure they went down.

Mr. KNUTSON. Between 1864 and 1867.

Mr. PATMAN. There was nothing to keep them from it, when they were only good for a limited purpose.

Mr. KNUTSON. What was the limited purpose?

Mr. PATMAN. I don't know, it has been so long since I read their history, but I know they were restricted in use, and they went down. Senator Owen could tell you.

Mr. KNUTSON. They were currency. The greenbacks that were issued during the War between the States were currency and circulated as such. I don't think there was any restriction on its use, how the money could be used.

Mr. PATMAN. Well, I hope the gentleman would not want to use that as a reason why this plan should not be adopted.

Mr. KNUTSON. The only reason I inquire is that I was in Germany immediately following the war, and I will never forget that I had to pay 1,250,000 marks, that had a normal value of one-quarter in dollars, which would be about $300,000, for a breakfast consisting of half an orange, a very small piece of ham, one egg, dry toast, and a cup of coffee that I couldn't drink. I thought it was a little bit excessive. I don't need to argue with you that we all want to get out of this debt as easily as we can. I am not saying you haven't got a plan, because I don't know enough about it. It is my understanding, or at least I have read somewhere, that Germany went into this war with about $28,000,000,000 gold reserves; is that correct?

Mr. PATMAN. It couldn't have had that much gold reserves; there isn't that much in the world, 28 billion.

Mr. KNUTSON. Twenty-eight million, I meant.

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Mr. PATMAN. Excuse me, I thought you said billion. I wouldn't be surprised. They had a small gold reserve.

Mr KNUTSON. If that be true, and they financed the war through taxing resources to the utmost, as against wealthy nations like America, Great Britain, Russia, and China, it does look to me as though we should be able to find a way of working out of this thing without placing too great a strain upon our economy. I can't say you haven't got a good plan, Mr. Patman, because I don't know. I have been listening to you with a great deal of interest, and I am sure I represent every member of this committee when I say we want to finance this war in the very easiest way possible.

Mr. PATMAN. I join you in that hope.

Mr. KNUTSON. And we appreciate your taking the time to come before us this morning and explain your plan.

Mr. PATMAN. May I suggest about this German money; Germany doesn't have any gold reserve, hardly. Gold reserve is not so important now as the integrity of the nation and the taxing power and the ability of the people to pay taxes and debts. That means more than any metallic substance that may be behind any government obligation. When the war was over, Germany was a conquered country. We don't have to go to Germany to find out about money or currency. Go to the Confederate States of America, after the War between the States, and you will find currency just as worthless.

Mr. KNUTSON. Germany isn't a comparable country——

Mr. PATMAN. No; but Germany is financing her debt without gold by only the credit of the Nation. That is all that is behind money, the integrity of the nation, the ability of the people to pay taxes.

Mr. ROBERTSON. Doctor Hanson, of Harvard, agrees with that theory. He said Germany financed its war without money, but added that it took over the manpower and resources of the nation.

Mr. PATMAN. Manpower would have no connection with this, I will say to the gentleman from Virginia.

Mr. ROBERTSON. That is the way Germany proposed to finance its war without money, and some economists say we could do it.

Mr. PATMAN. We are fortunate in that we can finance it in a way just as convenient and not take over the manpower, as Germany did. We can get all of the benefits. without any of the liabilities.

(The following matter was submitted for the record by Mr. Patman.)

EDISON'S VIEWS ON THIS SUBJECT

About 20 years ago Mr. Thomas A. Edison was inspecting Muscle Shoals. He remarked that the Government should operate that great project in the interest of the people. He was asked if he favored the Government borrowing the $30,000,000 necessary to make repairs. His answer substantially was: "No; why should the Government borrow its own credit? If it issues tax-exempt interest-bearing bonds and sells the bonds to Wall Street bankers to get the money, by the time the bonds are paid the bankers will have collected as much in interest as the Government received on the bonds. In other words, the bankers, who will not furnish an ounce of material or a lick of labor, will get as much out of it as the men who do the work and furnish the material." Mr. Edison also said at the same time: "Any government that can issue a dollar bond, interest bearing, that is good can issue a dollar bill, noninterest bearing, that is good; the only difference is the bill is easier to redeem because it does not draw interest." No one can answer Mr. Edison's argument. This same argument can consistently be made on our preparedness program.

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ECCLES AGAIN QUOTED ON MONEY CREATION

Chairman Marriner S. Eccles, the top authority of the Federal Reserve Board here in Washington, testified before the Banking and Currency Committee of the House during the hearings on the Banking Act of 1935, on private banks creating deposits and thereby becoming virtually private individual mints, as follows:

"In purchasing offerings of Government bonds, the banking system as a whole creates new money or bank deposits. When the banks buy a billion dollars of Government bonds as they are offered—and you have to consider the banking system as a whole, as a unit—the banks credit the deposit account of the Treasury with a billion dollars. They debit their Government-bond account a billion dollars, or they actually create, by a bookkeeping entry, a billion dollars."

By a sort of magic the money is created.

CONSTITUTIONAL MANDATE

The framers of the United States Constitution, in article I, section 8, very wisely said:

"Congress shall have the power to coin money and regulate the value thereof."

This provision of the Constitution is mandatory. All Members of Congress are sworn to uphold the Constitution. Why has this provision never been carried out? The answer is simple. In the early days of our national existence the people were deceived into believing that the subject of money was so mysterious and intricate that only a few of the financiers understood the subject, and therefore the great privilege of issuing and distributing money should be farmed out to them. This was done, and it has never been changed, except to give them more power and authority. The strange part of it all is that the ones who are the beneficiaries of this great privilege are not even charged with the duty of furnishing the people a sufficient circulating medium.

LEON HENDERSON'S TESTIMONY ON NO DEBTS, NO MONEY

In the hearings before the House Banking and Currency Committee on the price-control bill, the following questions were asked by me and the following answers given by Mr. Leon Henderson (pp. 981–982):

"Mr. PATMAN. * * * You stated yesterday that everybody should take advantage of this period of rising prices to pay their debts. You really don't believe everybody should pay their debts, do you? If you mean that, what would we do for money, since our money is based on debt?

"Mr. HENDERSON. I have been through that, the same as you have, and I don't believe our economy would come to a halt if people paid their debts.

"Mr. PATMAN. If everybody paid their debts?

"Mr. HENDERSON. If you are going to say that I have discounted the trade acceptances which the Federal Reserve has created by a couple of bookkeepers, that is not the connotation debt has for me.

"Mr. PATMAN. You had in mind individual debts, personal debts?

"Mr. HENDERSON. Yes.

"Mr. PATMAN. And if the policy is good for individuals, why isn't it good for corporations?

"Mr. HENDERSON. I think it is.

"Mr. PATMAN. All right. If everybody paid their debts, where would you get money to carry on business?

"Mr. HENDERSON. You would get into debt and come out again. I assume the healthy process of credit is that you do liquidate debt as you do the trade acceptances."

Mr. Speaker, Mr. Henderson's very clever reply was, in effect, that it is all right to pay the debts, but you should get right back into debt again in order for the country to have this circulating medium.

CHAIRMAN MARRINER S. ECCLES' TESTIMONY ON NO DEBTS, NO MONEY, IN HIS TESTIMONY ON THE PRICE-CONTROL BILL BEFORE THE BANKING AND CURRENCY COMMITTEE

Chairman Eccles, of the Federal Reserve Board, testified as follows, page 1338 of the hearings, September 30, 1941:

"Mr. PATMAN. * * * You made the statement that people should get out of debt instead of spending their money. You recall that statement, I presume?

"Mr. ECCLES. That was in connection with installment credit.

"Mr. PATMAN. Do you believe that people should pay their debts generally when they can?

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"Mr. ECCLES. I think that depends a good deal upon the individual; but, of course, if there were no debt in our money system——

"Mr. PATMAN. That is the point I wanted to ask you about.

"Mr. ECCLES. There wouldn't be any money.

"Mr. PATMAN. Suppose everybody paid their debts, would we have any money to do business on?

"Mr. ECCLES. That is correct.

"Mr. PATMAN. In other words, our system is based entirely on debt."

Mr. Speaker, there can be no dispute about the statement that our system is based entirely upon debt, and if a person and corporation paid their debts we would not have sufficient money to do business on.

If we were to change that system the Government would pay its own money into circulation, and the people would be saved billions of dollars a year in interest.

The Federal Reserve Banking System is privately owned. Not $1 of the stock is owned by the Government or by the people; it is owned by private banking corporations. It is a corporation owned by corporations. Many people believe that the Federal Reserve Banking System is owned by the Government because it is named Federal, but of course this is not true.

CREATE MONEY, BUY BONDS, AND COLLECT INTEREST

When the Honorable Marriner S. Eccles, Chairman of the Federal Reserve Board, was before the Banking and Currency Committee of the House, of which I am a member, on Tuesday, September 30, 1941, I interrogated him about how he obtained for the 12 Federal Reserve banks the $2,000,000,000 in Government bonds, which the System is now holding and charging the Government interest thereon. The questions and answers appear in the printed testimony, volume 2, page 1342, and is as follows:

"Mr. PATMAN. * * * How did you get the money to buy those $2,000,000,000 of Government securities?

"Mr. ECCLES. We created it.

"Mr. PATMAN. Out of what?

"Mr. ECCLES. Out of the right to issue credit, money.

"Mr. PATMAN. And there is nothing behind it, is there, except the Government's credit?

"Mr. ECCLES. We have the Government bonds.

"Mr. PATMAN. That's right; the Government's credit."

Mr. Speaker, the Government is now paying between forty and fifty million dollars a year to the Federal Reserve Banking System as interest on these bonds. The expenses, dividends, and profits of the System are paid in that way. It would be just as reasonable for each department of our Government to be allowed to purchase enough Government bonds to pay their expenses the same way. It would be just as reasonable for the Government to set aside enough interest-bearing bonds to each Federal employee to pay the Federal employee interest sufficient to pay his salary as it is for the Federal Reserve Banking System to get their expenses paid in that way.

Under our present system the Federal Reserve banks can purchase twenty-five or fifty billion, a hundred billion, or an unlimited amount of Government bonds the same way they purchased and then held the $2,000,000,000. The System now owns about $6,000,000,000 in United States securities acquired the same way. Officials of the Federal Reserve System are paid salaries up to $50,000 a year.

Commercial banks that obtain a large part of their earnings from United States bonds bought with created money paid their officials up to $175,000 a year.

(Article from the Congressional Record submitted by Mr. Patman follows:)

WAR DEBT CAN BE PAID IN 40 YEARS WITHOUT UNBEARABLE BURDEN ON TAXPAYERS BY CONGRESS USING THE GOVERNMENT'S CREDIT AND IDLE GOLD INSTEAD OF CONTINUING TO FARM IT OUT TO SPECIAL PRIVATE CORPORATE INTERESTS

"[H. R. 1, 78th Cong., 1st sess., Jan. 6, 1943]

"A BILL Providing for the issuance of nonnegotiable United States bonds to Federal Reserve banks and terminating the authority of the Treasury to issue other interest-bearing obligations of the United States to commercial banks, and for other purposes

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"*Be it enacted by the Senate and House of Representatives of the United States of America in Congress assembled,* That the Secretary of the Treasury, with the approval of the President, is authorized to issue from time to time United States bonds, the proceeds of which shall be available to meet any public expenditures authorized by law and to retire any outstanding obligations of the United States bearing interest or issued on a discount or on a combination interest-bearing and discount basis. Such bonds shall be issued in such form or forms and in such denominations, and mature at such times (not in excess of 40 years from the date of issue) as the Secretary of the Treasury may prescribe. Such bonds shall not bear interest or be issued on a discount basis and shall not be negotiable or transferable.

"SEC. 2. Bonds issued under the provisions of this act shall be issued solely to Federal Reserve banks and shall be subscribed for by the various Federal Reserve banks in such proportions of the entire issue as may be agreed upon by the Secretary of the Treasury and the Board of Governors of the Federal Reserve System. The Secretary of the Treasury shall pay, out of any funds hereafter appropriated for such purpose, to each Federal Reserve bank subscribing to bonds issued under this act, such amounts as he deems necessary to reimburse such bank for any expenses incurred by it in connection with such bonds.

"SEC. 3. The authority of the Secretary of the Treasury to issue any interest-bearing obligations of the United States (including obligations issued on a discount basis or on a combination discount and interest-bearing basis) under any other provisions of law is hereby terminated insofar as the issuance of United States bonds to any bank receiving demand deposits is authorized hereby. Except in accordance with such regulations as the Secretary of the Treasury may prescribe in order to provide for the orderly disposition of United States bonds held by any bank receiving demand deposits on the date of the enactment of this act, no such bank shall at any time hold any amount of United States bonds in excess of the amount held by it on December 31, 1941.

"SEC. 4. The first two paragraphs of section 7 of the Federal Reserve Act, as amended, are amended to read as follows:

" 'SEC. 7. After all necessary expenses of a Federal Reserve bank have been paid or provided for and a surplus equal to the paid-in capital stock of such bank accumulated, the annual net earnings of such bank shall be paid into the general fund of the Treasury.

" 'Should a Federal Reserve bank be dissolved or go into liquidation, any surplus remaining, after the payment of all debts and the par value of all stock, shall be paid to and become the property of the United States.' "

WILL STOP FARMING OUT GOVERNMENT CREDIT AND USE OF IDLE GOLD FREE TO BOND BUYERS

Section 1 of the bill will permit the Secretary of the Treasury, instead of selling Government interest-bearing bonds, to receive the money necessary to meet any public expenditure by issuing and depositing with the 12 Federal Reserve banks bonds that provide for no interest. These bonds will not be sold to the public, as the public generally would probably not be interested in buying them since they will not draw interest, but the Federal Reserve banks can keep them, and each year the Government can make a payment on the bonds to the Federal Reserve banks.

Under our present system the Treasury, when it needs money, sells bonds that provide for interest through the Federal Reserve banks, and in that way the Treasury receives credit at the Federal Reserve banks, which is checked upon in order to pay the debts of the Government. This proposal will permit the Treasury to receive the same amount of credit as on interest-bearing bonds and the Treasury may check upon this credit in the same manner that it is checked upon today when interest-bearing bonds are sold. In other words, when this proposal is enacted, the Treasury will give the same kind of checks to the same people for the same service, or in payment of the same debts. The people receiving these checks under the new proposal will deposit them or receive the money on them in the same way and manner that they now receive credit at the local banks, or receive the money in return for their checks.

This will not cause the distribution or circulation of one extra dollar of actual currency. Therefore, it cannot be considered a greenback or printing-press proposal. It is strictly an orthodox banking method, which will permit the Government to finance the war debt without paying tribute to a few people who are using the Government's credit and idle gold absolutely free.

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HOW NON-INTEREST-BEARING BONDS DISTRIBUTED

Section 2 of the bill provides the method by which the bonds, which will be noninterest bearing, will be distributed among the 12 Federal Reserve banks. The method that will be agreed upon will doubtless be according to the capital stock or resources of the particular bank. If the Treasury needs a million dollars, it will distribute the bonds among the 12 Federal Reserve banks, which will aggregate a million dollars. The largest Federal Reserve bank, of course, will take much more of the bonds than the smallest Federal Reserve bank.

The distribution will be made by the Treasury and the Board of Governors of the Federal Reserve System.

BANKS WILL BE PAID FOR SERVICE

This section also provides that the Federal Reserve banks will not lose any money by reason of servicing these loans to the Government without interest since the bill provides that each bank shall be reimbursed for any expenses incurred in connection with the bonds. The expenses, of course, will be practically nothing (not as much as one-twentieth of 1 percent interest) compared with the huge amounts of bonds that will necessarily be issued to finance the war debt.

IF MONEY IS TO BE CREATED IT SHOULD BE CREATED BY THE GOVERNMENT AND NO INTEREST PAID ON IT

Section 3, the first sentence, provides that no more interest-bearing obligations of the United States shall be issued and sold to commercial banks, or banks receiving demand deposits. The reason for that is that such a bank does not have anything to give the Government in return for its bonds. It merely receives the bonds and gives the Government credit in bookkeeping transactions, or pencil-mark or fountain-pen money. Every informed person admits that under such circumstances, the commercial banks create the money outright. If money is to be created outright it should be created by the Government and no interest paid on it.

BANKS CANNOT FURTHER INCREASE HOLDINGS OF GOVERNMENT BONDS

Section 3, in the second and last sentence, provides that no bank which receives deposits, in other words a bank that must create the money in order to buy bonds, shall at any time hold any amount of United States bonds in excess of the amount held by it on December 31, 1941. In other words, if a bank held $2,000,000 in Government securities on the date mentioned, it can sell any amount of those bonds that it desires to sell, and may in turn purchase other United States Government securities up to, but not in excess of the $2,000,000, which was the amount held December 31, 1941.

BANKS NOW LEND $10 TO EVERY $1 OWNED

The stockholders in all the banks in the United States have invested and would lose if the banks should be forced into bankruptcy or liquidation and there should be no recoveries, the total sum of $8,000,000,000. About three and one-half billion dollars of this is capital; about three and one-half billion dollars is surplus, and about $1,000,000,000 in undivided profits, making about $8,000,000,000. That is all the stockholders in banks in America have invested in these banks. Notwithstanding, only $8,000,000,000 are invested in all these institutions, they have purchased more than $40,000,000,000 in United States Government securities, and now hold these securities and receive interest on them annually and expect to hold $112,000,000,000 by the end of the next fiscal year. Without stating or discussing how much the banks should be allowed to expand, it is evident that orthodox banking methods, safe banking methods, and logical banking methods should prohibit any bank from expanding more than $10 for every one that it owns. Let us presume, for the sake of discussion, that it is right for a bank to be allowed to lend $10 for every one it has, and thereby receive interest on $10 for every $1 invested by the stockholders and still we cannot escape the logical conclusion that no bank should be allowed to expand more than $10 for every one.

CONGRESS SHOULD NOT SIT IDLY BY

This being true, why should Congress sit idly by and allow the banks to expand $20 to every one, or $50 to every one, in order to finance the war and the other expenditures of our Government when it is nothing more nor less than Congress

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permitting the credit of this Nation to be farmed out for the selfish benefit of private banking corporations?

GOVERNMENT CREDIT FARMED OUT

The Government of the United States, under the Constitution, has the power, and it is the duty of the Government, to create all money. The Treasury Department issues both money and bonds. Under the present system it sells the bonds to a bank that creates the money, and then if the bank needs the actual money, the actual printed greenbacks to pay the depositors, the Treasury will furnish that money to the banks to pay the depositors. In that way, the Government farms out the use of its own credit absolutely free.

BACKING FOR NON-INTEREST-BEARING BONDS

If the Federal Reserve banks provide the credit to finance the war, as proposed in the bill, inserted herewith, these bonds will be backed by the credit of the Nation, which includes the taxing power of the Nation, and also the $23,000,000,000 in gold that is now idle and unused, except that portion that is used free by the private banking system of this country.

BONDS BACKED BY TAXING POWER, TOO

A bond issued by the Government carries with it an obligation that Congress will pass laws levying taxes which will be sufficient to cause the taxpayers to pay money in taxes to pay the interest on the bonds, and to eventually retire them when due. The history of the issuance of long-term bonds by our Government is conclusive that the Government invariably pays $2 to every $1 that it borrows. In other words, it pays $1 in interest and $1 in principal.

GOVERNMENT TO PAY DOUBLE

A $100,000,000,000 debt means, under the present system, that the taxpayers will eventually have to pay $200,000,000,000. With a huge debt of $300,000,000,000, which is estimated by many Government authorities as being the amount that the public debt will reach before the war is over, it will probably be impossible for the taxpayers to pay enough money each year to liquidate any part of the principal of the bonds. Therefore they will remain in bondage for centuries because they will be unable to pay any more each year than is sufficient to provide for the interest on the bonds.

$1 PAID MONEY CREATES FOR EVERY $1 PAID A SOLDIER

Viewing the situation from the most optimistic viewpoint, the taxpayers will be compelled to pay at least $2 for every $1 borrowed. For every $1 that is paid to a soldier, the money creators have nothing to offer except the Government's credit, which has been given to them free, will also receive $1. For every $1 that is paid to every person for materials furnished, the money creators will receive $1 in interest for no service whatsoever in the form of interest for furnishing the Government's credit, which has been furnished to the money lender free. For every $1 that is paid out for any purpose, in this war or for peacetime pursuit, the interest will amount to at least $1, and the result will be that the taxpayer must pay $2 in order to liquidate every $1 debt.

I cannot understand why anyone should insist that the credit of this Nation and the use of the Government's gold should be farmed out absolutely free to the private banking corporations of this country, and require the taxpayers to pay at least $2 in order to obtain $1 in our war preparation.

REPAIR HOPELESSNESS OF PEOPLE

Let us repair the hopelessness that is now being felt by the people on account of what they think will probably happen after the war with a $300,000,000,000 public debt by changing the system so that the Government can use its own credit and its own gold and not pay $2 for every $1 that is borrowed.

WAR DEBT CAN BE PAID IN 40 YEARS

If our national debt for the war is $300,000,000,000, it can be paid over a period of 40 years without an unbearable burden on the taxpayers by the Government borrowing money from the Federal Reserve banks and paying it back 2½ percent

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each year. This 2½ percent will be no more than interest that is being charged today, and the amount will be sufficient to entirely pay off the bonds in 40 years. Whereas if we continue the present system of paying interest on these bonds, at the end of 40 years, after paying 2½ percent each year, we will still owe the principal amount of the bonds, and the debt will be just as large at the end of 40 years as it is today or when the debt is the largest.

WILL REDUCE CHANCES OF INFLATION

If we borrow the money to finance the war from the Federal Reserve banks and it is paid 2½ percent each year and entirely paid off and liquidated in 40 years, there will be no likelihood of inflation during that time. Whereas, if we continue paying tribute to a few for the use of the Government's own credit, we will in all probability have inflation unless it is possible to prevent it by price control and other methods.

DUTY OF CONGRESS TO MAKE CHANGE

It occurs to me that the duty of making this change is on Congress. It is not on the executive, the judiciary, or any department of our Government. It rests solely and alone upon the Congress of the United States to change the system that causes our credit to be farmed out and enormous interest burden paid unnecessarily and uselessly on its credit.

ABUSE OF POWER TO TAX

If Congress continues to require the people to pay billions of dollars a year unnecessarily as interest on Government bonds it occurs to me that it is an abuse on the part of Congress of the power to tax. Congress has the power to tax and is exercising that power to the limit, but certainly Congress should not abuse the power by levying taxes to pay a debt that is extravagant, wasteful, and unnecessary in every way.

NOW TIME TO MAKE THE CHANGE

One of these days, the American people are going to wake up and realize the situation, and they will blame this very Congress for not making the change at this time, when we are entering upon a $300,000,000,000 war program. Now is the time to make the change. It is not a change that will involve unorthodox banking methods. It is a change that will save the Government interest on the public debt hereafter contracted, but will not be in any way dangerous to the general welfare of the country. On the other hand, it will be greatly in the interest of the general welfare of the country because the war debt will cost the taxpayers only 50 percent, at least, of what it will cost under the present system.

BOND SALES TO PUBLIC SHOULD CONTINUE

I am not proposing that bond sales to the public be stopped or impeded in any way. It is my belief that bond sales to the public should be encouraged because they are calculated to prevent or stop inflation to a certain extent. At the same time we know that the bonds that the public are buying at this time, will, when this emergency is over, be in the market one way or another and, that being true, the money creators will be in a position to purchase them by using the Government's credit free and the idle gold free, and receive interest from the Government for no service whatsoever.

$1,000 INTEREST PER CAPITA TO BE PAID ON THIS YEAR'S BUDGET

The Budget for next year is $108,000,000,000. This means that it will cost the American taxpayer by the time the $108,000,000,000 debt is paid, under our present system of farming out our credit free, twice that amount, or $216,000,000,000. This means that every man, woman, and child in America, on this $108,000,000,000 debt, will have to pay about $1,000 in interest and $1,000 on the principal, presuming that the debt can be paid in 40 or 50 years. It is not right for Congress to make the people pay that $1,000 for every man, woman, and child in America as interest for the use of the Government's own credit and for the use of the Government's own idle gold by farming out the Government's great privilege and right to create money to private banking interests of the Nation.

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PERPETUAL DEBT

The current estimate of what the war, whole war, is going to cost us is $300,000,000,000. If we spend $300,000,000,000 on this war, it will cost about eight or nine billion dollars a year to pay the interest on the $300,000,000,000. In all probability, that is all the taxpayers of this country will be able to pay, and will, therefore, be unable to make any payment on the principal of the debt each year. That being true, all the money that will be raised in taxes to pay on the national debt will go to the people who are using the credit of the Nation absolutely free, and who have had farmed out to them the use of the idle gold free, and the people will thereby be caused to pay a debt that is useless, wasteful, extravagant, and unnecessary.

It Is Wrong for the Government of the United States That Is Sovereign To Pay Private Corporations to Create Money on the Government's Credit

UNITED STATES SOVEREIGN

No city is sovereign because it has superiors, the State and the National Government. A State is not sovereign because it has a superior in the National Government. The National Government is sovereign because it has no superior in the form of a government, and the National Government has the power to create its own credit upon which no interest should be paid instead of farming out that great privilege to the private banks of the country.

The Chairman. Have you finished your statement?

Mr. Patman. Yes, Mr. Chairman.

The Chairman. We thank you.

Mr. Patman. I want you to hear from the Honorable Robert Latham Owen, a Member of the United States Senate from the State of Oklahoma from 1907 to 1925. He was chairman of the Committee on Banking and Currency of the Senate and was coauthor of the Owen-Glass Federal Reserve bill when the Federal Reserve Act was enacted into law December 23, 1913.

Senator Owen is one of the best informed men in the world on our United States monetary system. He organized and has been a director of a successful national bank for 50 years. When President Woodrow Wilson signed the Federal Reserve Act December 23, 1913, he wrote Senator Robert L. Owen a beautiful letter that he was entitled to the gratitude of the country and gave him one of the gold pens with which he signed the bill.

The Chairman. How much time will he require?

Mr. Patman. I assure the chairman he can make a great contribution to this subject, or any other subject, and I hope you will hear him with consideration. I know he will be conservative in time. He never did take up much time. I assure you he will take no more than the subject justifies.

The Chairman. Very well; we will hear him.

Statement of Hon. Robert L. Owen, Former United States Senator From the State of Oklahoma, Before the Committee on Ways and Means, House of Representatives, February 13, 1943

Mr. Owen. My name is Robert L. Owen. Mr. Chairman and gentlemen of the committee, it is not what I might say to you, but what you receive, that is a matter of importance now before your committee.

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You are proposing a bill to expand the credit outstanding, the indebtedness of the United States, up to $210,000,000,000, as I understand it. Mr. Patman suggests that in doing so you hold down, as far as you can, that indebtedness by protecting the taxpayers from unearned interest on that debt. I have some familiarity with the banking system. I regard our free competitive system of industry and our banking structure as the best in the world, and the services of our bankers to the country have been very great. I have been a director of a bank for 53 years, in recent years, I think, purely complimentary, but I am familiar with the banking system, and I am familiar with its history, and I manufactured money myself in that capacity in a few little ways that I think might interest you, if I may take a moment.

When, in a great pressure one time for currency, with the consent of the citizens of the town, the bank of which I was president issued cashier's checks payable to bearer, $5 each. They circulate as money. perfectly good money. They functioned in exchanging commodities and services from one person to another in that locality.

I might give you another instance, or instances. The Chase National Bank has 2,000 forms of script money, issued by the citizens of this country without interest for the same purpose, of facilitating the exchange of commodities and services from one person to another.

On one occasion, as the president of a national bank, I wired to our New York correspondent to place an order and buy $500,000 of bonds, place them with the Comptroller of the Currency, make a deposit from our account of 5 percent, and receive from the Comptroller of the Currency national bank notes to the extent of $500,000, on which my bank received the interest for many, many years, and of which I was a beneficiary as a stockholder, without shame. It was the practice of the country.

But we are now facing a great World War, in which the resources of this country will be taxed to the utmost, to such an extent that this honorable committee has found it advisable to tax the little citizen of the country who is receiving $13 or more a week as compensation. That tax will be employed in defending the interests of our country on the battlefield and in furnishing our soldiers with the weapons of war.

But I call your attention most earnestly to the fact that when you expand this credit to $210,000,000,000 of indebtedness of the United States, as we must do—you have got no option about it; you have got to do it—when you do that, do not add to that burden, as a part of it, unearned interest money.

When I say it is unearned, I must justify that statement, if it is to have any force. Our forefathers had some experience with money. One of the contributing causes to the Revolutionary War, as recorded by Benjamin Franklin, was the fact that the English Parliament stopped the circulation of the colonial money, in order to put English money in circulation in the United States, and caused a tremendous depression, and idleness, and contributing to the distress of our forefathers at that time.

It was done by contracting the volume of money in circulation, which stopped the people from the free interchange of commodities and services, because they didn't have the medium of exchange.

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When I say unearned interest, gentlemen, I go back to the Constitution of the United States, where our forefathers put into the first section of the Constitution a provision that the Congress of the United States was exclusively authorized to coin money and regulate the value thereof. The Supreme Court of the United States, in the *Legal Tender cases*, held in substance that the term "coin" covered printing paper money. They also held that the Congress of the United States was exclusively authorized to create money, and that that right was withheld from the States, and when we come to creating money, and the question is asked, "what will be paid for a Government bond?" let us look at that transaction.

The Government sells to a bank a million dollars of Government bonds. Does the bank pay for it in currency or coin? Are they expected to pay for it in currency or coin? Certainly not. Well, what do they pay for it with? They pay for it with their individual banking credit, by an entry on the ledger of the banking house, whether a national bank or any other bank, and against that credit the Treasury Department can draw checks, and the same thing is done with the Federal Reserve banks as an agency of the United States, established for the express purpose of exercising supervisory control over the monetary system of this country.

Precisely the same thing takes place as when $5,000,000,000 was recently sold to the Federal Reserve banks against the credit on the books of those banks. Nothing strange about it. Everybody understands it who pays any attention to this question. But I realize, Mr. Chairman, and gentlemen of the committee, that a great many people in the United States have had no particular time to study the monetary science, there has been a general understanding that money was a mysterious thing, and nobody understood what made the value of money. That has been proclaimed from the housetops by some persons of rather high authority—that nobody knew what made the value of money.

Oh, well, we have learned now what makes the value of money, and we have learned that when we expand the credit of the United States by the issuance of bonds up to the present moment that we have created money and put that money in the banks and into the hands of private citizens, and we have learned that we must contract that amount of taxations so far as we can without destroying our productive processes, and we have found that we must contract it by selling bonds to individuals and corporations who have money on deposit in banks as demand bank deposits.

Why certainly we have got to do that. There is no doubt about it. No doubt about it. Otherwise, the volume of money in circulation would rise to a point where it would be impossible to fix prices and hold those prices down to a reasonable point.

As it is, with great skill, with great patriotism, the Treasury Department has been enabled to sell bonds to the extent necessary to hold the dollar index down to approximately par. It is true that in February a year ago it was 124, but then it came down approaching par, and those efforts on the part of our Government and on the part of this honorable committee and the Congress of the United States and the cooperation of the people have brought that dollar index down again, very, very slowly in the recent months, only a mill or two a week, only two mills last week. It is now 98 as compared to 1926.

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If you will examine the volume of money in circulation through the banking system in the device of individual accounts on the books of the banks, not including interbank checks, you will find that in 1926 the volume of money turned over in that way by check, amounted to $845,000,000,000, and had a turn-over approximately 40 times a year the amount that was being circulated. It is not far from that now. And the circulation of money has been kept down by this process of taxation and of selling bonds, so that the dollar index has been held down.

There is one feature, with your permission, I would like to comment upon, and that is this; that it should be true at all times that whether our industrial production is engaging in war products or domestic products, the ratio of the income arising from it corresponds to the amount actually employed in turn-over, the income being three times the amount of the money actually employed in actual circulation. So that it is of importance, particularly in this connection, that our domestic production, to be kept up to the maximum, will require the amount of money in circulation to be according to that formula.

I mention that because we are now being concerned about raising a sufficient amount of production to feed Europe as well as ourselves and our soldiers on the front. Therefore, the question of domestic production needs attention by the Congress of the United States, and in that connection, it needs to consider the employment of money as one of the agencies in expanding that domestic production.

Coming back, therefore, to the Constitution of the United States, where Congress was exclusively authorized to create money, and the process by which Congress has been creating it, I express the hope that this committee will consider with the greatest care the proposition submitted to it by Mr. Patman, of cutting down the expansion of the payment of unearned interest to anybody, including myself, as a stockholder in a bank.

I do not wish to take the time of the committee, further than to express these opinions. If there are any questions which any of the committee would like to ask me to comment on, I shall be glad to do it. My only purpose in coming here is to serve the people of the United States, and because I was urgently invited to come, thinking that my experience might be of interest or value to the committee. I pause, Mr. Chairman, for any questions that you or any member of the committee might care to ask me.

Mr. KNUTSON. Senator, would the plan that Mr. Patman proposes tend to bring on uncontrolled inflation?

Mr. OWEN. It would have a tendency to prevent, to the extent it is employed to prevent the expansion of the money which will produce inflation. I am not going to use the term "uncontrolled inflation." I know that inflation can be controlled by an intelligent and strong government, and I am in favor of it. I have always demanded stability in the purchasing power of money, and when I had been in the Senate less than 90 days I made an address before the Senate making that demand, and I based the address I made on the Aldrich bill, on the grounds of stabilizing the purchasing power of money because it would itself stabilize the industrial activities of this country and stabilize the productive power of the greatest people in the world, and I have been deeply disappointed in the administration of the act,

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which ought to have accomplished that result in a way in which I pointed out from time to time in the public press, and to which I have the right to refer now. It could have been prevented. The contraction which took place in 1920–21 was over my vehement protest and with my statement on the floor of the Senate that it would cause a depression, which it did cause immediately afterwards.

Mr. KNUTSON. That depression you are referring to in 1920–21 was caused altogether by the Federal Reserve calling their agricultural loans, was it not, Senator?

Mr. OWEN. No; not altogether.

Mr. KNUTSON. Largely, then?

Mr. OWEN. No; not largely. It had a ruinous effect on agriculture.

Mr. KNUTSON. From which it has never recovered.

Mr. OWEN. From which it has never recovered.

Mr. KNUTSON. You are right.

Mr. OWEN. Of course, I am right, and everybody knows it. What did take place at that time was a deliberate policy of contraction for the purpose of cutting down the market price of commodities and services and thereby increasing the purchasing power of money, and benefiting creditors and those having their investments in money, without giving time to the people to adjust themselves to it. Therefore, they created a panic.

Mr. KNUTSON. Well, it had the effect, up in our country, of bringing about forced sales of cattle and grain, and as a result the markets became glutted and it further accelerated the movement downward. Isn't that right?

Mr. OWEN. Yes; that took place. What took place in 1929–32 was an occurrence on the other side of contraction, that is, inflation of credit—about $14,000,000,000 in the security market. There was a gross expansion of credit in the security markets, so that billions of dollars of foreign money and billions of dollars of domestic money created by the sale of stocks of our great industrial companies which flowed into the security market, and caused the market price of securities to rise beyond reason, to rise beyond the point where they could possibly earn interest on the investment, rise to a point which showed to the thoughtful, prudent bankers of the country that there would be a collapse, and in May 1929 I wrote a memorandum of 16 pages to President Hoover, with 12 charts, and took it in my hands and presented it to him at lunch and urged him to study the matter for the purpose of meeting what was going to happen. What took place afterward, I will not comment on, except to observe that a credit convulsion and violent bear movement occurred in October 1929 resulting in enormous contraction of the money supply with panic and bankruptcy following.

The CHAIRMAN. What did he say about your charts?

Mr. OWEN. He said, in answer to my prayers, that if he interfered with the Federal Reserve Board or the Federal Reserve banks he would be accused of using politics in the System and it would injure the System, in his opinion. I replied to him that he, as President of the United States, was charged with the responsibility of leadership and of protecting the people of this country against what would inevitably happen unless the full powers of this Government were used to meet the crisis that was impending, and that if he did not do

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it, it would ruin him politically and ruin his party. And I put that in writing and I gave a copy of it to the chairman of the Banking and Currency Committee of the House, if any of you want to see it.

The CHAIRMAN. Have you brought the same situation to the attention of President Roosevelt? If so, what was his reply?

Mr. OWEN. President Roosevelt had his attention called to the violence of this depression by some very important occurrences which preceded his election, and which had been brought about by the very things I was protesting to Hoover. He came in after 1932, at which time I am telling you this country was manufacturing its own money from one end of the country to the other and establishing barter exchanges in order to exchange products where there was no money available for exchange. Mr. Roosevelt came in when this country was facing the greatest disaster, financially, it ever had faced in its history, and when he came in he had to declare a public holiday for the banks of the country. Why? Because the people of this country were so disturbed there was danger of runs on the banks from one end of the country to the other. Ten thousand banks failed under this depression of 1932 by the destruction of the value of their securities. Then Congress took steps to stabilize, authorized the issuance of money and of credit. As a matter of fact, the Federal Reserve Board and Federal Reserve banks, instead of expanding credit, contracted it during the next 18 months, to the extent of approximately $3,000,000,000. The record shows that and I pointed it out, and I pointed it out in writing to the proper authorities, with proof, and the proof of it can be found by anyone interested in it, by looking up the weekly statements of the Federal Reserve banks of March 14, 1933, and the corresponding week in 1934. I have been deeply interested in these matters and have made a most resolute effort to understand them.

The CHAIRMAN. I didn't quite get clear how far you had gone in prosecuting this matter proposed in Mr. Patman's bill and discussing it with Secretary Morgenthau and Mr. Roosevelt as it relates to our present situation, borrowing large amounts of additional money. Have you had any discussion with the administration about it?

Mr. OWEN. Oh, no; I have not been invited to discuss it, and I do not feel quite justified in imposing my personality upon the authorities of the Government. When I am called on to answer, I am glad to do the best I can to help solve these problems. But I want to say this, and say it very plainly; regardless of anybody's opinion, this committee now has the opportunity of saving the taxpayer's 2 or 3 billion dollars a year in unearned interest to be paid to the stockholders of the banks of this country. That is what I have got to say, and I am opposed to any further expansion of the debt for that purpose, and I wish my opposition to be put in the record. I did not come here for that purpose, but now that I am here, I feel like expressing my opinion, because I have no reason not to, and because I think it may be useful. I think it is a very grave responsibility on any member of this Congress to be taxing $13 a week and giving away unearned interest to the extent of billions per annum. I will not approve that, as a citizen of the United States; and, as a citizen, I speak.

The CHAIRMAN. You always speak very interestingly, Senator.

Mr. OWEN. I have a very determined view about it.

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The CHAIRMAN. May I ask you this question, just for my own guidance. If the administration and the Secretary of the Treasury have a great responsibility in guarding the credit of the Government at this time, during the war, do you think before we take any further action on this that they should be called in to give their viewpoint?

Mr. OWEN. I certainly do, and I would like them to answer the questions I am putting to you—why billions of dollars in unearned interest to stockholders and taxes on $13 a week? Ask them to answer that and I will be content to hear it.

The CHAIRMAN. I believe Mr. Patman has a bill, H. R. 1.

Mr. PATMAN. Yes, sir; H. R. 1.

The CHAIRMAN. It was thought this matter would more properly come up here, rather than have protracted hearings——

Mr. OWEN. You don't need any protracted hearings, in my opinion.

The CHAIRMAN. We all have respect for Mr. Patman. There is no man in Congress we think more highly of, and I listen very attentively to what he presents. I was wondering whether, on this bill, we would have time to get all the needed information.

Mr. OWEN. You don't require much time.

The CHAIRMAN. And call the various witnesses.

Mr. OWEN. You don't need very much time.

The CHAIRMAN. I know in your opinion, and the opinion of Mr. Patman, you wouldn't require very much time.

Mr. OWEN. Either what I have said is true and just, or it is not. And if Mr. Morgenthau can come here and show it isn't, that can be done in a few minutes.

The CHAIRMAN. I know, but there is hardly ever a question comes up here that there is not a difference of opinion. We have had scores of witnesses here on this other matter, and hardly any two of them agreed, and each one said that what they said was true.

Mr. OWEN. It is for the intelligence and judgment of this committee to determine what is just and true.

The CHAIRMAN. We don't know until we hear both sides of a question, do we? If you have a case in court, you wouldn't hear the plaintiff and not the defendant.

Mr. OWEN. I have just said to you that I suggest Mr. Morgenthau answer what I have told you.

The CHAIRMAN. I just ask you whether you think the committee should do that before we attempt to decide this matter. This bill Mr. Patman introduced should be considered seriously, but whether or not, at the same time, we should go into lengthy hearings—the banks will want to be heard, the administration will want to be heard, the representatives of all kinds of people will want to be heard. This is a rather sweeping change, and the committee could hardly be expected to come to a satisfactory decision until it heard all the facts from the people who wish to be heard. And it would require a long time to hold a hearing and hear all the witnesses.

Mr. OWEN. Mr. Chairman, may I make this suggestion?

The CHAIRMAN. Any suggestion you want to make is welcome.

Mr. OWEN. The legislative processes are well understood by most men who have had any experience with legislation, and it is well known how difficult it is to get a bill considered and passed when there are powerful self-centered interests opposed to it. Therefore I think an amendment to the bill you have is important, in a legislative sense, in order to get action upon the prayer which Mr. Patman has

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been submitting to you. That is what I think. That can be obviated, I think, by the committee itself agreeing to pass upon the bill introduced by Mr. Patman immediately they dispose of the present bill.

The CHAIRMAN. Have you concluded your statement, Senator?

Mr. OWEN. I have.

The CHAIRMAN. We don't want to cut you off.

Mr. OWEN. I have said all I think is necessary. I will be glad to answer any questions. A man often says things which he thinks are understood, and afterward finds they were not understood.

The CHAIRMAN. Mr. Disney wishes to inquire, Senator.

Mr. DISNEY. Senator Owen, in response, I think, to Mr. Knutson's question a little while ago, you rather implied that we now have the legal means in our fiscal system to prevent uncontrolled inflation.

Mr. OWEN. Yes.

Mr. DISNEY. Is that your view?

Mr. OWEN. Yes.

Mr. DISNEY. And that with our further law on the subject?

Mr. OWEN. I think the laws could be improved, but I think even as it stands they have very great power.

Mr. DISNEY. You believe an uncontrolled inflation could be prevented by processes we already have, if they are used?

Mr. OWEN. Yes; I think, of course, they could be improved, and I think the United States ought to unhesitatingly put itself absolutely behind the Federal Reserve System and make itself responsible for all indebtedness and liabilities of the Federal Reserve System. In other words, the Federal Reserve System should be recognized, in explicit terms, as an agency of the United States, behind which is the sovereign power of the United States. One of the reasons why I felt disposed to appear before the committee with regard to this matter of what I call unearned interest was this: That, in my opinion, the sovereign power of the United States was involved, and it is in the exercise of the sovereign power only that money is created by Congress, or through its authority, and I am opposed to any private interest taxing the sovereign power of the United States to make credit for the protection of the people of this country in a great war in which we are involved, or even in peacetimes.

Mr. DISNEY. I have heard it suggested that would put the Government in the banking business.

Mr. OWEN. Put the Government in the banking business?

Mr. DISNEY. I have heard that statement in connection with Mr. Patman's bill.

Mr. OWEN. The Government should leave the banking business to the banks, most emphatically, and the banks should leave the governing business and the exercise of sovereignty to the Government and its Representatives in the Congress of the United States. That is my opinion.

Mr. DISNEY. But the suggestion about the Federal Reserve System, as you may well know, brings out that suggestion, that that may well put the Government in the banking business.

Mr. OWEN. The only thing that will put the Government in the banking business is the failure of the Congress to protect the people of the United States against harm and injury that would come from an unwise administration of our banking system and the creation of

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another great panic. We have had three. I remember the one of 1907 very distinctly, and that I know was deliberately caused. I was told so in terms most explicit by a very well-informed man in the marble room of the Senate of the United States in January 1907, when he whispered in my ear a great secret, that there was going to be a big squeeze put on in stocks and bonds. It came about, but it didn't squeeze me. I had my bank protect itself by taking additional security without squeezing other people.

Mr. DISNEY. Senator, in a word, give me your understanding of the practical aspects of Mr. Patman's proposal under H. R. 1, if you are familiar with that. How would it operate?

Mr. OWEN. It would operate simply by the United States Government, through the Treasury Department, putting its bonds, or certificates of debt, which is better—you are not going to sell these bonds anyway. It would be just a certificate of indebtedness against which the United States would take credit, and pass those credits through the Reserve System, just as it would through any bank, and then the Government could liquidate that indebtedness without penalty as rapidly as the people of the United States could pay the taxes in without suffering. It has been supposed that we are going to have great difficulty in meeting the terrible cost of this war, $210,000,000,000. I beg the committee to look at the letter I wrote to Mr. Spence, of Kentucky, a year or so ago, pointing out the money we lost directly from the panic of 1932–33, and indirectly. Take it all together, it amounted to above $600,000,000,000. Nobody ever questioned the facts. I stated I took it from the record. The potential loss was nearly $400,000,000,000; the actual loss dropping from $81,000,000,000 per annum to $38,000,000,000 per annum, which made a total in 10 years of about $200,000,000,000. This country has the capacity to meet the cost of this war, great as it is, and to liquidate the debt, and to go through it and come out of it the industrial, commercial, financial, and moral leader of the world. Of that I haven't the slightest doubt.

Mr. KNUTSON. Senator, this question is purely for information, and I hope you treat it as such, because I frankly confess, as I told Mr. Patman, that I am a novice in the field of finance. I am purely seeking information, that is all. What is the difference, Senator, between non-interest-bearing notes, such as I understand the Patman bill contemplates—that is what your bill contemplates, is it not, Mr. Patman, non-interest-bearing notes?

Mr. PATMAN. To the Federal Reserve banks only.

Mr. KNUTSON. What is the difference between non-interest-bearing notes and printing-press money?

Mr. OWEN. I am glad you asked me that question, Mr. Congressman. When you speak of the notes to which Mr. Patman refers, the notes of indebtedness of the United States Treasury to the Federal Reserve banks, it merely represents an indebtedness of the United States Government to be liquidated as soon as it can be conveniently done out of the incoming revenues provided by legislation passed by your committee. When you talk about printing-press money, it is a term of derision employed by those who use the term "greenbacks" and use the term "fiat money" in order to express contempt of our currency on the ground that there is nothing behind it. Such criticism ignores the vital fact that our currency daily liquidates itself by exchange from one hand to another and that it is backed by the

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taxing power of the United States and the sovereignty of Congress with its power to contract and expand and to regulate the value of money. The taxing power that goes into untold billions on the productive energies and income of the greatest people in the world. The idea of printing-press money and greenbacks is to discredit what Abraham Lincoln did to save the Union when he issued $386,000,000 of greenbacks in 1862, which were promptly discredited by having a provision put into the law that they were not receivable for interest on the public debt or for the payment of duty on imports, and therefore led the people into the belief that that money ought to be sold at a discount and thus permit a racket by which a few profited at the expense of the many.

Mr. KNUTSON. Would it be your thought that such notes as might be issued, such non-interest-bearing notes as you might issue and place with the Federal Reserve, should be to all intents and purposes negotiable money?

Mr. OWEN. It is credit, Mr. Knutson, which is in the Federal Reserve banks, and against which a check would be drawn by the United States Government.

Mr. KNUTSON. Well——

Mr. OWEN. Just a minute; let me conclude. When that check is passed through a commercial bank, the commercial bank would deposit it in a Reserve bank for payment and it would function exactly as if it were money, exactly as if it were currency, for that matter.

Mr. KNUTSON. Senator, suppose that we issued $5,000,000,000 in non-interest-bearing notes and deposited them with the Federal Reserve banks, suppose the holders of those notes were to immediately pay them back to the Government for income-tax purposes.

Mr. OWEN. The Federal Reserve banks holding that credit would not be called upon to pay income tax to the Government.

Mr. KNUTSON. The member banks would.

Mr. OWEN. The member banks would not have the credits to which we are referring.

Mr. KNUTSON. Wouldn't the member banks be able to draw on this $5,000,000,000 deposit?

Mr. OWEN. No, they wouldn't be able to draw on it, as belonging to them. They could not check on it, if that is what you mean. It belongs to the United States Government.

Mr. KNUTSON. You would freeze them?

Mr. OWEN. I don't freeze them at all. I simply put them to the credit of the United States and check on them, because it belongs to the United States. That is all. It is simply a bank credit created by Uncle Sam and Uncle Sam checks on it.

Mr. KNUTSON. The only experience I have had with banking is to pay interest. I have never been——

Mr. OWEN. As a stockholder of a bank, I congratulate you.

Mr. KNUTSON. I wouldn't say I am not a stockholder, but I am not posted on banking. That is all, Mr. Chairman.

Mr. ROBERTSON. Senator Owen, you will no doubt recall that Tom Paine, of revolutionary fame, said that credit is suspicion gone to sleep——

Mr. OWEN. Credit is what?

Mr. ROBERTSON. That credit is suspicion gone to sleep.

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Mr. OWEN. That is a very interesting epigram. I would like to say this; that at present we have issued billions of Federal Reserve notes that are not in circulation and have gone to sleep and are not paying any interest, but are held by the people in reserve for their own purposes at a time which will follow this war. There are billions of that money issued, in large denominations.

Mr. ROBERTSON. But the reason for that unprecedented amount of Government obligations outstanding in currency, which you say has been issued on the faith and credit of the Government, is that the people have confidence in the credit of the Government, they think the Government is sound and will stay sound, and they have not gotten suspicious of Government credit. You have told us that if we proceed to finance a substantial part of the war cost by the present method of issuing Federal Reserve notes, we will pay a substantial price in interest for that method of financing. On the other hand, if we adopt the plan recommended by you and Mr. Patman, and the banks of the country should call that new issue printing-press money, let us say, or whatever term they want to use to indicate they do not think it is sound money, it would be possible for them, I fear, to create a psychology of fear and suspicion, which once aroused I feel we could never bring within bounds again.

Mr. OWEN. There isn't the slightest possibility of such a thing. No bank would dare do it, for one thing. No bank would want to do it, for another thing, and it would be against the interest of the bank to create a condition that would destroy the value of its own collateral and cause a panic to occur in the country through his expressing suspicion and distrust of the Government.

Mr. ROBERTSON. Well, you may be right.

Mr. OWEN. I am right.

Mr. ROBERTSON. And yet the fact remains, I believe by your own testimony, and likewise that of Mr. Patman, that all the bankers have consistently in the past opposed this method of issuing money.

Mr. OWEN. The banks have not had this particular proposition before them. I think the bankers of this country are just as patriotic as anybody else. What if they are pursuing the natural policy, and following the teachings of the past? That does not argue that they are unpatriotic or unintelligent or unfair in any way, but here we are dealing with the sovereign power of the United States, and you are the custodians of the sovereignty of the United States, and I am telling you that the sovereignty ought not be taxed for the benefit of private individuals, however honorable and worthy they are, and certainly there are no people in the country that deserve more respect than our honored bankers to whom the people entrust all their savings. They are worthy of trust, too. I honor them and I am their friend. But I also believe in the sovereignty of the United States. I believe we ought to cut down this expense by cutting out unearned interest on any more credits extended.

Mr. KNUTSON. Senator, you say, as did Mr. Patman, that the credit of the United States would be behind these notes.

Mr. OWEN. Why, certainly.

Mr. KNUTSON. That being true, why have the Federal Reserve issue these notes? Why not have the Federal Treasury issue them rather than the Federal Reserve?

Mr. OWEN. The Federal what?

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Mr. KNUTSON. The Federal Reserve. Why not have the Federal Treasury issue the notes and put them in circulation.

Mr. OWEN. The Treasury would, in effect, be using this agency as its place of deposit and would be using it so as to distribute its activities throughout the 12 districts according to the respective demands in each of those districts. They need the mechanism and the mechanism has been extremely useful for that purpose. The notes of indebtedness to the Reserve banks proposed by me are in very large denomination and not currency but the basis of bank credit. Over 90 percent of our business is thus transacted by checks.

Mr. KNUTSON. Would the Treasury be unable——

Mr. OWEN. The Treasury would have to set up similar mechanism. They have already got all they need in the Federal Reserve System for that purpose. And it should prove the extreme value of the checking system. It is much better than currency. This Federal Reserve System would take your check in California, without you paying postage, or charging you collection or anything else, and it is transferred at par, so that when you write a check on a valid bank, you just send that as money and it functions as money because it transfers money and can be converted into legal tender on demand.

Mr. KNUTSON. And we have travelers' checks——

Mr. OWEN. That is another form of it.

Mr. KNUTSON. I understand, it is a form of negotiable paper that is good all over the country.

Mr. OWEN. All over the world.

Mr. KNUTSON. But you do feel it is necessary to operate the plan proposed in H. R. 1 through the Federal Reserve?

Mr. OWEN. Oh, yes.

Mr. KNUTSON. It couldn't be done through the Treasury?

Mr. OWEN. It could be, but it would be expensive and awkward and require a reorganization. It is unnecessary to do that, because they have a wonderful organization now.

The CHAIRMAN. Thank you, Senator.

Mr. OWEN. Well, I am much obliged to you gentlemen, for your patience with one of your old brothers, and I appreciate coming in and having a little chat with you. I know you will act with patriotism and with intelligence.

The CHAIRMAN. We thank both you and Mr. Patman for your appearance and the information given the committee.

Mr. PATMAN. Thank you, Mr. Chairman. May I express the hope that if you do not pass on this in connection with this bill that you give me a hearing on it some time in the future?

The CHAIRMAN. Mr. Voorhis said he would like about 10 minutes.

STATEMENT OF HON. JERRY VOORHIS, A REPRESENTATIVE IN CONGRESS FROM THE STATE OF CALIFORNIA BEFORE THE COMMITTEE ON WAYS AND MEANS, HOUSE OF REPRESENTATIVES, FEBRUARY 13, 1943

Mr. VOORHIS. I would just like to say that I agree in substantial part with what has been said by Mr. Patman and Senator Owen. I want to read first, if I may, two sentences from a little pamphlet written by Winthrop W. Aldrich, chairman of the board of directors

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of the Chase National Bank. Mr. Aldrich says in this pamphlet, which is entitled "Economic Implications of Internal Public Debts:"

Through 1942 commercial banks absorbed about $19,000,000,000 of Government obligations, which represented 38 percent of the increase in the total debt; through 1943 it is estimated that the commercial banking system, that is the commercial banks, plus the 12 Federal Reserve banks, may have to absorb $40,000,000,000 of Government obligations, an amount equal to about 60 percent of the estimated increase in the total Federal debt.

Now, Mr. Chairman, I submit that that means (1) that 38 percent in 1943 and 60 percent in 1944 of the increase in debt of the Nation will be the result of the increase of brand new money by the commercial banks of the country. It will not be the result of the transfer of actual money possessed by the people from them to the Government in the purchase of obligations. In the second place, it will mean a very high degree of concentration of ownership of this public debt in the hands of the commercial banks; and, in the third place, I agree thoroughly with what has been said to the effect that interest paid upon obligations paid for with new money created by private banking institutions is unearned interest. If the public debt, as Mr. Patman pointed out, is $210,000,000,000 in June of 1944, the interest on that at 2½ percent would be $5,250,000,000, and the interest on 40 percent of that, roughly the amount held by commercial banks, would be $2,100,000,000. That amount can be saved by the general method proposed by the gentleman from Texas, Mr. Patman.

My conception is that the ideal banking and monetary system is one in which banks lend money, but do not create it, and in which the Government creates money, but does not lend it. I think the piling up of huge amounts of Government obligations in the banks makes a tendency for the banks to create money for the Government instead of engaging in the commercial banking business, and I think that tendency has been present for quite a long time. This is an inflationary proposition as long as these bonds are sold to commercial banks, and it seems to me of tremendous consequence.

I might say that I have a bill almost exactly similar to that by Mr. Patman, which I introduced on the first day of the session. The thing that would happen were this policy pursued, would be this: The Treasury would issue non-interest-bearing certificates and sell them to the Federal Reserve banks. The Federal Reserve banks would purchase them with exactly the same credit they now use to purchase interest-bearing obligations. The Government would then secure a credit with the Federal Reserve against which it would draw checks to pay its bills.

Ideally we should pay for as much of this war as possible out of taxes and the sale of bonds to individuals and nonfinancial corporations, or even financial corporations, if they can pay for them with their own money and not with the credit of the people.

Mr. ROBERTSON. Will you yield for a question there?

Mr. VOORHIS. Certainly, Mr. Robertson.

Mr. ROBERTSON. Do you contend the sale of bonds to a commercial bank has an inflationary trend, even more inflationary than the issuance by our Government of the same amount of money?

Mr. VOORHIS. I think it might, for this reason: When you sell to a bank an interest-bearing obligation, that bond then becomes collateral for the issuance of Federal Reserve notes if the bank wants to use it

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for that purpose. It can, in effect, be reserves in the hands of that bank. If, on the other hand, you adopt the plan that is proposed here this morning and sell non-interest-bearing obligations to the Federal Reserve banks, it would be at the same time quite possible to provide for an increase in the reserve requirements in the banks, and thus control inflation by that means, and that has been suggested and outlined by Senator Owen in testimony before another committee.

In other words, the control of inflation is one question which must be dealt with, as the Senator pointed out. It is true to the extent anybody creates new money it is inflationary, of course, and substantially, therefore, I would agree with you, but I wouldn't agree, if by your question, you mean that the adoption of the proposal advanced here this morning by Mr. Patman and Senator Owen would be any harder to control, if, indeed, as hard, as the present system.

What I was about to say when you asked your question was that my own view is that we should get as close as we can to paying for this war out of taxes and legitimate bond sales. That is the only real way we can control inflation, and the extent to which we fail to do that, is the real inflationary danger, rather than farm prices, for example. But if we are to let anybody create new money the people of this Nation ought not be charged an interest burden of $2,100,000,000, by 1944 on that new money, because that credit belongs to the people in the first place.

Mr. ROBERTSON. Isn't it true that for many years the theory of sound money has been that currency, whether anchored to gold or not, is sound if money is issued solely with relation to the amount of money work that is to be done?

Mr. VOORHIS. Right. I agree thoroughly with that.

Mr. ROBERTSON. Your proposal will issue money to be used for the payment of debt.

Mr. VOORHIS. No, sir. May I, first of all, agree a little more in detail with your first statement, that the soundness of money depends upon the relationship of the volume of that money with the work it is to do, which, stated in other words, means the soundness of money depends upon the relationship between the volume of money and the amount of goods and services produced in the Nation. At the present time we are in a war; we are in a war which requires colossal expenditures, and to the extent we are in that war the kind of monetary policies which I would advocate in peacetime should be precisely reversed. In other words, whereas in peacetime I would urge that the Government, as a deliberate policy, put in circulation and create enough money to keep up with the expansion of production, today the expansion of production of supplies, civilian goods, is partially restricted, so that sound monetary policy means we should keep down to the greatest possible extent the creation of new money, and we should, on the contrary, tax and sell bonds to the greatest extent possible, in order to prevent the volume of buying power from exceeding the supply of civilian goods, consumer goods. But the fact remains, as Mr. Aldrich himself has pointed out, that that has not happened, that it is not likely to happen, that we are likely to let the commercial banks create a huge amount of money for the purchase of Government obligations, and then draw interest on that credit, which was the people's credit. My contention is that to the extent that we fail to pay for

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the war out of taxes or legitimate bond sales, the people should not be charged with the interest-bearing debt for the margin between the cost of the war on the one hand and the degree to which we come up to paying for it currently.

Mr. ROBERTSON. Do we have a lot of hoarding of money at the present time?

Mr. VOORHIS. I couldn't answer that. Many people feel that there is a considerable amount of hoarding of money.

Mr. ROBERTSON. And is it not also true that bank deposits are at an unprecedented height?

Mr. VOORHIS. That is true.

Mr. ROBERTSON. That is check money, is it not?

Mr. VOORHIS. That is correct.

Mr. ROBERTSON. If we have enough money in the amount of check money and plus an unprecedented amount of money in circulation, and the hoarding of money that is not in circulation, I feel it is a fair conclusion that we already have outstanding more money than is necessary to do the money work of the Nation, and that the issuance of further money is money issued to pay debts and not to do money work.

Mr. VOORHIS. But, Mr. Robertson, every dime of the $19,000,000,000 of bonds mentioned by Mr. Aldrich here as having been sold to the commercial banks in 1942, every dime of that was additional deposits created by the banks.

Mr. ROBERTSON. That makes it inflationary.

Mr. VOORHIS. That is true, so that the inflationary question is neither here nor there so far as this proposition is concerned.

Mr. ROBERTSON. I believe it is here.

Mr. DISNEY. Mr. Knutson asked a question of Senator Owen a minute ago. He inquired why not let the process of issuance be the Treasury of the United States, of notes without interest. What have you to say about that?

Mr. VOORHIS. Well, there would be two difficulties. In the first place, it is conceivable that in the future we may have a condition in the Nation where it would be desirable to reduce the volume of money outstanding. I earnestly hope we are not going to go in for a program of deflation after this war, like we did after the last war, because I think it was disastrous. But we may conceivably have a situation where we do have a surplus of revenues coming into the Treasury over the needs of the Government. If that happened, and if we had non-interest-bearing certificates in the hands of the Federal Reserve, you could then pay off some of those certificates, as it was sound fiscal policy to do so. Of course, you could also retire currency and accomplish the same result, if you wanted to, but I think the best reason for doing it the way Mr. Patman suggested and that I have suggested—with modesty I will say—the best argument for it is, it is customary in this country for us to do business, not with a huge volume of cash money, but to do it by means of bank deposits and check money, and people are more accustomed to that than they are to the use of very large amounts of cash.

Furthermore, the amount of cash that will actually be used by people is determined by their convenience. I mean, in other words, they will deposit it in the bank if they don't want to use it, and the

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amount of cash currency that circulates is determined by the convenience of our trade, rather than any other circumstances, so that I do not think it would particularly make sense to put out many billions of dollars of currency when you don't need to; there isn't any use going to the expense of printing it. And, furthermore, I think it is a much more understandable method to use precisely the method that you now use for the sale of interest-bearing bonds, when you handle the non-interest-bearing securities. Mr. Patman has suggested that is what you would be doing—you would be selling them to the Federal Reserve in precisely the same way you sell interest-bearing bonds to them, and they buy them with the credit of the American people.

The CHAIRMAN. Thank you, Mr. Voorhis.

Mr. PATMAN. Mr. Chairman, I am inserting herewith excerpts from the hearing before the Committee on Banking and Currency, United States Senate, 78th Congress, 1st session, on S. 700, February 17, 1943, as follows:

Mr. ECCLES. * * * Now if there had been any desire to create an inflationary process on the part of the Government, or the Federal Reserve, we did not have to use this particular mechanism. The Thomas amendment has been on the books since 1933, and has never been used. We never had any thought or intention of using it.

Senator TOBEY. At the same time when you try to repeal it, they protest very bitterly. They say they will not use it, but do not repeal it.

Mr. ECCLES. So far as I am concerned, I have no objection to repealing it.

Senator TOBEY. It is still a sword of Damocles handing up there?

Mr. ECCLES. Yes. But inflation will never come from the issuance of currency.

Senator TOBEY. I think you are right.

Mr. ECCLES. The only way inflation can come is through the Congress of the United States appropriating money. Now, there is no other way you can get inflation, except the way that Congress appropriates money and fails to provide means of collecting it.

Senator TOBEY. It seems to me, Mr. Eccles—and I make this prediction, that some of our printing-press money friends, fiat-money friends, will use your words this morning to plague you, wherein you speak of these notes and the Government's promise to pay. If we put behind them Government bonds, that would have been a promise to pay. Taking that away from the context entirely, they will quote Marriner S. Eccles and say that is the law.

Mr. ECCLES. I have a statement, if you would like to have it. I wrote Mr. Patman and I have debated this issue with him time and time again——

Senator TOBEY. I know you have.

Mr. ECCLES. On the subject of orthodox means of financing, and you can see just what Mr. Patman proposes and then what is the effect of it. That in itself would not create inflation if you did just what Mr. Patman proposes. That is not the inflationary route.

The objection to what the Patmanites propose is that you would create a huge volume of deposits; you would create a like amount of excess funds on the part of the banks; but you would have the banks without any earnings assets. With all of the present work and time and expense involved, you would either have to provide the banks with an income to replace the bond interest, or you would not have any banks. So the point is whether you provide them with the income through orthodox means, which is the cheapest and the easiest and the best way to do it. Mr. Patman cannot save the Government anything by his proposal.

It will be noticed that Mr. Eccles states that my proposal will not cause inflation. He contends that the banks should be paid for servicing money that is put into circulation and that the interest method is a good way to do it. In other words, if a bank buys a $1,000,000 bond, providing for 2 percent interest, the bank under

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present methods creates the money to buy this $1,000,000 bond. The bank will thereafter collect $20,000 a year interest from the Government on the bond. My suggestion is that instead of having the banks collect this interest from the Government each year, which will put the Government in a position of never being able to pay out, it would be much better for the Federal Reserve banks to take non-interest-bearing bonds and create the money for the Treasury. Then when the money is transferred to the banks, let the depositors and others, who obtain services from the bank, pay the cost of the service. It is true it will be more expensive to those who now obtain the services of the banks, but at the same time it will enable the Government to get out of debt; and after all we should look at it from the Government's standpoint.

I want to ask one or two questions that won't take so much time.

We hear a lot about the debt limit. Do you know when this country or Congress first adopted the policy of fixing a debt limit, Mr. Eccles?

Mr. Eccles. No; I do not.

Mr. Patman. I never could see why a debt limit was necessary to be fixed by Congress, as long as Congress makes appropriations. And even though it exceeded the debt limit, it would be the latest expression on the subject and would automatically increase it. Have you given consideration to that?

Mr. Eccles. I agree with you it does not make much sense to have a debt limit when Congress makes the appropriations that make necessary the public debt.

Mr. Patman. Therefore, you cannot understand why all this talk about a debt limit?

Mr. Wolcott. Will you yield to me there?

Mr. Patman. Yes, sir.

Mr. Wolcott. When the first debt limit bill was passed, there was a differential between the amount of bonded indebtedness and total indebtedness and it was undoubtedly passed as a check upon the Treasury, to limit the Treasury in the issuance of bonds. With the removal of that differential back in 1936, when the debt was converted, from that time on our action each year has been nonsensical.

Mr. Patman. In raising the debt limit?

Mr. Wolcott. Yes. When we removed the differential, we destroyed the whole effectiveness of the act.

Mr. Patman. Now, one question on this Trans-America Corporation. Have you given consideration to that set-up, Mr. Eccles?

Mr. Eccles. In what way?

Mr. Patman. In the way of it being a menace to the country?

Mr. Eccles. Well, I would not want to say it has been a menace to the country.

Mr. Patman. Or it adopts a bad policy that, if pursued, would eventually become a menace?

Mr. Eccles. Are you referring to the Trans-America policy, or the Bank of America?

Mr. Patman. I mean just exactly what I said—Trans-America.

Mr. Eccles. I have given considerable thought to the operations and the development of Trans-America.

Mr. Patman. Do you look upon that as a wholesome undertaking?

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Mr. ECCLES. No, I do not. I agree that Trans-America, in their purchase of stock of banks and in their purchase of stock of corporations that have nothing whatever to do with banks is pursuing what, to my mind, is an improper and unsound policy.

Mr. PATMAN. Do not you have some power and authority to deal with that situation?

Mr. ECCLES. We do not.

Mr. PATMAN. Have you ever asked for any?

Mr. ECCLES. No, we have not.

Mr. PATMAN. Or do you expect to?

Mr. ECCLES. Well, so far as the Board is concerned, I would think, if any power were asked for to deal with that situation, it should not be done by the Reserve System alone, but the Comptroller's office, having supervision over national banks, and the F. D. I. C., carrying the insurance of all member banks should be included in the program.

Mr. PATMAN. Have you ever had any discussion of any program along that line?

Mr. ECCLES. Several years ago we discussed this whole situation with the Trans-America people. The three Federal supervisory agencies met and discussed the whole question of the operation of Trans-America with the Trans-America people.

Mr. GIFFORD. Governor Eccles, we have heard a good deal about this. If I give my note or bond to my local bank and they finally discount it with you, you have to pay them the money for it, whatever it is worth?

Mr. ECCLES. Have to what?

Mr. GIFFORD. If my local bank comes to you, you have to create the credit or give them the money for that, do you not?

Mr. ECCLES. That is the Federal Reserve banks?

Mr. GIFFORD. Yes.

Mr. PATMAN. A member bank.

Mr. ECCLES. Yes; they have to provide them with credit.

Mr. GIFFORD. And we say "we" create money when it is created by the banks. Well, they create money on my note; if the Federal bank does not have money enough on hand, they create money. And when the Government wants money and comes to you, you create money or you give them credit and the Government spends the money it has in that greater amount or uses it in canceling bonds.

What I want to know is, Mr. Patman, some years ago, felt like they should issue printed money without giving a note or a bond for that same debt, and I want to ask, Mr. Patman, are you now willing at least to give the Federal Reserve a bond when you get the money?

Mr. PATMAN. Oh, that is a matter that does not make any difference; you give credit on the books just like when you pass the amount to the credit of the bank.

Mr. GIFFORD. Do you not know the bond is going to be the same; that would be the whole obligation?

Mr. PATMAN. Yes; there should be a certificate of indebtedness, which is commonly what we call bonds.

Mr. GIFFORD. I am talking about the due date.

Mr. PATMAN. Yes; I want a due date so that we will pay off this national debt in 40 years.

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Mr. GIFFORD. I am going to ask Governor Eccles about the 3½ billion dollars. I do not know why our Government, which is now so much in competition with private folks in business, can borrow by printing, or get its money for nothing, when I have to pay interest; I do not know why we should give them any power that the citizens do not have.

Mr. PATMAN. There is a difference.

Mr. GIFFORD. There is no difference, except they have better credit than I do; that is all.

Mr. PATMAN. When the miners went out in the hills and mountains and dug out the gold and silver with their hands, they worked for that gold and silver and, if the Government wanted to borrow and use it, the Government should have paid interest on it, because they actually worked for it. It was theirs. But now, when you need more money you just artificially create it.

Mr. GIFFORD. They created gold and silver in such great quantity that they wanted the Government to buy it; they went in daily to work the lode and send it in. But what has the 3½ billion of capital stock got to do with the expense of the large banks? Governor Eccles has shown you that the interest is declining and their 3½ billions would not get so much interest from the Government.

Mr. PATMAN. But what has that to do with the banks' activities?

Mr. GIFFORD. It is what they get on their capital stock.

Mr. PATMAN. Let me pursue that view. If we borrowed money from a foreign government, we should pay interest on it; but here is the Government of the United States that is solvent, that creates the money it has, and we place ourselves in the idiotic position of giving the banks Federal money and bonds—in practice that is what it means—both Government obligations, and tell the bank "Now, you pay out the money upon which there is no interest and keep the bonds and you will draw interest on those bonds from now on."

Mr. GIFFORD. When I give my note, the Federal Reserve bank creates money.

Mr. PATMAN. Or creates Government credit.

Mr. GIFFORD. And when the bank collects the money on that credit, it has to pay it back again.

Mr. PATMAN. But it is paying the money to the Government itself.

Mr. FORD. The United States Government, we will say, takes over the Federal Reserve, and it issues money and there is no interest or anything else. That money goes out into circulation and the Government spends all the money it wants to and has nothing to pay, and it expects it to lay there and the Treasury pay back 2½ percent a year and, in 40 years, it is paid off. But here is the State of California which goes out into the market and wants to get $5,000,000; it has to pay 3 or 4 percent, or whatever the rate is, and it begins to wonder "why the United States Government is getting its money for nothing; why cannot we get it?" Then the city of Los Angeles comes along and it has to borrow $5,000,000. It finds the State has clearance on its State obligations and says "Why cannot we; why should the Federal Government get money for nothing when we cannot?" Then it comes down to the individual "Why cannot I go and get money?" And if you are suggesting we eliminate the cost of it, then it is just a question of making money and giving it to use to anybody who needs it.

Mr. PATMAN. That is not the question at all.

Mr. FORD. That is what it amounts to.

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Mr. PATMAN. The Government creates; the Government is sovereign, and the State of California is not sovereign.

Mr. FORD. Oh, yes; it is, and Texas is.

Mr. PATMAN. It is a sovereign State, but it is not the sovereign all-powerful government with money creating powers like the United States Government.

Mr. WOLCOTT. Might I say for the record that this whole matter is very thoroughly covered and very intelligently discussed in Samuel Crowther's new book entitled "Time to Inquire" in chapter 3. I would suggest to the committee that they read that, and that is probably an answer to the whole question.

Mr. PATMAN. I apologize to the committee for taking so much time, and I thank Mr. Eccles for his patience with me.

Mr. WOLCOTT. I do not think you need to apologize. I think we have enjoyed this very much. For once in the last 5 years we are talking about finance banking. We have not had much finance banking in the last 3 or 4 years, and it is very interesting.

Mr. PATMAN. With this observation, I will give up the witness. I will ask Mr. Eccles to use that same diligence in trying to find a plan to save the taxpayers' money on a large part of this debt that he has used on trying to get Congress to pass tax laws, and I hope when he does that, he will be able to submit a plan pretty soon that will enable us to pay off this debt in 40 years.

Mr. FORD. If Congress would pass some tax laws, you would not have to borrow so much money.

Mr. SMITH. I wonder if Mr. Eccles would care to explain the cause for the reduction of interest, or earnings, of 1942 as compared with 1941, that is, of the banks.

Mr. ECCLES. I think I can only express an opinion, and of course the causes would vary with different banks, but the smaller banks, the middle-sized banks in particular, have lost loans. The loans bore a substantially higher interest rate than the Government bonds which they purchased.

The farmers have been able to reduce their debts with the country banks. Installment credit has declined very greatly. Many banks were carrying installment paper, and the amount of installment credit outstanding has declined over the past 2 years close to $4,000,000,000. Home mortgage lending has likewise been declining. Loans on the books of the banks are being reduced. Business concerns, many of them, are paying off their indebtedness as a result of the reduction in the accounts outstanding, and as a result of reductions in their inventories. All this reduction of debt by private borrowers has been made possible by the large expansion of expenditures financed by the increase in the debt on the part of the Government which has created a large amount of deposits.

In other words, the Government's borrowing from the banks did create a lot of money, and that money as disbursed went into the hands of corporations and individuals who in turn used those funds to pay off indebtedness to the banks where they had indebtedness to the banks. The reduction in the aggregate indebtedness bearing a higher rate of interest was a large factor, I think, in reducing their net earnings. Add to that factor the increased cost factor due to increase in the number of personnel, increase in compensation, and decreased efficiency.

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Mr. SMITH. It is your opinion, then, that there has been an absolute shift as well as a relative shift from private financing by banks to Government financing. Would that be a fair statement?

Mr. ECCLES. That is right.

Mr. SMITH. Absolute shift as well as a relative shift. Just one more question. I wonder if you would insert in the record figures showing Government securities as of—I think you gave the date, December 31, 1942, classified as to commercial banks; that is, member banks and nonmember banks taken together, commercial banks and savings banks; No. 2, as to direct and indirect, or guaranteed Government obligations; No. 3, as to interest charges and maturities on these several securities. Would that be advisable?

Mr. ECCLES. I do not know. Will you repeat that?

Mr. SMITH. Classified as to commercial banks and savings banks. Now, commercial banks would include both member banks and nonmember banks.

Then as to direct and indirect, or guaranteed Government obligations.

Mr. ECCLES. You mean as to those separately?

Mr. SMITH. Yes.

Mr. ECCLES. What difference would that make? I do not know whether we could get that separately.

Mr. SMITH. I believe that you have that.

Mr. ECCLES. Maybe they have the statistical information, but you want it separately, the amount guaranteed and the amount of direct obligations by the various kinds of banks, groups of banks?

Mr. SMITH. That is right, and then as to interest charges and maturities of the several obligations held by the banks. Would that be feasible?

Mr. ECCLES. I do not know whether that information is available or not. I have not seen it. We might get an estimate of it, but the portfolios of the banks are changing very rapidly, and at some particular date I suppose it would be possible to figure out what the interest income on those bonds is, but that interest income on the bonds might not reflect the earnings that the banks would get on those bonds.

Mr. SMITH. I do not care about the earnings, just so it is stated, the interest paid and all the particular securities and the maturities. I imagine that you have that classified in that manner.

Mr. ECCLES. If it is available we will put it in the record.

(The information referred to is as follows:)

Holdings of United States Government obligations, direct and guaranteed, by all banks except Federal Reserve banks

[In thousands of dollars]

Member banks:		
Direct	$35,006,436	
Guaranteed	2,539,753	
		37,546,189
Nonmember banks excluding mutual savings banks		8,832,865
Mutual savings banks excluding 3 member banks		4,562,143
All banks		45,941,197

A break-down of nonmember bank holdings of Government securities according to direct obligations and guaranteed obligations, respectively, is not available.

Interest income from securities.—Bank reports do not distinguish between interest on Government securities and interest on other securities. The accompany-

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ing table, however, gives some estimates of the amount of income derived from these two classes of securities by all insured commercial banks and by member banks for the years 1941 and 1942. It should be noted that the figures for 1942 represent a compounding of estimates, since the banks' reports of earnings for the year 1942 have not yet been tabulated, and the rough estimate for the year 1942 is based largely on reports of member banks for the first half of the year.

Although bank reports do not distinguish between earnings on Government securities and earnings on other securities, a rough estimate has also been made of the average rate of return that banks received in 1941 and 1942 on Government securities. As nearly as can be figured United States Government security portfolios of all banks at the end of 1941 were producing revenue at the rate of about 1¼ percent. The average rate on those acquired during 1942 was about 1 percent, or possibly slightly more. It should be noted that the securities held by banks at the end of 1941 were a mixture of partially tax-exempt and taxable issues but that those acquired during 1942 were all taxable. This fact tends to minimize the disparity between the two rates which otherwise would be greater, of course, because of the large proportion of Treasury bills and certificates sold to banks during 1942. The securities bought by banks in the December campaign had an average yield of 1.14 percent, but other securities, particularly the bills and certificates, sold at other times during the year reduced this average.

Interest income from securities

[In millions of dollars]

	1941 (partly estimated)			1942 (roughly estimated)		
	Total	U. S. Government direct and guaranteed	Other securities	Total	U. S. Government direct and guaranteed	Other securities
Insured commercial banks	509	304	205	610	410	200
Member banks	445	272	173	540	370	170
Insured nonmember banks	64	32	32	70	40	30

Mr. SMITH. I have one more question. Does this matter of the banks handling so much of Government securities place a considerable burden upon the banks? It does, does it not?

Mr. ECCLES. You mean handling the securities that are sold to the public?

Mr. SMITH. The bonds and the securities which the banks take directly, that is, those securities that are financed through the banks. That is a considerable burden on the banks, is it not?

Mr. ECCLES. I would not say it is a burden. No; it is no burden to the banks to buy these Government securities and hold them.

Mr. SMITH. No burden at all?

Mr. ECCLES. No.

Mr. SMITH. The only reason I asked the question, in connection with Mr. Patman's questioning as to the actual work of handling these bonds—what is it worth to the banks—and it is your idea, Mr. Patman, that they get this interest without doing a great deal of work, is that your idea?

Mr. PATMAN. I did not get that question.

Mr. SMITH. They get this interest without really doing much work for it, is that your idea?

Mr. PATMAN. A large part of it is unearned interest.

Mr. SMITH. I do not know myself. I am merely asking for information.

Mr. FORD. May I ask a question. To what extent is it unearned? If a bank buys $1,000,000 of bonds, what does it buy with? It is a

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bookkeeping transaction, that is true, and it puts the bonds away, but it has to take out of its deposits, or something, that $100,000, does it not?

Mr. ECCLES. It creates the $100,000 and it buys the $100,000 of bonds, but there is no assurance that the deposits might not be shifted somewhere else, and the bank then may have to sell the bonds, as they did in the last war at substantial losses.

Mr. PATMAN. They cannot do it under the present situation.

Mr. ECCLES. At the end of the last war, of course, the bonds that they did purchase, the long-term bonds, were sold by many banks at substantial losses. But it is not any burden to the banks to purchase and hold the securities. Where the burden to the banking system comes in is that where the Government spends the money represented by the deposits created when the banks buy the securities, that money goes out and increases the volume of deposits which the banks handle.

For instance, today, the banks of this country are handling twice, or more, I suppose, the volume of business that was true 3 or 4 years ago. Take the Federal Reserve banks, for instance, which reflect the activities of the commercial banks, and the commercial banks reflect the employment and general activity of the country. The personnel of the Federal Reserve banks has increased approximately 50 percent in the last 2 or 3 years. Now, the personnel of the private bank has likewise increased. The compensation paid to their employees has increased and the efficiency of the employees, as a general rule, has decreased. Now, that is merely one item of increased expense that the banks have had to incur as the result of this increased activity.

Mr. SMITH. That ties in again with the first question I asked about the cause of this reduction in earnings. I am just wondering. My question naturally implied the carrying through of the entire transaction. I mean all that is involved in the taking over by the banks of these Government securities. That will include their redeposit after they are checked out by the Government, finding their way back into the banking system again. It is that point that I think is rather important here so far as these deposits are concerned. You already indicate that there is less private business; consequently, less opportunity for earning the normal earnings than previously, and consequently it would seem to me if you figured that out, carried that clear through, you would find a considerable burden placed upon the banking system as the result of that financing of Government obligations through the banks.

Mr. ECCLES. I agree with you that if you carry it through——

Mr. CRAWFORD. Governor Eccles, we have had an enormous amount of correspondence with banks out through the country, at least I have, particularly the north and central west and the northwest, to the effect that the R. A. C. C. was greatly interfering with their earnings through absorbing away from them first-class loans, we will say, in the agricultural areas in particular. Have your studies brought you to where you care to make a comment on that, what effect it has had?

Mr. ECCLES. We have received a good many letters from bankers throughout the country complaining about that competition, and I think there is considerable justification in the complaints. I received a letter from a committee of Congress which is considering a bill with reference to the R. A. C. C., and I expect to reply to that letter stating my views, or possibly the Board's views with reference to this question.

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I would like to supplement what I said to Congressman Patman with reference to the banks' increased costs and the reduction in their earnings. The banks, as you possibly all know, have undertaken to sell bonds and stamps, and in many cases they are handling the pay roll allotment plans. Many of these War Saving bonds are issued and distributed through commercial banks. That has greatly increased, that one item alone, the expense of the personnel of the banking system as a whole. The banks get no compensation whatever for that service. They were recently requested to handle ration coupons for which they are supposed to be compensated at their actual out-of-pocket cost. That would not include, of course, the distribution of overhead expenses, taxes, rentals, and such expenses as that.

They cash without cost millions of Government checks. I would say that in the great majority of cases the people that cash those checks carry no accounts with the banks. That is a very big item of expense, the handling and the collection of all those checks.

The banks have been subject to the foreign-funds control of the Treasury. You will recall they froze all foreign funds in the banks, and these funds could only be disbursed on the basis of regulations issued by the Treasury. That required considerable extra cost on the part of the banks, particularly the larger banks where there was a substantial amount of foreign funds held.

Those are some of the items of service that the banks are rendering to the Government in the war effort without compensation and which are responsible for a considerable amount of increase in costs.

Mr. SMITH. The Government has to pay for this service in one way or another, either by direct appropriations, or through interest. That is correct, is it not?

Mr. ECCLES. That is right.

Mr. PATMAN. Oh, no; you don't agree with that. The Government has to pay it, you don't agree with that. The people that have the deposits pay it.

Mr. ECCLES. As a practical matter, I do not think that is possible.

Mr. HULL. Are we going to have the committee here in time to act on this bill or not?

The CHAIRMAN. We cannot vote on the bill today. The members are insisting on going to the House. We will have to meet tomorrow.

Governor Eccles, will you be available for the meeting tomorrow?

Mr. ECCLES. I will be available, if we can get this bill out. I hope, Mr. Chairman, that we can conclude this tomorrow.

The CHAIRMAN. I am hoping that we can. I do not see any way of getting it up to the House before Friday.

Mr. ECCLES. The passage of this bill promptly, if possible, is quite urgent. If it is passed, it would immediately have the effect of reducing the reserve requirements by quite a substantial amount.

Mr. PATMAN. You have the power to do that now.

Mr. ECCLES. I was going to say, it would reduce the reserve requirements on these Treasury balances, and it would make it unnecessary for the System to buy $400,000,000 or $500,000,000 of securities, possibly, which would be the equivalent of the effect it would have. The uncertainty of this thing makes our operation extremely difficult. There is an other point that I want to make on a question that Mr.

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Patman raised the other day when I did not make it, and I want it to be in the record because it is very important, and it is this:

The policy of the Open Market Committee of the Reserve System is to keep the excess reserves of the banks down, to provide the banks with just sufficient reserves to enable them to purchase the securities which are not placed outside of the banks, and not to give to the banks the larger reserves, the redundancy of reserves, which might become necessary if this bill is not passed, and which might put the banks in a position where they would be trying to buy a lot of securities on the market. Just as soon as this drive was over, and the funds started to go back to the public, let us assume that this bill had not passed and that the proceeds from this financing were not deposited in the war loan accounts with the banks but came directly from the community to the Treasury. The Federal Reserve would offset the loss of those funds in the community by reducing reserve requirements or by an open-market operation. Then as these funds were disbursed by the Treasury and went back into the community the banks would have excess reserves of substantial proportions which they would, no doubt, immediately want to use in the purchase of securities in the open market.

The Open Market Committee would have much less control than they should have in order to exercise an adequate influence upon the reserve positions of the banks. In other words, we do not want the banks to have reserves in excess of what they need to finance that part of the war expense that cannot be financed outside the banks.

The CHAIRMAN. Gentlemen, I do not think this bill can be gotten out sooner than Friday of this week, and the members desire to have another day for consideration.

Mr. PATMAN. And I want to hear Mr. Morgenthau, because the Treasury is more interested in this than anyone else.

Mr. ECCLES. That is not true, Mr. Patman. As far as the Treasury is concerned, they make the offering and it is up to the Open Market Committee to so manage the market as to assure the success of the drive. Now, the real burden is on the Federal Reserve. The Treasury will get the funds one way or the other, and they have much less concern than we do in this.

The CHAIRMAN. I am sure the members of the committee fully appreciate the responsibility that the Federal Reserve has; there is no question about that; and the members of the committee want to report this bill as soon as we can, but we have to get away now and will come back tomorrow at 10:30.

(The committee thereupon adjourned until tomorrow, April 6, 1943, at 10:30 a. m.)

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FEDERAL RESERVE ACT AMENDMENT

WEDNESDAY, APRIL 7, 1943

House of Representatives,
Committee on Banking and Currency,
Washington, D. C.

The committee met, pursuant to adjournment, at 10:45 a. m., Hon. Henry B. Steagall (chairman) presiding.

The Chairman. The committee will come to order.

Mr. Smith has a matter to which he wishes to call our attention for just a moment.

STATEMENT OF HON. FREDERICK C. SMITH, A REPRESENTATIVE IN CONGRESS FROM THE STATE OF OHIO

Mr. Smith. Mr. Chairman and gentlemen, before the commiittee proceeds with consideration of H. R. 1699, I wonder if the committee would take up H. R. 2206 and possibly consider disposing of it by an amendment.

When H. R. 2206 first came up for consideration by the committee, it appeared to me that it did not provide as much security for the veteran as it should. I was inclined to think that a provision might be added to the bill providing for some relief to the veteran with respect to accrued interest charges on the mortgages that might take place during his service. It was my thought that the veteran should be entitled to at least some substantial extension of time in which he might pay such accrued interest.

I have taken this matter up with Mr. Ketchum, who represents the Veterans of Foreign Wars, and with Mr. Sullivan, who represents the American Legion in matters of this kind. It seems that they are inclined to agree with me that the veteran could be given more protection than the bill as at present written provides. However, they both seem to think that if anything is done along this line, it should be done by an amendment to the Soldiers' and Sailors' Civil Relief Act rather than to H. R. 2206.

I, therefore, ask that this bill be considered by the committee and recommended for passage immediately.

Mr. Patman. This does not relate to the bill we have under consideration this morning?

Mr. Smith. No. I think we are all agreed on this.

The Chairman. I think I can explain briefly what this is. If you will remember, it is to amend the Federal Housing Act so as to take care of any delinquent payments by the mortgagor for the protection of the mortgagee in extending mortgages of that kind for members of the armed forces as long as they are in the service. Dr. Smith raised

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a question about it. It is a little difficult to understand from a practical viewpoint, but I think it can be handled, and everybody, I think, will agree to it.

Mr. PATMAN. That is the one about which Mr. Kean wrote a letter?

Mr. KEAN. Yes. I did not think it was coming up so soon.

The CHAIRMAN. Dr. Smith wanted to make known his position on account of his suggestion the other day.

Mr. SMITH. My point the other day was that it gave protection to the man holding the mortgage but possibly did not give such protection as I thought was deserving to the serviceman involved, and my thought was to offer an amendment to take care of that phase of it. After going into the matter carefully with the veterans' organizations, I find that this is perhaps not the proper place for an amendment. There is an inclination on their part to wish to do that which I would wish to accomplish under this bill, but they think it should be offered as an amendment to another bill. Therefore, I am calling up this bill and asking for its passage immediately.

The CHAIRMAN. Unless the committee wishes to report it by agreement, we will pass it over. Dr. Smith just wanted to make known his position about it. We will take it up when we have time. We do not wish to keep these gentlemen waiting. If we can report it by consent immediately, we had better report it.

At this time we will hear from Governor Eccles.

STATEMENT OF MARRINER S. ECCLES, CHAIRMAN, BOARD OF GOVERNORS, FEDERAL RESERVE SYSTEM

The CHAIRMAN. Governor Eccles, the proposition is: Should we place State banks in the same category as national banks and member banks with respect to the practice of the Federal Reserve System in taking over any bonds that the banks purchase? In other words, with respect to Government bonds, should the Federal Reserve offer the same cushion and protection to State banks, as to Government bonds, that it does to member banks?

Mr. ECCLES. Well, it does now.

The CHAIRMAN. Well, now, does it?

Mr. ECCLES. Yes.

Mr. PATMAN. It does not have to in practice.

Mr. ECCLES. No; but it does as a matter of practice. What the Federal Reserve is interested in is not so much the member banks or the State banks; we are interested in sustaining the Government bond market and getting wide distribution of Government securities.

The CHAIRMAN. I am sure of that, but let me ask you: You are doing this by regulation? There is no law requiring it?

Mr. ECCLES. There is no law requiring that we do it for national banks either.

The CHAIRMAN. That is what I mean. There is no law requiring it to be done for anybody. It is a question of monetary management?

Mr. ECCLES. Naturally.

The CHAIRMAN. It is purely a regulation of the Federal Reserve?

Mr. ECCLES. It is a matter of policy that is adopted by the Open Market Committee in some instances; in other cases it is a matter of policy adopted by the Board. For instance, take the establishment of what we call a buying rate for Treasury bills. The Open Market

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Committee established a buying rate for Treasury bills and instructed every Federal Reserve bank to buy bills on the basis of three-eighths whenever those bills were offered. In the case of borrowing rates on Government securities, every Reserve bank right after the war started in Europe in 1939 agreed to loan to any bank an amount equal to par on Government securities. It was not only to member banks; it was to all banks. The rate to both member and nonmember banks for loans secured by Government bonds is 1 percent. Now, that is a matter of policy; it is not a matter of statute at all. It seems to me that it cannot be otherwise than a matter of policy to be adopted by the Federal Reserve banks with the approval of the Board. Buying policy must be directed, of course, by the Open Market Committee.

The CHAIRMAN. To what extent have State banks availed themselves of this privilege?

Mr. ECCLES. I do not think that either members or nonmembers have availed themselves to any substantial extent of the privilege of borrowing from the Reserve banks. They have preferred, if they needed funds, to sell their Government securities in the market; and, of course, the Open Market Committee has purchased Government securities offered in the market, so there has been a ready market for their securities, and all banks have preferred to sell their securities, if they needed to, rather than borrow. The very fact, however, that they know they can borrow has, I am sure, helped stabilize the Government market and has, I think, given the banks greater confidence in their holdings of Government securities.

I think that some of the nonmember banks—I do not have the information available—have sold to the Reserve banks of their districts bills at the three-eighths buying rate. They are given an option to buy those bills back on the basis of the three-eighths rate at any time during the life of the bills. So, they can sell a bill to the bank today and buy it back tomorrow, if today they are short of funds and tomorrow they have funds. That makes it a very elastic means of enabling a bank to meet its reserve needs, whether the bank is a member or nonmember.

The CHAIRMAN. You say there has been no discrimination?

Mr. PATMAN. The point is that they have not had occasion to use that privilege. There has been no necessity for its use. But suppose that when this war is over there should be an emergency. The regulation could be changed to where the national banks or member banks would be favored in the way that the regulation now provides, and the State banks might be excluded from purchasing.

Mr. ECCLES. Do you mean a State nonmember bank?

Mr. PATMAN. That is right; a State nonmember bank.

The CHAIRMAN. This bill would take care of that by saying that there should be no discrimination and that the privileges should be both as to bills and other obligations.

Mr. PATMAN. As far as Government obligations are concerned.

The CHAIRMAN. Yes; make it all obligations.

Mr. PATMAN. No, not all; all Government obligations.

Mr. ECCLES. The minute you do that, you are going to give to the nonmember bank the privileges of membership.

The CHAIRMAN. No.

Mr. PATMAN. No; just as to Government bonds only.

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Mr. Eccles. Just as to their ability to borrow on Government bonds.

The Chairman. Just for the war financing program; the Government's own obligations. I understand how the Federal Reserve feels about extending the ordinary privileges of member banks to nonmember banks that do not assume any of the obligations. What we are talking about is giving them the same facilities that are extended to member banks in connection with Government obligations.

Mr. Eccles. I am perfectly sure that there is no need to put any such provision in the statute because, as a practical matter, no Federal Reserve bank or Open Market Committee would do otherwise. The whole purpose of the special provisions for advancing funds against Government securities or for establishing a buying rate for securities is to stabilize the Government's credit in the securities market.

The Chairman. We understand that fully. Perhaps in the present situation there would not be a necessity for any action at all. But let me remind you of what happened following the other war. I know of instances in which little State banks that really were not able to carry Government obligations at all at the rate that they received, were caught with a lot of those bonds on hand, that they disposed of at close to 80 cents on the dollar. We do not want a thing like that ever to happen again. We know you do not.

Mr. Eccles. That was true not only of the State banks or nonmember banks; that was true of the member banks likewise. You must remember that at the end of the last war there was no such thing as open-market operation. It was a technique of central banking that was unknown in this country.

The Chairman. That was in the law then, was it not?

Mr. Eccles. No, it was not in the law. There was no Open Market Committee then.

Mr. Patman. I may suggest that the Open Market Committee would run to the Federal Reserve, and if you had a Federal Reserve Board or Open Market Committee that wanted to force all the banks to the Federal Reserve System, they would have a mighty good hammer after this is over by saying, "You will not have the rediscount privilege. The Open Market Committee will not buy your bonds at certain rates."

Mr. Eccles. Let me answer that, Mr. Patman, because I think that that just is not an accurate statement of what the facts are. Just assume a nonmember bank could not borrow from the Reserve System. It could sell its securities in the open market.

Mr. Patman. That is, with the Open Market Committee?

Mr. Eccles. The Open Market Committee would have to withdraw completely from the market and let the Government bond market go to pot.

Mr. Patman. The national banks would be taken care of through the rediscount privilege?

Mr. Eccles. That is right; but it does not seem to me to make sense to say that the Open Market Committee would refuse to buy securities to stabilize the market while the member banks could obtain loans at par on Government securities. In the first place, banks are loath to borrow from the Reserve banks. There has been practically no borrowing since 1932 from the Reserve banks. Banks would prefer to liquidate their securities or other assets rather than show bills

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payable in their statements. The experience that banks had from 1929 to 1933 in borrowing, and the effect that the showing of bills payable in their statements had on the public in bringing about runs on the banks, has caused the banks to resist all borrowing from the Reserve banks.

Mr. PATMAN. If there is no objection, and you say it will always be done——

Mr. ECCLES. In the first place, it would require that the matter go over to the Senate, and that would delay this bill.

Mr. PATMAN. There would not be any delay. They could accept an amendment in 10 minutes.

Mr. ECCLES. What you are proposing is very controversial; and it would, in effect, I think, kill the bill. I think it is unnecessary.

Mr. PATMAN. Do you mean to say that if something that you say is going to be done anyway by regulation—there is no doubt about it—is proposed to be officially enacted into law, it cannot be passed?

Mr. ECCLES. I do not say it is going to be done; that the Reserve banks would always give this privilege of special borrowing on Government bonds to nonmember banks. I do say that, so far as the market for Government securities is concerned, nonmember banks could sell their securities in the market, and the Open Market Committee would have to purchase those securities. It may well be that the special borrowing privilege given to nonmember banks, that now exists, would not be continued indefinitely.

Mr. PATMAN. A 1-percent reduction in the price of Government bonds will wipe out the capital structure of every bank in this Nation today. They hold more than $35,000,000,000 in Government bonds. No, I am incorrect; that would be 10 percent. It would take a 10-percent reduction to do that.

Mr. ECCLES. That is right. Of course, that is looking at it on the basis that everything is going to be sold tomorrow.

Mr. PATMAN. When this war is over, everyone will have Government bonds. Probably everybody will be loaded up with Government bonds. Of course, people will be cashing their bonds. The State nonmember banks can be placed in a very embarrassing position if the Open Market Committee and the Federal Reserve Board are not in sympathy with them, so I think we ought to provide against that now. We do not know who will be in charge of the Open Market Committee, and we do not know who will be in charge of the Federal Reserve Board. I think that we should provide against that possibility now by law.

Mr. ECCLES. You are taking a position here that the Open Market Committee, which is, of course, the authority that determines the purchase and sale of securities on the open market, could discriminate against one class of banks. As a matter of fact, in buying in the market, we have not the remotest idea of who has sold the securities. The securities may come from individuals, corporations, member banks, or nonmember banks.

Mr. PATMAN. But, Mr. Eccles, do not overlook the fact that they would not have to discriminate; they could just fail to buy for a few days.

Mr. ECCLES. Buy anybody's securities?

Mr. PATMAN. Yes; and they would not be discriminating; but the effect would be to discriminate against the nonmember State banks.

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Miss SUMNER. But would your amendment prevent that?

Mr. PATMAN. Yes. They would be required to permit a nonmember State bank to have the rediscount privilege on Government obligations only, on the theory that they have induced them to load up with Government bonds during this emergency. Therefore, we should give them some protection.

Miss SUMNER. What is the advantage, then, of being a member of the Federal Reserve System if everybody else has that privilege?

Mr. PATMAN. There are many other advantages.

Miss SUMNER. That is the principal advantage.

Mr. PATMAN. No; not on Government obligations. Other obligations will not be included. This will be on Government securities only.

Miss SUMNER. This is the principal obligation they use, is it not, Mr. Eccles?

Mr. ECCLES. They do not use much of any kind. They have not done any substantial borrowing for 10 years.

Mr. KUNKEL. Under your philosophy of this proposal, does it not mean that we here today are deciding that we know more about what should be done in the future than a board or an Open Market Committee and the Chairman of the Federal Reserve, who have been studying the matter, will know, in the light of everything that has transpired between now and the time this situation might arise?

Mr. PATMAN. I think it is more a question of whether we are willing to trust these people with the State banks or nonmember State banks when we fairly well know that they are not in sympathy with them and there is strong possibility that we might have someone on the Open Market Committee wipe out the securities, and Congress would not have time to act before it was done, because it would be done so quickly. I think that common prudence should dictate to us that we should guard against any such possibility, especially when we are inducing the State banks to load up with these bonds during the emergency.

Mr. ECCLES. Mr. Patman, it is discretionary on the part of 12 different Reserve banks whether or not they will make a loan to a member bank or a nonmember bank. If a Reserve bank feels that a bank is borrowing funds on Government securities for the purpose of supporting some other speculative activity, it may decline to loan a member bank on Government securities; it may decline likewise to loan a nonmember bank on Government securities.

Mr. PATMAN. That is right.

Mr. ECCLES. So, the whole question of whether or not a Federal Reserve bank will make an advance on Government securities or on any other paper to a member or nonmember bank is left up to the discretion of the board of directors of each of the 12 banks. Their rate of discount is subject to the approval of the Federal Reserve Board.

Mr. PATMAN. Right there is where we do not want discrimination. When the directors of a Federal Reserve bank, as in Dallas, Tex., agree to accept the paper—the Government paper—of the national bank, we want to require them to give the same privilege to the State banks or nonmember banks only to the extent of Government securities.

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Mr. Eccles. But what if they make a loan to a bank, and they find that that bank is using the credit it is getting on Government securities to support stock market activity?

Mr. Patman. You would not do that. You are saying something that is not material.

Mr. Eccles. The whole thing is discretionary with the banks.

Mr. Patman. If they let the national bank have it, they will let the State bank have it under their rules—under the same rule—on Government paper only, and they exclude this speculative paper.

Mr. Eccles. They are permitted to do it. In other words, the Federal Reserve Board has approved a program, which is national in scope, which is permissive as to making advances on Government securities to member banks as well as to nonmember banks at the uniform rate.

Mr. Patman. Do you think that is a good rate?

Mr. Eccles. Yes, I do.

Mr. Patman. We want to write it into law to protect these banks when the emergency is over; you want it to remain only as a regulation.

Mr. Eccles. I think it is desirable to leave it that way. The Federal Reserve Board is an agency of Congress, and at such time as the Federal Reserve Board fails to perform its duty in what is considered by Congress to be in the public interest, Congress can certainly remove them and change the law at any time it sees fit. But I certainly feel that this is not the time or the place to inject this matter, which I think should be given more consideration than I feel can be given at this time. I would like to see this bill passed as it is, and the matter that you are proposing be discussed as another bill, because I do think there are many angles to it that I, not contemplating this discussion, may have overlooked, and I do not feel prepared today to say that it should be made a part of this bill.

The Chairman. If I understand the situation, it is all embraced in the realm of regulatory provisions by the Federal Reserve bank and the open market committee. While these securities are being sold, and during the period when the difficulties of that problem may become accentuated, you propose to put the State banks on the same basis as member banks with respect to all transactions where Government securities or Government obligations are held.

Mr. Eccles. As I say, I see no reason to put, we will say, a State nonmember bank as a matter of statutory requirement in that position any more than we would put other public lending institutions, such as mutual savings banks, insurance companies, and building and loan companies, in that position. They all have public funds and are encouraged to invest their funds in Government securities.

The Chairman. I think I need not remind you that it is important that all our banks—and, of course, those in charge of the banks recognize it is important and are going to be governed by it in their transactions—be kept more liquid than other lending institutions and individuals, because banks are trustees of public funds that they must account for on demand—their deposits. That puts them in a different category. If they are caught with unusual investments—investments

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in unusual amounts—to aid the Government in its financing program, it seems to me that you are doing the right thing in treating them as you do member banks for that purpose. If you are going to do that and recognize that right, why should we not say, not that you shall not do anything for a State bank or make any advance or loan to a State bank or accord it any rediscount privilege, or anything like that, but that insofar as advances upon the obligations of the Government are concerned they shall have the same privilege as member banks, without discrimination? It seems to me that that would help in financing the war program. We feel some responsibility toward all the banks of the country in this program.

If I understand the situation, the banks are carrying something like half—that is, they are taking care of something like half—of the Government financing activities at this time. If one class of our banks found themselves lacking the ability to secure privileges another class of our banks have, it would throw things out of joint, and it might become troublesome.

Mr. Eccles. As a practical matter, all institutions that carry the funds of the public and invest in Government securities—such as insurance companies, mutual savings banks, building and loan societies, and also individuals—are entitled to some protection on their investment. Now, the Banking Act of 1935 gives to a public body the power and, likewise, it seems to me, the authority and the obligation to stabilize, so far as they are able to do so, the money-market situation. That can, it seems to me, be done only through their operation in the Government security market. I am sure that the nonmember banks as well as the member banks will use the open market to dispose of securities to meet any withdrawal of deposits, and the open-market committee will have to assume responsibility for the stabilization, it seems to me, of that market. It is not likely to be stabilized through the amount of money that either the member or nonmember banks are likely to borrow from the Federal Reserve banks.

The Chairman. But is it not desirable that the nonmember banks participate in this program to a larger extent than they are doing?

Mr. Eccles. It is desirable, Mr. Chairman, that not only the nonmember banks but the public generally and all institutions should participate in it just as fully as possible.

The one element of danger in the Government security market would be a failure to prevent inflation—that is, an undue inflation. To the extent that prices are permitted to go up and the purchasing power of the dollar diminishes, to that extent is the entire Government security market jeopardized, just as any fixed-income investment would be jeopardized. There possibly is no way of overcoming the inflationary effects of a greatly increased living cost on any fixed-interest-bearing obligations.

Mr. Rolph. In the event the policy in the future should go against the nonmember State banks, could they not achieve the same end through their correspondent relations with banks which are members?

Mr. Eccles. That is where they would go. That is where they have gone in the past, and I am sure that that is exactly where they would go in the future, rather than to the Federal Reserve bank, because they have had little or no relations with the Federal Reserve

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bank. They do not know the personnel, and they have had no dealings with them. Should they decide to borrow rather than to sell their securities, they very likely would go to the city correspondent where they carry their reserves.

Mr. ROLPH. Should they choose to turn their Government securities over to a correspondent bank, could not the correspondent bank furnish them to the Federal Reserve bank?

Mr. ECCLES. It could.

Mr. CRAWFORD. Without having any thought of bringing this phase of it into the banking machinery, I think it is important to bring it out at this moment. The Treasury has laid down the proposition that if we are to avoid inflation, the securities issued by the Treasury, necessary to finance our dollar appropriations, and after we have paid our taxes, must be purchased by the private citizen, the proprietorship, the partnership, the corporation, and lending institutions other than commercial banks. To that end, these sources have been investing their reserve funds in Government securities.

I have been watching the balance sheets of our industrial corporations—large, intermediate, and small—with a great deal of interest from this standpoint, because it appears to me that our industrial corporations are going to put literally billions of dollars into Government securities, and the possibility of these corporations adjusting themselves to the postwar operations will be subject to their ability to finance themselves out of, we will say, the ownership of Government securities. So, Government securities are spread over all these institutions in such manner as to present to us problems very dissimilar to what we have had heretofore, as we move into the postwar period. I just want to mention that in connection with the fact that you have pointed out that these lending institutions that are not member or nonmember banks are filling their portfolios with Government securities.

The CHAIRMAN. It occurs to me that we have embarked on a discussion here that had better be held in executive session. I just make the suggestion to you, Governor Eccles, that perhaps we should conclude discussion of this bill in executive session.

Mr. ECCLES. That is all right with me. I would like to make this point; that the proposal that the chairman and Mr. Patman have made is something that should be given more thought and consideration than certainly I have had time to give it while sitting here. It is a matter that I think the other members of the Board should have an opportunity to give some thought to. It may be that the suggestions you have made may be acceptable, but I do feel that to bring them in at this time, in connection with this bill, that I think is rather urgent and should be gotten out, is a mistake. I do not want it to appear that I am opposing necessarily your proposal. I might, if I had an opportunity to consider all the aspects of it, not have an objection to it. At first thought, as I have tried to express my views today, it does not seem to be necessary or called for.

The CHAIRMAN. I am going to express the hope that we will get this bill out today, and I now make the suggestion that the committee go into executive session.

(At 11:40 a. m., the committee went into executive session.)

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