

MINUTES OF SPECIAL MEETING

of the

FEDERAL ADVISORY COUNCIL

April 10, 1935

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A special meeting of the Federal Advisory Council was convened in Room 736 of the Mayflower Hotel, Washington, D. C., on April 10, 1935, at 9:30 A. M., the President, Mr. Smith, in the Chair.

Present:

Mr. Thomas M. Steele	District No. 1
Mr. James H. Perkins	District No. 2
Mr. Howard A. Loeb	District No. 3
Mr. Arthur E. Braun	District No. 4
Mr. Charles M. Gohen	District No. 5
Mr. H. Lane Young	District No. 6
Mr. Solomon A. Smith	District No. 7
Mr. Walter W. Smith	District No. 8
Mr. Theodore Wold	District No. 9
Mr. E. E. Mullaney	District No. 10
(Alternate for Mr. Kemper)	
Mr. Joseph H. Frost	District No. 11
Mr. Walter Lichtenstein	Secretary

Absent:

Mr. M. A. Arnold	District No. 12
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The minutes of the special meeting of the Council of March 28-29, 1935, were read by the Secretary and approved.

The Secretary made a statement in reference to his interview on April 2 with Governor Eccles at the time of delivering the report of the Council, dated April 1, 1935.

After some discussion the meeting adjourned at 10:30 A. M.

WALTER LICHTENSTEIN,

Secretary.

MINUTES OF SPECIAL MEETING OF THE FEDERAL ADVISORY COUNCIL

April 10, 1935.

The special meeting of the Federal Advisory Council was reconvened in the office of Governor Eccles, Washington Building, Washington, D. C., at 11:15 A. M.

Present:

Governor Marriner S. Eccles, and Dr. E. A. Goldenweiser, Director, Division of Research and Statistics, Federal Reserve Board.

Members of the Federal Advisory Council:

Mr. Walter W. Smith, President; Mr. Howard A. Loeb, Vice President; Messrs. T. M. Steele, J. H. Perkins, A. E. Braun, C. M. Gohen, H. L. Young, S. A. Smith, Theodore Wold, E. E. Mullaney, J. H. Frost, and Walter Lichtenstein, Secretary.

Governor Eccles made a statement in which he said that the objects of Title II of the proposed Banking Act of 1935 were to:

1. Fix more definitely the responsibility for monetary policy.
2. Improve machinery of the System in order to avoid conflicts and prevent cleavage, especially between Federal Reserve agent and governor in the respective Federal Reserve banks.
3. Remove from Federal Reserve banks and member banks unnecessary restrictions hampering recovery and which have proved dangerous in the past.

A lengthy discussion took place covering the whole report which the Council had made.

The meeting adjourned at 3:25 P. M.

WALTER LICHTENSTEIN,

Secretary.

MINUTES OF SPECIAL MEETING OF THE FEDERAL ADVISORY COUNCIL

April 10, 1935.

The special meeting of the Federal Advisory Council was reconvened in Room 736 of the Mayflower Hotel, Washington, D. C., at 4:15 P. M., the President, Mr. Smith, in the Chair.

Present: Mr. Walter W. Smith, President; Mr. Howard A. Loeb, Vice President; Messrs. T. M. Steele, J. H. Perkins, A. E. Braun, C. M. Gohen, H. L. Young, S. A. Smith, Theodore Wold, E. E. Mullaney, J. H. Frost, and Walter Lichtenstein, Secretary.

It was decided to go page by page through the whole of Title II of the report and decide what changes, if any, the Council desired to make in the report which it had previously presented to Governor Eccles.

By a vote of six to four, Messrs. Steele, Braun, S. A. Smith, and Frost voting in the negative, it was decided to change page 13 of the report, so that the governor of each Federal Reserve bank will have to be approved anew by the Federal Reserve Board every three years.

On page 14 of the report it was voted to add the amendment proposed by Governor Eccles, striking out lines 14-16 on page 40 of H. R. 5357.

It was decided to make no changes in pages 15-18, inclusive, of the report as originally presented to Governor Eccles.

On page 19 of the report a slight verbal change was voted.

On page 20 of the report some changes in phraseology were voted.

It was decided to make no changes on page 21 of the report as originally presented to Governor Eccles.

On page 22 of the report it was voted to omit the words "in exceptional and exigent circumstances and".

It was decided to make no changes on pages 23 to 25, inclusive, of the report as originally presented to Governor Eccles.

At 5:25 P. M. Mr. Gohen left the meeting.

Page 26. It was voted to provide that real estate loans made for a period of twelve years should be paid off at the rate of five per centum per annum.

It was voted to adopt the report as amended.

The Secretary was instructed to inform Governor Eccles of the changes made in the original report of the Council and to supply him with copies of these changes.

The Secretary was also instructed to inform Governor Eccles that after a period of five days had elapsed copies of the final report of the Council would be delivered to the Chairmen of the committees on Banking and Currency of the Senate and House of Representatives.

The meeting adjourned at 5:50 P. M.

WALTER LICHTENSTEIN,

Secretary.

STATEMENT OF THE
FEDERAL ADVISORY COUNCIL

ON

S. 1715, H. R. 5357

(BANKING ACT OF 1935)

APRIL 10, 1935

Title I

Title I of the proposed Banking Act of 1935 amends Section 12 B. of the Federal Reserve Act which deals with the subject of deposit insurance. The Federal Advisory Council approves this Title of the proposed bill, but suggests the following changes, the underscored portion representing new material:

Section 8, page 10, change to read as follows:

"By striking out subsection (h) and inserting in lieu thereof the following:

'(h) (1) The assessment rate shall be one-twelfth of 1 per centum per annum upon the total amount of the liability of the insured bank for deposits (according to the definition of the term 'deposit' in and pursuant to paragraph (11) of subsection (c) of this section, without any deduction for indebtedness of depositors) based on the daily average determined from such total-as-of-the-close-of-business for the six months ending on the last day of June and the last day of December of each year: Provided, That the board of directors from time to time may fix a lower rate or may determine that there shall be no assessment or may provide for a refund or credit by a percentage upon the last annual assessment rate not-exceeding-50-per-centum thereof, when it finds that such action will provide or leave, as the case may be, adequate revenue and reserves for the Corporation having due regard to experience and conditions affecting banks. In computing the total deposits for the purpose of this subsection any bank may deduct from the amount of its gross deposits the amounts of balances due from other banks (except balances due from foreign banks, and required reserve balances carried with Federal Reserve Banks) including cash items with Federal Reserve banks and other banks in process of collection, checks on other banks in the same place, and exchange for clearing houses. The rate or percentage so fixed shall be applicable to all insured banks, except that the board of directors on a similar finding, from time to time, may provide that the rate so fixed shall be applicable to insured mutual savings banks only or may provide a different rate applicable to mutual savings banks only.

Explanation

The above changes provide that the assessment shall be based upon the average deposits for the six months' period, instead of the total deposits as of June 30th and Dec. 31st, thereby providing a more stable basis, inasmuch as the deposits for a single day might be affected by special temporary conditions.

It was also felt that the Board of Directors of the Federal Deposit Insurance Corporation should have the power to decrease the assessment in accordance with their judgment, even by eliminating it entirely when the fund reaches such volume as they may believe will serve its purpose.

The definition of total deposits appearing in Title III, Section 323, has been here inserted, except that excess reserve balances with Federal Reserve banks are treated the same as balances due from other banks.

Section 8, subsection (h), page 10, change to read as follows:

" (2) On or before the 15th day of July of each year, each insured bank shall file with the corporation a certified statement under oath showing the ~~total~~ average amount of its total liability liabilities for deposits ~~as of the close of business~~ for the six months ended on the 30th day of June last preceding, computed as provided in subsection (h) (1) of this section, and shall pay to the corporation the portion of the annual assessment equal to one-half of the annual rate fixed by this subsection (h) multiplied by its said ~~total~~ average deposits ~~on the date for which such statement is made~~ as shown by such statement. On or before the 15th day of January of each year each insured bank shall file a like statement showing the ~~total~~ average of its total liability liabilities for deposits for the six months ended as of the close of business on the 31st day of December last preceding, computed as provided in subsection (h) (1) of this section, and shall pay to the corporation the portion of the annual assessment equal to one-half of the annual rate fixed by this subsection (h) multiplied by its said ~~total~~ average deposits ~~on the date for which such statement is made~~ as shown by such statement.

Explanation

Section 8, change the proviso in paragraph (5) line 24, page 12, to read as follows:

Provided, That where a fiduciary bank deposits any of such trust funds in another insured banks, ~~the amount so held by other insured banks on deposit on the last day of the month preceding~~ such fiduciary bank may upon the filing of the certified statement required by paragraph (2) of subsection (h) of this section, deduct the average daily amount of such trust funds so deposited which for the purpose of such statement shall not be considered to be a deposit liability of the fiduciary bank, but shall be considered a deposit liability of the bank in which such funds are so deposited by such fiduciary bank.

Explanation

To conform with changes recommended in Section 8 basing assessments on average daily deposits rather than deposits at December 31st and June 30th.

Section 13 (5), page 30, change as follows:

"If any depositor in a closed bank shall fail to claim his insured deposit from the Corporation, or shall fail to claim or arrange to continue the transferred deposit with the new bank or other bank assuming liability therefor within ~~one~~ two years after the appointment of the receiver for the closed bank, all rights of the depositor against the Corporation in respect to the insured deposit or against the new bank and such other bank in respect to the transferred deposit shall be barred, and all rights of the depositor against the closed bank, its shareholders or the receivership estate to which the Corporation may have become subrogated shall thereupon revert to the depositor. The amount of any transferred deposits not claimed within said ~~one~~ two-year period, shall be refunded to the Corporation."

Explanation

It is believed that one year is not sufficient time for depositors to make their claims, in view of the difficulties which sometimes exist of ascertaining ownership of deposits.

Section 18, page 34, change to read as follows:

"By adding at the end of subsection (r) the following:

'The board of directors, from time to time, shall gather information and data and shall make investigations and reports upon the organization, operation, closing, reopening, reorganization, and consolidation of banks, banking practices ~~and-management~~, and the security of depositors ~~and-adequacy-of-service-to-borrowers~~. The board of directors, in any annual or special report to Congress, shall report its findings and make such recommendations and requests as it shall find necessary and appropriate for the purpose of carrying out the purpose of this section and fully providing for all of the obligations of the Corporation'."

Explanation

It is felt that the elimination of the clause indicated above will not impair the proper functions of the Federal Deposit Insurance Corporation. The elimination is made to avoid duplication of examinations.

Section 22 (3), page 36, change to read as follows:

"No insured bank shall pay any dividends on its capital stock while it remains in default in the payment of any assessment due to the Corporation; and any director or officer of any insured bank, who with knowledge of such default participates in the declaration or payment of any such dividend shall, upon conviction, be fined not more than \$1,000 or imprisoned not more than one year, or both."

Explanation

It would seem obvious that no penal liability should attach to a director or officer who participates in the declaration of a dividend without knowledge of such default. Such a provision would be contrary to all penal statutes which only make liable those who wilfully do an act which is unlawful.

Section 22 (5), page 36, change to read as follows:

"Each insured bank shall provide ~~such~~ protection and indemnity against burglary, fidelity, and other similar insurable losses in such amounts as the board of directors by regulation may require adequately to reimburse the bank for such losses.

Whenever any insured bank fails to comply with any such regulation the corporation may contract for such protection and indemnity and add the cost thereof to the assessment otherwise payable by such bank.

Explanation

The above changes clarify the apparent intent of this section and would eliminate the possibility that the section, as now worded, might confer upon the Federal Deposit Insurance Corporation the power to discriminate between insurance companies.

TITLE II

The Federal Advisory Council has considered most carefully Title II of the proposed Banking Act of 1935. The provisions of Title II change fundamentally in many respects the Federal Reserve System as it has existed since its inception. The Council questions whether there is any emergency at the present time which makes it necessary to enact into law the provisions of Title II without further careful consideration and study. The Council wishes to point out that in recent years so many changes have been made in the whole fiscal and financial structure of the country that there may well be some real concern entertained as to whether a proper relationship between the various parts has been maintained. These doubts are not concerned with this or that detail of Title II. Twenty-five years ago, before the Federal Reserve Act was enacted, a series of studies was undertaken by a national commission. Since then many different types of financial institutions have sprung up, so that it would seem most desirable to have another detailed study made analogous to the one which preceded the enactment of the Federal Reserve Act.

In spite of what has been said, if the Government deems it advisable to enact at this time legislation making fundamental changes in the Federal Reserve System, the Federal Advisory Council after a careful study of the proposed measure suggests certain amendments which it regards as fundamental. The Council deems it essential to preserve the autonomy of the regional Federal Reserve banks as provided in the original Act and in order to maintain this principle, it makes certain suggestions which will be detailed below.

Title II may be divided into three general subjects:

The first has to do with the control of money, the organizations set up to exercise this control, and the powers to be employed. The control over money may be maintained by a change in the discount rate or by the increase or decrease of the percentage of reserves kept by member banks with the Federal Reserve banks, or finally by operations in the open market, i.e., by the purchase or sale of Government bonds by the Federal Reserve banks.

The exercise of these powers is of the greatest importance to the commerce, industry, and agriculture of the country. As far as possible the members of the body to whom is to be entrusted this vast authority should be free of wrongful influences whether political or financial. While, therefore, there should be independence of judgment, it is recognized that there is a proper relationship between governmental financial policies and the action of those authorities controlling the banking system of the country and that it is desirable that there be close cooperation and harmony between the two. With this in mind, the Federal Advisory Council recommends the following changes in the proposed law:

1. That the Secretary of the Treasury and the Comptroller of the Currency cease to be members of the Federal Reserve Board.
2. That the Board be reduced to five members.
3. That the governor and members be appointed for fifteen years, but compelled to retire at the age of seventy.
4. That the Federal Reserve bank governors be appointed by the directors of the Federal Reserve banks with the approval of the Federal Reserve Board, but that after the approval of the Board has once been obtained, the governor may be re-elected by the Board of the bank without approval by the Board.
5. That a committee composed of the members of the Federal Reserve Board and four of the bank governors, selected by the twelve governors, shall be given the power to fix the discount rate, the percentage of reserves, and direct the open-market policies of the banks.

The second general subject dealt with in Title II is the liberalization of rediscount privileges. The Council recommends the re-enactment of Section 10 (b) as detailed below.

The third general subject dealt with in Title II is that of real estate loans. There is unquestionably need of some effective private agency to finance the requirements of real estate. The difficulty is that banks are in a very different position from other institutions; they have limited capital, and such capital as they have must be protected as far as possible.

It is the opinion of the Council that a further study of this subject should be made, but if a law is to be passed at the present time the Council feels that the power should be given to the several Federal Reserve banks to lower the percentage of value up to which a bank may loan, and to lower from time to time the percentage of individual bank capital and surplus which may be represented by loans secured by real estate in banks within its district. Any percentage so fixed by the Federal Reserve bank should be subject to change from time to time, upon ten days notice, and it should be the duty of the bank to establish such percentages with a view to preventing the undue use of bank loans for the speculative carrying of real estate. The Federal Reserve bank should have power to direct any member bank to refrain from further increase of its loans secured by real estate for any period up to one year, under penalty of suspension of all rediscount privileges at the Federal Reserve bank. The Council also feels that the present provisions of the law, restricting the area within which banks should be permitted to make real estate loans, should be incorporated in this act, i.e., within the Federal Reserve District or within a radius of 100 miles of the place in which such bank is located.

The detailed changes necessary to carry out these recommendations will follow, the underscored portion representing new material.

The proposed amendments, if accepted, would take from Title II the features which the Council conceives to be the most dangerous. Without them the Council feels that prior to the independent study which is earlier suggested, Title II must be disapproved in its entirety.

Section 201, page 39, change paragraph beginning at line 9, to read as follows:

"Effective ninety days after the enactment of the Act containing this amendment, the offices of Governor and chairman of the board of directors of each Federal Reserve Bank shall be combined. The Governor shall be the chief executive officer of the bank and shall be appointed annually by the board of directors, ~~subject to the approval of the Federal Reserve Board.~~ He shall not take office for the first term until approved by the Federal Reserve Board and thereupon and thereafter he shall be subject to the approval by the Federal Reserve Board every three years, and after such approval he shall be appointed and reappointed by the Federal Reserve Board as one of the Class C directors of the bank," etc.

Explanation

The Federal Advisory Council originally proposed that the Federal Reserve Board should have the right to confirm the governors of the respective Federal Reserve banks only at the time of the initial election of such a governor and that thereafter the governors should be re-elected by the boards of directors of the local Federal Reserve banks without the necessity of re-approval by the Federal Reserve Board. In view, however, of the amendment suggested by Governor Eccles in the second paragraph on page 40 of H. R. 5357 which would turn over to the governors of the respective Federal Reserve banks all the functions at present exercised by the Federal Reserve agents, it seemed to the Council that there was merit in the suggestion of the Governor that the Board have the right periodically to pass on the question as to whether a given governor was the one whom the Board desired to have as its representative.

Section 201. Page 40. Strike out the sentence beginning line 14, reading as follows: ~~"All duties prescribed by law for the Federal Reserve agent shall be performed by such person as the Federal Reserve Board shall designate"~~ and substitute the following: "All duties prescribed by law for the Federal Reserve agent shall be performed by the Governor of the bank or by such other person or persons as he may designate."

Explanation

This is in accord with Governor Eccles' suggestion and will turn over to the governor of the Federal Reserve bank all the functions at present exercised by the Federal Reserve agent of such bank.

Section 201. Page 40. Eliminate paragraph beginning at line 17 reading as follows:

~~"No member of the Board of Directors of a Federal Reserve bank, other than the Governor and Vice Governor, shall serve as a director for more than two consecutive terms of three years each. This shall not prevent the present incumbents from serving out the remainder of their present terms."~~

Explanation

It is felt that the inclusion of this paragraph might deprive many of the regional Reserve banks of the services of directors who are invaluable on account of their experience gained by length of service, especially in such districts where the number of men most qualified to serve as directors may be limited. At the present time, a number of the Federal Reserve banks have already adopted restrictions similar to the one proposed in the bill, and it is suggested to the Council that this matter might well be left to the discretion of each Federal Reserve bank.

Section 203, page 41, of the Banking Act of 1935, change to amend Section 10 of the Federal Reserve Act, to read as follows:

A Federal Reserve Board is hereby created, which shall consist of ~~eight~~ six members ~~including the Secretary of the Treasury and the Comptroller of the Currency who shall be members ex-officio and six members~~ appointed by the President of the United States, by and with the advice and consent of the Senate; provided, however, that whenever the membership shall be reduced by death, resignation, expiration of term or other cause, the vacancy thus created shall not be filled if it would increase the membership to more than five. In selecting the ~~six~~ six appointive members of the Federal Reserve Board the President shall choose persons well qualified by education or experience or both to participate in the formulation of national economic and monetary policies, not more than one of ~~the appointive members~~ whom shall be selected from any one Federal Reserve district, except that this limitation shall not apply to the selection of the Governor. ~~The President shall have due regard to a fair representation of the financial, agricultural, industrial, and commercial interests, and geographical divisions of the country.~~ The ~~six~~ six members of the Federal Reserve Board ~~appointed by the President and confirmed as aforesaid~~ shall devote their entire time to the business of the Federal Reserve Board and shall each receive ~~the sum of \$12,000 payable monthly together with actual necessary traveling expenses, and the Comptroller of the Currency as ex-officio member of the Federal Reserve Board, shall, in addition to the salary now paid him as Comptroller of the Currency receive the sum of \$7,000 annually for his services as a member of said Board.~~ ~~The appointive members of the Federal Reserve Board appointed after July 1, 1935, shall each receive~~ a salary at the same rate as that of the heads of

the executive departments who are members of the President's Cabinet, together with actual necessary traveling expenses. Each ~~appointive~~ member of the Federal Reserve Board heretofore appointed may retire from active service upon reaching the age of seventy or at any time thereafter, and all members hereafter appointed shall retire upon reaching the age of seventy. Each member of the Board so retired from active service who shall have served for at least five years shall receive, during the remainder of his life retirement pay in an amount equal to the annual salary paid to appointive members prior to the enactment of the Act containing this amendment: Provided, That if he shall not have served as much as ~~twelve~~ fifteen years his retirement pay shall be at the rate of ~~one-twelfth~~ fifteenth of such annual salary for each year and for any fraction of an additional year of such service; ~~Provided,~~ ~~further,-That any member whose term expires after he reaches the age of sixty-five and who is not reappointed shall receive retirement pay upon the same basis as if he had been retired under the provisions of this paragraph.~~ Provided, further, That any member who is not reappointed upon the expiration of his term shall receive retirement pay upon the same basis as if he had been retired under the provisions of this paragraph. The funds necessary for such retirement pay shall be provided by the Federal Reserve banks in such manner as the Federal Reserve Board shall prescribe.

~~The Secretary of the Treasury and the Comptroller of the Currency shall be ineligible during the time they are in office and for two years thereafter to hold any office, position, or employment in any member bank.~~ The ~~appointive~~ The members of the Federal Reserve Board shall be ineligible during the time they are in office and for two years thereafter to hold any office, position or employment in any member bank, except that this restriction shall not apply to a member who has served the full term for which he was appointed. Upon the expiration of the term of any ~~appointive~~ member of the Federal Reserve Board in office when this paragraph as amended takes effect, the President shall fix the term of the

(Sec. 203, p. 41)

successor to such member at not to exceed ~~twelve~~ fifteen years, as designated
 by the President at the time of nomination, but in such manner as to provide for
 the expiration of the term of not more than one appointive member in any ~~two~~
~~three-year~~ period, and thereafter each ~~appointive~~ member shall hold office for
 a term of ~~twelve~~ fifteen years from the expiration of the term of his predecessor.

(Note: Words underlined with a broken line are from Section 10 of the Federal Reserve Act.)

EXPLANATION

The above changes eliminate the Secretary of the Treasury and the Comptroller of the Currency as ex officio members of the Federal Reserve Board, and provide for the eventual reduction of the Board to five members and increases their term of office to fifteen years, thereby giving them, it is felt, greater independence and security.

They also increase the salary of the present members of the Federal Reserve Board to an equality with that proposed for members appointed after July 1, 1935.

Provision is also made that any member of the Board not reappointed upon the expiration of his term shall be pensioned in the same manner as if he had reached the age of seventy. (This is in accord with Governor Eccles' recommendation before the House Committee).

Section 203 (3), page 43, change to read as follows:

"By striking out the fourth sentence of the second paragraph and inserting in lieu thereof the following: 'Of the ~~six-appointive~~ members of the Board one shall be designated by the President as Governor and one as Vice Governor of the Federal Reserve Board, to serve as such until the further order of the President, ~~and-the-provisions-of-the~~ ~~next-preceding-sentence-of-this-paragraph-shall-not-apply-to-the-member~~ ~~designated-as-Governor,--The-term-of-office-of-the-member-designated~~ ~~as-Governor-shall-be-the-period-during-which-he-shall-continue-as~~ ~~Governor-and,-upon-the-termination-of-his-designation-as-Governor,~~ ~~he-shall-be-deemed-to-have-served-the-full-term-for-which-he-was~~ ~~appointed~~', provided, that when the member designated as Governor shall cease to be designated as Governor by the President, he may resign from the Board, and in such event he shall be deemed to have served the term for which he was appointed."

Explanation

The suggested changes are made with a view to rendering the members of the Federal Reserve Board sufficiently independent so that competent men may be induced to serve, also, to provide that if the Governor is removed by the President he may immediately resign from the Federal Reserve Board and reenter private business.

Section 205, line 11, page 44, change to read as follows:

"Section 12A. There is hereby created a Federal Open Market Committee (hereinafter referred to as the 'Committee'), which shall consist of the Governor of the Federal Reserve Board, who shall be its chairman-of-the-Committee, ~~two~~ the members of the Federal Reserve Board, ~~selected-by-the-board,~~ and ~~two~~ four governors of the Federal Reserve banks, selected by the governors of the Federal Reserve banks, in accordance with procedure prescribed by regulations of the ~~Federal-Reserve-Board,~~ governors of the twelve Federal Reserve banks. The terms of the members of the Committee, other than the Governor and members of the Federal Reserve Board, shall expire at the end of ~~each-calendar-year~~ ten years from the date of appointment, provided, that the four first appointed subsequent to the taking effect of this Act, shall be appointed for terms of four, six, eight and ten years, respectively; and provided further, that if any of the four governors shall cease to be a governor of a Federal Reserve bank he shall thereupon cease to be a member of said Open Market Committee. Whenever a vacancy shall occur a successor shall be selected, who shall hold office until the expiration of the term of his predecessor, in the same manner as his predecessor was selected. Meetings of the Committee shall be held from time to time upon the call of the Governor, at the request of the Board or of any two members of the Committee.

The Committee from time to time shall consider, adopt, and transmit to the Federal Reserve banks resolutions setting forth policies which in the judgment of the Committee should be followed with respect to open-market operations of the Federal Reserve banks, and the Federal Reserve banks shall conform their open market operations to the provisions thereof. The Committee shall aid in the execution of such policies and/or perform such other duties relating thereto

Sec. 205, line 11, p. 44

as the Federal Reserve Board may prescribe. ~~All open-market operations of the Federal Reserve Banks shall be subject to regulations prescribed by the Federal Reserve Board. The Committee from time to time shall also make recommendations to the Federal Reserve Board regarding the discount rates of the Federal Reserve banks.~~ The Committee, from time to time in order to prevent injurious credit expansion or contraction, may, by regulation, change the requirements as to reserves to be maintained against demand or time deposits, or both, by all member banks in (1) central Reserve and Reserve cities, or (2) other member banks; provided that in no event may the reserve requirements be fixed at an amount in excess of thirty per centum of the aggregate of demand and time deposits nor at an amount less than ten per centum of demand deposits and three per centum of time deposits in the case of Central Reserve and Reserve cities, nor less than seven per centum of demand deposits and three per centum of time deposits in the case of all other member banks than those in Central Reserve and Reserve cities. The Committee shall have power to approve and from time to time to amend rates of discount to be charged by the various Federal Reserve banks for each class of paper. The Committee shall aid in the execution of such policies and/or perform such other duties relating thereto as the Federal Reserve Board may prescribe. ~~All open-market operations of the Federal Reserve banks shall be subject to regulations prescribed by the Federal Reserve Board. The Committee from time to time shall also make recommendations to the Federal Reserve Board regarding the discount rates of the Federal Reserve banks.~~ The employment of the powers herein conferred upon the Committee shall be governed with a view to accommodating commerce, industry and agriculture, and with regard to their bearing upon the general credit situation of the country.

EXPLANATION

The above changes reconstitute the Federal Open Market Committee to consist of five members of the Federal Reserve Board and four Governors of the Federal Reserve Bank of St. Louis, and provides for the serial ap-

pointment of the latter for ten year terms. It also consolidates in the Federal Open Market Committee, in addition to control over open market operations, control of member bank reserve balances and control of rediscount rates. The change in regard to reserve balances is in accord with the suggestion of Governor Eccles, and the division between urban and rural districts would seem to be proper. The Council makes an addition to Governor Eccles' proposal in recommending that the limit to which reserve requirements can be increased be restricted to thirty percent of the aggregate of demand and time deposits. This exception is most essential for there can be no conceivable emergency which would justify higher reserve requirements. Essentially higher reserves than thirty per cent would probably mean that the commercial banking system would cease functioning.

It also seems advisable to the Council to set minimum reserve requirements.

In order to conform the present bill and the Federal Reserve Act to the preceding changes, the following is necessitated :

1. Eliminate Title II, section 209, from the Banking Act of 1935, inasmuch as the matter included therein is incorporated in Section 205 above, which confers the control over reserve requirements to the Federal Open Market Committee,
2. Amend Section 14 (d) of the Federal Reserve Act to substitute :
"Federal Open Market Committee" for "Federal Reserve Board."
3. Amend Section 19 of the Federal Reserve Act to eliminate subsection (c) beginning with the words "Notwithstanding the foregoing provisions of this section, the Federal Reserve Board..."

Section 206, page 45, line 18, change to read as follows:

Sec. 206. Section 13 of the Federal Reserve Act, as amended, is further amended by adding at the end thereof a new paragraph reading as follows:

~~"Upon the endorsement of any member bank, which shall be deemed a waiver of demand, notice and protest as to its own endorsement exclusively, and subject to such regulations as to maturities and other matters as the Federal Reserve Board may prescribe, any Federal Reserve bank may discount any commercial, agricultural or industrial paper and may make advances to any such member bank on its promissory notes secured by any sound assets of such member bank."~~ When any member bank has no further eligible and acceptable assets available to enable it to obtain adequate credit accommodations through rediscounting at the Federal Reserve bank or any other method provided by this act, any Federal Reserve bank, under rules and regulations prescribed by the Federal Reserve Board, may make advances to such member bank on its time or demand notes secured to the satisfaction of such Federal Reserve Bank. Each such note shall bear interest at a rate not less than one per centum per annum higher than the highest discount rate in effect at such Federal Reserve Bank on the date of such note.

Explanation Section 206, as presented in the proposed bill, might offer an inducement to member banks to lend indiscriminately and without any regard whatsoever as to the liquidity of the assets obtained. The Council feels that the Section as presented above, which is merely a re-enactment of Section 10(b) of the Federal Reserve Act, which has expired, will meet any situation which is likely to arise.

Note: In order to conform the Act, Section 10B of the Federal Reserve Act should be stricken out, inasmuch as it has expired, and the matter is now being covered in Section 13 above.

Sec. 208. Page 46, amend to read as follows:

"Sec. 208. Section 16 of the Federal Reserve Act, as amended, is further amended in the following respects:

~~(1) By striking out the first ten paragraphs and substituting therefor the following:-~~

~~"See 10. Each Federal Reserve bank may issue Federal Reserve notes, which shall be obligations of the United States, secured by a first and paramount lien on all of the assets of such bank. Federal Reserve notes shall be issued and retired under such rules and regulations as the Federal Reserve Board may prescribe and shall be legal tender for all purposes.~~

~~"Every Federal Reserve bank shall maintain reserves in lawful money (other than Federal Reserve notes or Federal Reserve bank notes) of not less than 35 per centum against its deposits and reserves in gold certificates of not less than 40 per centum against its Federal Reserve notes in actual circulation. Each Federal Reserve note shall bear upon its face a distinctive letter, which shall be assigned by the Federal Reserve Board to each Federal Reserve bank, and also a serial number.~~

~~"When received by the Treasurer of the United States from a source other than a Federal Reserve bank, Federal Reserve notes unfit for further use shall be canceled and retired, and, upon receipt of advice of such cancellation and retirement, the issuing Federal Reserve bank shall reimburse the Treasurer of the United States for the notes so canceled and retired. When received by a Federal Reserve bank, Federal Reserve notes unfit for further use shall be canceled and forwarded to the Treasurer of the United States for retirement, and, if issued by another Federal Reserve bank, such issuing bank shall reimburse the Federal Reserve bank which canceled such notes and forwarded them to the Treasurer of the United States.~~

~~"In order to furnish suitable notes for circulation as Federal Reserve notes, the Comptroller of the Currency shall cause plates and dies to be engraved in the United States to guard against counterfeiting and fraudulent alterations, and shall~~

~~have printed therefrom and numbered such quantities of such notes of the denominations of \$5, \$10, \$20, \$50, \$100, \$500, \$1,000, \$5,000 and \$10,000 as may be required to supply the Federal Reserve banks. Such notes shall be in form and tenor as directed by the Secretary of the Treasury and shall bear the distinctive numbers of the several Federal Reserve banks through which they are issued. When such notes have been prepared, they shall be held in the Treasury subject to the order of the Comptroller of the Currency for delivery to the Federal Reserve banks. Federal Reserve notes unfit for circulation shall be returned by the Federal Reserve banks to the Comptroller of the Currency for cancellation and destruction."~~

(1) By amending the second paragraph to read as follows:

"Any Federal reserve bank may make application to the local Federal reserve agent for such amount of the Federal reserve notes hereinbefore provided for as it may require. Such application shall be accompanied with a tender to the local Federal reserve agent of collateral in amount equal to the sum of the Federal reserve notes thus applied for and issued pursuant to such application. The collateral security thus offered shall be notes, drafts, bills of exchange, or acceptances acquired under the provisions of section 13 of this Act, or bills of exchange indorsed by a member bank of any Federal reserve district and purchased under the provisions of section 14 of this Act, or Bankers' acceptances purchased under the provisions of said section 14, or gold or gold certificates: ~~Providing, however, that until March 5, 1935, or until the expiration of such additional period not exceeding two years as the President may prescribe, the Federal Reserve Board may, should it deem it in the public interest, on the affirmative vote of not less than a majority of its members authorize the Federal Reserve banks to offer and Federal Reserve agents to accept as such collateral security direct obligations of the United States. On such date or upon the expiration of such period so prescribed by the President, or sooner should the Federal Reserve Board so decide, such authorization is terminated and such obligations of the United States be retired as security for Federal Reserve notes.~~ Provided, however, that should the Federal Open Market Committee, at any time, declare an emergency to exist, it may, upon the affirmative vote of not less

and the Federal Reserve agents to accept as such collateral direct obligations of the United States. Upon the determination and in the discretion of the Federal Open Market Committee such authorization shall terminate and such obligations of the United States be retired as security for Federal Reserve notes. In no event, however, shall the aggregate amount of Federal Reserve notes issued upon the security of the obligations of the United States exceed the aggregate amount of one billion dollars. A charge, at the rate of three per centum per annum, shall be paid by each Federal Reserve bank upon the amount of Federal Reserve notes applied for by it and outstanding secured by obligations of the United States. Such charge shall be payable for the period during which said notes are outstanding or until the applicant bank deposits with the Treasurer of the United States Federal Reserve notes for the retirement thereof. In no event shall such collateral security be less than the amount of Federal reserve notes applied for. The Federal reserve agent shall each day notify the Federal Reserve Board of all issues and withdrawals of Federal reserve notes to and by the Federal reserve bank to which he is accredited. The said Federal Reserve Board may at any time call upon a Federal reserve bank for additional security to protect the Federal reserve notes issued to it.

Note - The above quotes the second paragraph of Section 16 of the present Federal Reserve Act, the underscored portion representing new material.

Explanation

The Council does not believe it desirable to permit Federal reserve notes to be issued on the basis of Government bonds, except to meet an emergency. It must be remembered that one of the original purposes of the Federal Reserve Act was to get rid of a bond-secured currency and to substitute therefor an elastic currency responsive to the needs of commerce, industry and agriculture.

Note - In order to conform with the above, the Council recommends that Section 4, Paragraph 4 provision numbered "Eighth", and Section 18, of the Federal Reserve Act be repealed.

Section 210, page 49, line 4, change to read as follows:

"Sec. 210. The first paragraph of section 24 of the Federal Reserve Act, as amended, is amended to read as follows:

"Sec. 24. Any National Banking Association may make loans secured by first liens upon improved real estate, including improved farm land and improved business and residential properties, within its Federal Reserve District or within a radius of one hundred miles of a place in which such bank is located, irrespective of District lines. A loan secured by real estate within the meaning of this section shall be in the form of an obligation or obligations secured by mortgage, trust deed, or other instrument upon real estate when the entire amount of such obligation or obligations is made or is sold to such association. The amount of any such loan shall not exceed ~~60~~ 50 per centum of the actual value of the real estate offered for security, but no such loan upon such security shall be made for a longer term than ~~three~~ five years, provided, that loans may be made in amounts not exceeding ~~75~~ 60 per centum of the actual value of the real estate offered for security, if they are ~~required to be completely amortized within periods not exceeding twenty years by means of substantially equal monthly, quarterly, semi-annual, or annual payments on principal with interest added or on principal and interest combined~~ made payable within twelve years and provide for reduction by payments of not less than 5 per centum per annum on principal in addition to current interest. Any bank may make such loans in an aggregate sum equal to the amount of the capital stock of

such association paid in and unimpaired plus its unimpaired surplus fund, or equal to 60 per centum of the amount of its time and savings deposits, whichever is the greater: Provided, that the Federal Reserve Banks of the respective districts may from time to time set such lower percentage of actual value as may be loaned or such lower percentage of capital funds and surplus and/or time and savings deposits as may be loaned against real estate by banks within their respective districts for the purpose of preventing the undue use of bank credit for the speculative carrying of real estate. The Board of Directors of the respective Federal Reserve Banks shall have further power to direct any member bank within its district to refrain from further increase of its loans secured by real estate for any period up to one year, under penalty of suspension of all rediscount privileges at the Federal Reserve Bank; and Provided further, That in computing, etc."

Explanation

The above amends the provisions with respect to real estate loans to reduce the amount which may be loaned on any property to 50% of its value, provided the loan matures within five years, permitting the loans to be made up to 60% of the value of the property for a twelve year period if they are amortized by substantially equal annual payments. The suggested provisions give the respective Federal Reserve banks power to exercise such control as it is believed is necessary to prevent the use of bank credit for the speculative carrying of real estate. In this connection, Federal Reserve banks are given the same control over real estate as is given to the Federal Reserve Board, in other sections of the Banking Act, with respect to security loans.

Section 325 of the Revised Statutes amend to read:

"The Comptroller of the Currency shall be appointed by the President, on the recommendation of the Secretary of the Treasury, by and with the advice and consent of the Senate, and shall hold his office for the term of five years unless sooner removed by the President, upon reasons to be communicated by him to the Senate; and he shall be entitled to a salary of ~~five~~ twelve thousand dollars a year.

Note - Section 10 of the Federal Reserve Act provides that the Comptroller of the Currency shall be an ex officio member of the Federal Reserve Board and shall, in addition to his salary as Comptroller, receive the sum of \$7,000 annually for his service on said Board."

Explanation

Inasmuch as the changes suggested elsewhere eliminate the Comptroller of the Currency from the Federal Reserve Board, this change is suggested to compensate for the salary of which he would otherwise be deprived.

Title III

The Federal Advisory Council endorses and recommends the adoption and passage of Title III of the proposed Banking Act of 1935 (with the changes here recommended), and feels that it will correct many of the operating defects of the present banking law.

The following changes in Title III are recommended, the underscored portion representing new matter:

BANKING ACT OF 1935

Change Section 314, page 59, to read as follows:

"Sec. 5199. The directors of any association may, semi-annually, declare a dividend of so much of the net profits of the association as they shall judge expedient; but each association shall, before the declaration of a dividend on its shares of common stock, carry not less than one-tenth part of its net profits of the preceding half year to its surplus fund until the same shall equal the amount of its common capital; Provided, that any amounts paid into a fund for the retirement of any preferred stock of any such association out of the net earnings of such association for the six months' period shall be deemed to have been an addition to its surplus fund, for the purpose of this section."

Explanation

Some banks, as a result of their preferred stock retirement fund, are currently adding an amount to surplus in excess of the required one-tenth of net profits. The effect of the above suggested change would be to give such banks a credit for the amounts ~~paid~~ to the preferred stock retirement fund against the surplus ~~and~~ additions required by this section.

BANKING ACT OF 1935

Change Section 328, page 73, beginning at line 24 to read as follows:

"Sec. 8. No director, officer, or employee of any member bank of the Federal Reserve System shall be at the same time a private banker or a director, officer, or employee of any other bank, banking association, savings bank (other than a mutual savings bank), or trust company except in limited classes of cases in which the Federal Reserve Board may allow such service by general regulations when in the judgment of the Federal Reserve Board such classes of institutions are not in substantial competition or such service is not incompatible with the public interest."

Explanation

This suggested addition adopts the wording of the present Act enabling the Federal Reserve Board to issue general regulations permitting service when, in its opinion, such action is not incompatible with the public interest.

Statement of the
Federal Advisory Council

on

S. 1715, H. R. 5357

(BANKING ACT OF 1935)

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April 10, 1935

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Section references and page references, unless otherwise indicated, refer to official print of S. 1715 and H. R. 5357.

TITLE I

Title I of the proposed Banking Act of 1935 amends Section 12 B. of the Federal Reserve Act which deals with the subject of deposit insurance. The Federal Advisory Council approves this Title of the proposed bill, but suggests the following changes, the *italic* portion representing new material.

Section 8, page 10, change to read as follows:

By striking out subsection (h) and inserting in lieu thereof the following:

"(h) (1) The assessment rate shall be one-twelfth of 1 per centum per annum upon the total amount of the liability of the insured bank for deposits (according to the definition of the term 'deposit' in and pursuant to paragraph (11) of subsection (c) of this section, without any deduction for indebtedness of depositors) based on the *daily* average determined from such total ~~as of the close of business~~ *for the six months ending* on the last day of June and the last day of December of each year: Provided, That the board of directors from time to time may fix a lower rate *or may determine that there shall be no assessment* or may provide for a refund or credit by a percentage upon the last annual assessment rate ~~not exceeding 50 per centum thereof~~, when it finds that such action will provide or leave, as the case may be, adequate revenue and reserves for the Corporation having due regard to experience and conditions affecting banks. *In computing the total deposits for the purpose of this subsection any bank may deduct from the amount of its gross deposits the amounts of balances due from other banks (except balances due from foreign banks, and required reserve balances carried with Federal Reserve banks) including cash items with Federal Reserve banks and other banks in process of collection, checks on other banks in the same place, and exchange for clearing houses.* The rate or percentage so fixed shall be applicable to all insured banks, except that the board of directors on a similar finding, from time to time, may provide that the rate so fixed shall be applicable to insured mutual savings banks only or may provide a different rate applicable to mutual savings banks only."

Explanation

The above changes provide that the assessment shall be based upon the average deposits for the six months' period, instead of the total deposits as of June 30th and Dec. 31st, thereby providing a more stable basis, inasmuch as the deposits for a single day might be affected by special temporary conditions.

It was also felt that the Board of Directors of the Federal Deposit Insurance Corporation should have the power to decrease the assessment in accordance with their judgment, even by eliminating it entirely when the fund reaches such volume as they may believe will serve its purpose.

The definition of total deposits appearing in Title III, Section 323, has been here inserted, except that excess reserve balances with Federal Reserve banks are treated the same as balances due from other banks.

Section 8, subsection (h) page 10, change to read as follows:

“(2) On or before the 15th day of July of each year, each insured bank shall file with the corporation a certified statement under oath showing the ~~total~~ average amount of its ~~total liability liabilities~~ for deposits ~~as of the close of business for the six months ended on~~ the 30th day of June last preceding, *computed as provided in subsection (h) (1) of this section*, and shall pay to the corporation the portion of the annual assessment equal to one-half of the annual rate fixed by this subsection (h) multiplied by its said ~~total~~ average deposits ~~on the date for which such statement is made as shown by such statement~~. On or before the 15th day of January of each year each insured bank shall file a like statement showing the ~~total~~ average of its ~~total liability liabilities~~ for deposits *for the six months ended as of the close of business on the 31st day of December last preceding, computed as provided in subsection (h) (1) of this section*, and shall pay to the corporation the portion of the annual assessment equal to one-half of the annual rate fixed by this subsection (h) multiplied by its said total average deposits ~~on the date for which such statement is made as shown by such statement~~.”

Explanation

Amended to conform with Section 12 (b), Subsection H (1) above.

Section 8, change the proviso in paragraph (5) line 24, page 12, to read as follows:

“Provided, That where a fiduciary bank deposits any of such trust funds in another insured banks, ~~the amount so held by other insured banks on deposit on the last day of the month preceding such fiduciary bank may upon~~ the filing of the certified statement required by paragraph (2) of subsection (h) of this section, *deduct the average daily amount of such trust funds so deposited which for the purpose of such statement shall not be considered to be a deposit liability of the fiduciary bank, but shall be considered a deposit liability of the bank in which such funds are so deposited by such fiduciary bank.*”

Explanation

To conform with changes recommended in Section 8 basing assessments on average daily deposits rather than deposits at December 31st and June 30th.

Section 13, (5), page 30, change as follows:

“If any depositor in a closed bank shall fail to claim his insured deposit from the Corporation, or shall fail to claim or arrange to continue the transferred deposit with the new bank or other bank assuming liability therefor within ~~one~~ two years after the appointment of the receiver for the closed bank, all rights of the depositor against the Corporation in respect to the insured deposit or against the new bank and such other bank in respect to the transferred deposit shall be barred, and all rights of the depositor against the closed bank, its shareholders or the receivership estate to which the Corporation may have become subrogated shall thereupon revert to the depositor. The amount of any transferred deposits not claimed within said ~~one~~ two- year period, shall be refunded to the Corporation.”

Explanation

It is believed that one year is not sufficient time for depositors to make their claims, in view of the difficulties which sometimes exist of ascertaining ownership of deposits.

Section 18, page 34, change to read as follows:

“By adding at the end of subsection (r) the following:

“The board of directors, from time to time, shall gather information and data and shall make investigations and reports upon the organization, operation, closing, reopening, reorganization, and consolidation of banks, banking practices ~~and management~~, and the security of depositors ~~and adequacy of service to borrowers~~. The board of directors, in any annual or special report to Congress, shall report its findings and make such recommendations and requests as it shall find necessary and appropriate for the purpose of carrying out the purpose of this section and fully providing for all of the obligations of the Corporation.’”

Explanation

It is felt that the elimination of the clause indicated above will not impair the proper functions of the Federal Deposit Insurance Corporation. The elimination is made to avoid duplication of examinations.

Section 22 (3), page 36, change to read as follows:

“No insured bank shall pay any dividends on its capital stock while it remains in default in the payment of any assessment due to the Corporation; and any director or officer of any insured bank, who *with knowledge of such default* participates in the declaration or payment of any such dividend shall, upon conviction, be fined not more than \$1,000 or imprisoned not more than one year, or both.”

Explanation

It would seem obvious that no penal liability should attach to a director or officer who participates in the declaration of a dividend without knowledge of such default. Such a provision would be contrary to all penal statutes which only make liable those who wilfully do an act which is unlawful.

Section 22 (5), page 36, change to read as follows:

“Each insured bank shall provide ~~such~~ protection and indemnity against burglary, fidelity, and other similar insurable losses *in such amounts* as the board of directors by regulation may require adequately to reimburse the bank for such losses. Whenever any insured bank fails to comply with any such regulation the corporation may contract for such protection and indemnity and add the cost thereof to the assessment otherwise payable by such bank.”

Explanation

The above changes clarify the apparent intent of this section and would eliminate the possibility that the section, as now worded, might confer upon the Federal Deposit Insurance Corporation the power to discriminate between insurance companies.

TITLE II

The Federal Advisory Council has considered most carefully Title II of the proposed Banking Act of 1935. The provisions of Title II change fundamentally in many respects the Federal Reserve System as it has existed since its inception. The Council questions whether there is any emergency at the present time which makes it necessary to enact into law the provisions of Title II without further careful consideration and study. The Council wishes to point out that in recent years so many changes have been made in the whole fiscal and financial structure of the country that there may well be some real concern entertained as to whether a proper relationship between the various parts has been maintained. These doubts are not concerned with this or that detail of Title II. Twenty-five years ago, before the Federal Reserve Act was enacted, a series of studies was undertaken by a national commission. Since then many different types of financial institutions have sprung up, so that it would seem most desirable to have another detailed study made analogous to the one which preceded the enactment of the Federal Reserve Act.

In spite of what has been said, if the Government deems it advisable to enact at this time legislation making fundamental changes in the Federal Reserve System, the Federal Advisory Council after a careful study of the proposed measure suggests certain amendments which it regards as fundamental. The Council deems it essential to preserve the autonomy of the regional Federal Reserve banks as provided in the original Act and in order to maintain this principle, it makes certain suggestions which will be detailed below.

Title II may be divided into three general subjects:

The first has to do with the control of money, the organizations set up to exercise this control, and the powers to be employed. The control over money may be maintained by a change in the discount rate or by the increase or decrease of the percentage of reserves kept by member banks with the Federal Reserve banks, or finally by operations in the open market, i.e., by the purchase or sale of Government bonds by the Federal Reserve banks.

The exercise of these powers is of the greatest importance to the commerce, industry, and agriculture of the country. As far as possible the members of the body to whom is to be entrusted this vast authority should be free of wrongful influences whether political or financial. While, therefore, there should be independence of judgment, it is recognized that there is a proper relationship between governmental financial policies and the action of those authorities controlling the banking system of the country and that it is desirable that there be close cooperation and harmony between the two. With this in mind, the Federal Advisory Council recommends the following changes in the proposed law:

1. That the Secretary of the Treasury and the Comptroller of the Currency cease to be members of the Federal Reserve Board.
2. That the Board be reduced to five members.
3. That the governor and members be appointed for fifteen years, but compelled to retire at the age of seventy.
4. That the Federal Reserve bank governors be appointed by the directors of the Federal Reserve banks with the approval of the Federal Reserve Board, but that after the approval of the Federal Reserve Board has once been obtained, the governors may be re-elected annually by the directors of the banks subject to the approval by the Federal Reserve Board every three years.
5. That a committee composed of the members of the Federal Reserve Board and four of the bank governors, selected by the twelve governors, shall be given the power to fix the discount rate, the percentage of reserves, and direct the open-market policies of the banks.

The second general subject dealt with in Title II is the liberalization of rediscount privileges. The Council recommends the re-enactment of Section 10 (b) as detailed below.

The third general subject dealt with in Title II is that of real estate loans. There is unquestionably need of some effective private agency to finance the requirements of real estate. The difficulty is that banks are in a very different position from other institutions; they have limited capital, and such capital as they have must be protected as far as possible.

It is the opinion of the Council that a further study of this subject should be made, but if a law is to be passed at the present time the Council feels that the power should be given to the several Federal Reserve banks to lower the percentage of value up to which a bank may loan, and to lower from time to time the percentage of individual bank capital and surplus which may be represented by loans secured by real estate in banks within its district. Any percentage so fixed by the Federal Reserve bank should be subject to change from time to time, upon ten days notice, and it should be the duty of the bank to establish such percentages with a view to preventing the undue use of bank loans for the speculative carrying of real estate. The Federal Reserve bank should have power to direct any member bank to refrain from further increase of its loans secured by real estate for any period up to one year, under penalty of suspension of all rediscount privileges at the Federal Reserve bank. The Council also feels that the present provisions of the law, restricting the area within which banks should be permitted to make real estate loans, should be incorporated in this act, i.e., within the Federal Reserve District or within a radius of 100 miles of the place in which such bank is located.

The detailed changes necessary to carry out these recommendations will follow, the *italic* portion representing new material.

The proposed amendments, if accepted, would take from Title II the features which the Council conceives to be the most dangerous. Without them the Council feels that prior to the independent study which is earlier suggested, Title II must be disapproved in its entirety.

Section 201, page 39, change paragraph beginning at line 9, to read as follows:

“Effective ninety days after the enactment of the Act containing this amendment, the offices of Governor and chairman of the board of directors of each Federal Reserve Bank shall be combined. The Governor shall be the chief executive officer of the bank and shall be appointed annually by the board of directors, ~~subject to the approval of the Federal Reserve Board~~. He shall not take office *for the first term* until approved by the Federal Reserve Board and thereupon *and thereafter* he shall be *subject to the approval by the Federal Reserve Board every three years, and after such approval he shall be* appointed and *reappointed* by the Federal Reserve Board as one of the Class C directors of the bank, etc.”

Explanation

The Federal Advisory Council originally proposed that the Federal Reserve Board should have the right to confirm the governors of the respective Federal Reserve banks only at the time of the initial election of such a governor and that thereafter the governors should be re-elected by the boards of directors of the local Federal Reserve banks without the necessity of reapproval by the Federal Reserve

Board. In view, however, of the amendment suggested by Governor Eccles in the second paragraph on page 40 of H. R. 5357 which would turn over to the governors of the respective Federal Reserve banks all the functions at present exercised by the Federal Reserve agents, it seemed to the Council that there was merit in the suggestion of the Governor that the Board have the right periodically to pass on the question as to whether a given governor was the one whom the Board desired to have as its representative.

Section 201, page 40. Strike out the sentence beginning at line 14, reading as follows:

~~“All duties prescribed by law for the Federal Reserve agent shall be performed by such person as the Federal Reserve Board shall designate”~~ and substitute the following: *“All duties prescribed by law for the Federal Reserve agent shall be performed by the Governor of the bank or by such other person or persons as he may designate.”*

Explanation

This is in accord with Governor Eccles' suggestion and will turn over to the governor of the Federal Reserve bank all the functions at present exercised by the Federal Reserve agent of such bank.

Section 201, page 40. Eliminate paragraph beginning at line 17 reading as follows:

~~“No member of the Board of Directors of a Federal Reserve bank, other than the Governor and Vice Governor, shall serve as a director for more than two consecutive terms of three years each. This shall not prevent the present incumbents from serving out the remainder of their present terms.”~~

Explanation

It is felt that the inclusion of this paragraph might deprive many of the regional Reserve banks of the services of directors who are invaluable on account of their experience gained by length of service, especially in such districts where the number of men most qualified to serve as directors may be limited. At the present time, a number of the Federal Reserve banks have already adopted restrictions similar to the one proposed in the bill, and it seems to the Council that this matter might well be left to the discretion of each Federal Reserve bank.

Section 203, page 41, of the Banking Act of 1935, change to amend Section 10 of the Federal Reserve Act, to read as follows:

A Federal Reserve Board is hereby created, which shall consist of ~~eight~~ six members including the Secretary of the Treasury and the Comptroller of the Currency who shall be members ex officio and six members appointed by the President of the United States, by and with the advice and consent of the Senate; provided, however, that whenever the membership shall be reduced by death, resignation, expiration of term or other cause, the vacancy thus created shall not be filled if it would increase the membership to more

than five. In selecting the ~~six appointive~~ members of the Federal Reserve board the President shall choose persons well qualified by education or experience or both to participate in the formulation of national economic and monetary policies, not more than one of ~~the appointive members~~ whom shall be selected from any one Federal Reserve district, except that this limitation shall not apply to the selection of the Governor. ~~The President shall have due regard to a fair representation of the financial, agricultural, industrial, and commercial interests, and geographical divisions of the country.~~ The ~~six~~ members of the Federal Reserve Board appointed by the President and confirmed as aforesaid shall devote their entire time to the business of the Federal Reserve Board and shall each receive ~~the sum of \$12,000 payable monthly together with actual necessary traveling expenses, and the Comptroller of the Currency as ex officio member of the Federal Reserve Board, shall, in addition to the salary now paid him as Comptroller of the Currency receive the sum of \$7,000 annually for his services as a member of said Board.~~ The appointive members of the Federal Reserve Board appointed after July 1, 1935, shall each receive a salary at the same rate as that of the heads of the executive departments who are members of the President's Cabinet, together with actual necessary traveling expenses. Each appointive member of the Federal Reserve Board heretofore appointed may retire from active service upon reaching the age of seventy or at any time thereafter, and all members hereafter appointed shall retire upon reaching the age of seventy. Each member of the Board so retired from active service who shall have served for at least five years shall receive, during the remainder of his life retirement pay in an amount equal to the annual salary paid to appointive members prior to the enactment of the Act containing this amendment: Provided, That if he shall not have served as much as ~~twelve~~ *fifteen* years his retirement pay shall be at the rate of one ~~twelfth~~ *fifteenth* of such annual salary for each year and for any fraction of an additional year of such service; ~~Provided, further, That any member whose term expires after he reaches the age of sixty five and who is not reappointed shall receive retirement pay upon the same basis as if he had been retired under the provisions of this paragraph.~~ *Provided, further, That any member who is not reappointed upon the expiration of his term shall receive retirement pay upon the same basis as if he had been retired under the provisions of this paragraph.* The funds necessary for such retirement pay shall be provided by the Federal Reserve banks in such manner as the Federal Reserve Board shall prescribe.

~~The Secretary of the Treasury and the Comptroller of the Currency shall be ineligible during the time they are in office and for two years thereafter to hold any office, position, or employment in any member bank.~~ ~~The appointive~~ The members of the Federal Reserve Board shall be ineligible during the time they are in office and for two years thereafter to hold any office, position or employment in any member bank, except that this restriction shall not apply to a member who has served the full term for which he was appointed. Upon the expiration of the term of any ~~appointive~~ member of the Federal Reserve Board in office when this paragraph as amended takes effect, the President shall fix the term of the successor to such member at not to exceed ~~twelve~~ *fifteen* years, as designated by the President at the time of nomination, but in such manner as to provide for the expiration of the term of not more than one appointive member in any ~~two~~ *three*-year period, and thereafter each ~~appointive~~ member shall hold office for a term of ~~twelve~~ *fifteen* years from the expiration of the term of his predecessor.

(Note: Words in bold face type are from Section 10 of the Federal Reserve Act.)

Explanation

The above changes eliminate the Secretary of the Treasury and the Comptroller of the Currency as ex officio members of the Federal Reserve Board, and provide for the eventual reduction of the Board to five members and increases their term of office to fifteen years, thereby giving them, it is felt, greater independence and security.

They also increase the salary of the present members of the Federal Reserve Board to an equality with that proposed for members appointed after July 1, 1935.

Provision is also made that any member of the Board not reappointed upon the expiration of his term shall be pensioned in the same manner as if he had reached the age of seventy. (This is in accord with Governor Eccles' recommendation before the House Committee.)

Section 203 (3), page 43, change to read as follows:

“By striking out the fourth sentence of the second paragraph and inserting in lieu thereof the following: ‘Of the ~~six appointive~~ members of the Board one shall be designated by the President as Governor and one as Vice Governor of the Federal Reserve Board, to serve as such until the further order of the President, ~~and the provisions of the next preceding sentence of this paragraph shall not apply to the member designated as Governor. The term of office of the member designated as Governor shall be the period during which he shall continue as Governor and, upon the termination of his designation as Governor, he shall be deemed to have served the full term for which he was appointed~~, provided, that when the member designated as Governor shall cease to be designated as Governor by the President, he may resign from the Board, and in such event he shall be deemed to have served the term for which he was appointed.’”

Explanation

The suggested changes are made with a view to rendering the members of the Federal Reserve Board sufficiently independent so that competent men may be induced to serve, also, to provide that if the Governor is removed by the President he may immediately resign from the Federal Reserve Board and reenter private business.

Section 205, line 11, page 44, change to read as follows:

“Section 12A. There is hereby created a Federal Open Market Committee (hereinafter referred to as the ‘Committee’), which shall consist of the Governor of the Federal Reserve Board, who shall be *its* chairman ~~of the Committee, two~~ the members of the Federal Reserve Board, ~~selected by the board,~~ and ~~two~~ four governors of the Federal Reserve Banks, selected by the governors of the Federal Reserve Banks, in accordance with procedure prescribed by regulations of the ~~Federal Reserve Board,~~ *governors of the twelve Federal Reserve banks.* The terms of the members of the Committee, other than the Governor *and members of the Federal Reserve Board,* shall expire at the end of ~~each calendar year~~ *ten years from the*

date of appointment, provided, that the four first appointed subsequent to the taking effect of this Act, shall be appointed for terms of four, six, eight and ten years, respectively; and provided further, that if any of the four governors shall cease to be a governor of a Federal Reserve bank he shall thereupon cease to be a member of said Open Market Committee. Whenever a vacancy shall occur a successor shall be selected, who shall hold office until the expiration of the term of his predecessor, in the same manner as his predecessor was selected. Meetings of the Committee shall be held from time to time upon the call of the Governor, at the request of the Board or of any two members of the Committee.

The Committee from time to time shall consider, adopt, and transmit to the Federal Reserve banks resolutions setting forth policies which in the judgment of the Committee should be followed with respect to open-market operations of the Federal Reserve banks, and the Federal Reserve banks shall conform their open market operations to the provisions thereof. The Committee shall aid in the execution of such policies and/or perform such other duties relating thereto as the Federal Reserve Board may prescribe. ~~All open-market operations of the Federal Reserve Banks shall be subject to regulations prescribed by the Federal Reserve Board. The Committee from time to time shall also make recommendations to the Federal Reserve Board regarding the discount rates of the Federal Reserve banks. The Committee, from time to time in order to prevent injurious credit expansion or contraction, may, by regulation, change the requirements as to reserves to be maintained against demand or time deposits, or both, by all member banks in (1) central Reserve and Reserve cities, or (2) other member banks; provided that in no event may the reserve requirements be fixed at an amount in excess of thirty per centum of the aggregate of demand and time deposits nor at an amount less than ten per centum of demand deposits and three per centum of time deposits in the case of Central Reserve and Reserve cities, nor less than seven per centum of demand deposits and three per centum of time deposits in the case of all other member banks than those in Central Reserve and Reserve cities. The Committee shall have power to approve and from time to time to amend rates of discount to be charged by the various Federal Reserve banks for each class of paper.~~ The Committee shall aid in the execution of such policies and/or perform such other duties relating thereto as the Federal Reserve Board may prescribe. ~~All open market operations of the Federal Reserve banks shall be subject to regulations prescribed by the Federal Reserve Board. The Committee from time to time shall also make recommendations to the Federal Reserve Board regarding the discount rates of the Federal Reserve banks. The employment of the powers herein conferred upon the Committee shall be governed with a view to accommodating commerce, industry and agriculture, and with regard to their bearing upon the general credit situation of the country.~~

Explanation

The above changes reconstitute the Federal Open Market Committee to consist of the five members of the Federal Reserve Board and four Governors of the Reserve banks appointed by the twelve Governors, and provides for the serial appointment of the latter for ten year terms. It also consolidates in the Federal Open Market Committee, in addition to control over open market operations, control of member bank reserve balances and control of rediscount rates. The change in regard to reserve balances is in accord with the suggestion of Governor Eccles, and the

division between urban and rural districts would seem to be proper. The Council makes an addition to Governor Eccles' proposal in recommending that the limit to which reserve requirements can be increased be restricted to thirty per cent of the aggregate of demand and time deposits. This exception is most essential for there can be no conceivable emergency which would justify higher reserve requirements. Essentially higher reserves than thirty per cent would probably mean that the commercial banking system would cease functioning.

It also seems advisable to the Council to set minimum reserve requirements.

In order to conform the present bill and the Federal Reserve Act to the preceding changes, the following is necessitated:

1. Eliminate Title II, section 209, from the Banking Act of 1935, inasmuch as the matter included therein is incorporated in Section 205 above, which confers the control over reserve requirements to the Federal Open Market Committee.
 2. Amend Section 14 (d) of the Federal Reserve Act to substitute:
"Federal Open Market Committee" for "Federal Reserve Board."
 3. Amend Section 19 of the Federal Reserve Act to eliminate subsection (c) beginning with the words "Notwithstanding the foregoing provisions of this section, the Federal Reserve Board . . ."
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Section 206, page 45, line 18, change to read as follows:

Sec. 206. Section 13 of the Federal Reserve Act, as amended, is further amended by adding at the end thereof a new paragraph reading as follows:

~~"Upon the endorsement of any member bank, which shall be deemed a waiver of demand, notice and protest as to its own endorsement exclusively, and subject to such regulations as to maturities and other matters as the Federal Reserve Board may prescribe, any Federal Reserve bank may discount any commercial, agricultural or industrial paper and may make advances to any such member bank on its promissory notes secured by any sound assets of such member bank."~~ *When any member bank has no further eligible and acceptable assets available to enable it to obtain adequate credit accommodations through rediscounting at the Federal Reserve bank or any other method provided by this act, any Federal Reserve bank, under rules and regulations prescribed by the Federal Reserve Board, may make advances to such member bank on its time or demand notes secured to the satisfaction of such Federal Reserve Bank. Each such note shall bear interest at a rate not less than one per centum per annum higher than the highest discount rate in effect at such Federal Reserve Bank on the date of such note.*

Explanation

Section 206, as presented in the proposed bill, might offer an inducement to member banks to lend indiscriminately and without any regard whatsoever as to the liquidity of the assets obtained. The Council feels that the Section as presented

above, which is merely a re-enactment of Section 10(b) of the Federal Reserve Act, which has expired, will meet any situation which is likely to arise.

Note: In order to conform the Act, Section 10B of the Federal Reserve Act should be stricken out, inasmuch as it has expired, and the matter is now being covered in Section 13 above.

Section 208, page 46, amend to read as follows:

"Sec. 208. Section 16 of the Federal Reserve Act, as amended, is further amended in the following respects:

(1) By striking out the first ten paragraphs and substituting therefor the following:

~~"Sec. 10. Each Federal Reserve bank may issue Federal Reserve notes, which shall be obligations of the United States, secured by a first and paramount lien on all of the assets of such bank. Federal Reserve notes shall be issued and retired under such rules and regulations as the Federal Reserve Board may prescribe and shall be legal tender for all purposes.~~

~~"Every Federal Reserve bank shall maintain reserves in lawful money (other than Federal Reserve notes or Federal Reserve bank notes) of not less than 35 per centum against its deposits and reserves in gold certificates of not less than 40 per centum against its Federal Reserve notes in actual circulation. Each Federal Reserve note shall bear upon its face a distinctive letter, which shall be assigned by the Federal Reserve Board to each Federal Reserve bank, and also a serial number.~~

~~"When received by the Treasurer of the United States from a source other than a Federal Reserve bank, Federal Reserve notes unfit for further use shall be canceled and retired, and, upon receipt of advice of such cancelation and retirement, the issuing Federal Reserve bank shall reimburse the Treasurer of the United States for the notes so canceled and retired. When received by a Federal Reserve bank, Federal Reserve notes unfit for further use shall be canceled and forwarded to the Treasurer of the United States for retirement, and, if issued by another Federal Reserve bank, such issuing bank shall reimburse the Federal Reserve bank which canceled such notes and forwarded them to the Treasurer of the United States.~~

~~"In order to furnish suitable notes for circulation as Federal Reserve notes, the Comptroller of the Currency shall cause plates and dies to be engraved in the best manner to guard against counterfeiting and fraudulent alterations, and shall have printed therefrom and numbered such quantities of such notes of the denominations of \$5, \$10, \$20, \$50, \$100, \$500, \$1,000, \$5,000 and \$10,000 as may be required to supply the Federal Reserve banks. Such notes shall be in form and tenor as directed by the Secretary of the Treasury and shall bear the distinctive numbers of the several Federal Reserve banks through which they are issued. When such notes have been prepared, they shall be held in the Treasury subject to the order of the Comptroller of the Currency for delivery to the Federal Reserve banks. Federal Reserve notes unfit for circulation shall be returned by the Federal Reserve banks to the Comptroller of the Currency for cancelation and destruction."~~

(1) By amending the second paragraph to read as follows:

"Any Federal reserve bank may make application to the local Federal Reserve agent for such amount of the Federal Reserve notes hereinbefore provided for as it may require.

Such application shall be accompanied with a tender to the local Federal Reserve agent of collateral in amount equal to the sum of the Federal Reserve notes thus applied for and issued pursuant to such application. The collateral security thus offered shall be notes, drafts, bills of exchange, or acceptances acquired under the provisions of section 13 of this Act, or bills of exchange indorsed by a member bank of any Federal Reserve district and purchased under the provisions of section 14 of this Act, or Bankers' acceptances purchased under the provisions of said section 14, or gold or gold certificates: ~~Providing, however, that until March 3, 1935, or until the expiration of such additional period not exceeding two years as the President may prescribe, the Federal Reserve Board may, should it deem it in the public interest, on the affirmative vote of not less than a majority of its members authorize the Federal Reserve banks to offer and Federal Reserve agents to accept as such collateral security direct obligations of the United States. On such date or upon the expiration of such period so prescribed by the President, or sooner should the Federal Reserve Board so decide, such authorization is terminated and such obligations of the United States be retired as security for Federal Reserve notes. Provided, however, that should the Federal Open Market Committee, at any time, declare an emergency to exist, it may, upon the affirmative vote of not less than a majority of its members, authorize the Federal Reserve banks to offer and the Federal Reserve agents to accept as such collateral direct obligations of the United States. Upon the determination and in the discretion of the Federal Market Open Committee such authorization shall terminate and such obligations of the United States be retired as security for Federal Reserve notes. In no event, however, shall the aggregate amount of Federal Reserve notes issued upon the security of the obligations of the United States exceed the aggregate amount of one billion dollars. A charge, at the rate of three per centum per annum, shall be paid by each Federal Reserve bank upon the amount of Federal Reserve notes applied for by it and outstanding secured by obligations of the United States. Such charge shall be payable for the period during which said notes are outstanding or until the applicant bank deposits with the Treasurer of the United States Federal Reserve notes for the retirement thereof. In no event shall such collateral security be less than the amount of Federal Reserve notes applied for. The Federal Reserve agent shall each day notify the Federal Reserve Board of all issues and withdrawals of Federal Reserve notes to and by the Federal Reserve bank to which he is accredited. The said Federal Reserve Board may at any time call upon a Federal Reserve bank for additional security to protect the Federal Reserve notes issued to it.~~

Note—The above quotes the second paragraph of Section 16 of the present Federal Reserve Act, the *italic* portion representing new material.

Explanation

The Council does not believe it desirable to permit Federal Reserve notes to be issued on the basis of Government bonds, except to meet an emergency. It must be remembered that one of the original purposes of the Federal Reserve Act was to get rid of a bond-secured currency and to substitute therefor an elastic currency responsive to the needs of commerce, industry and agriculture.

Note—In order to conform with the above, the Council recommends that Section 4, Paragraph 4 provision numbered "Eighth", and Section 18, of the Federal Reserve Act be repealed.

Section 210, page 49, line 4, change to read as follows:

"Sec. 210. The first paragraph of section 24 of the Federal Reserve Act, as amended, is amended to read as follows:

"Sec. 24. Any National Banking Association may make loans secured by first liens upon improved real estate, including improved farm land and improved business and residential properties, *within its Federal Reserve District or within a radius of one hundred miles of a place in which such bank is located, irrespective of District lines.* A loan secured by real estate within the meaning of this section shall be in the form of an obligation or obligations secured by mortgage, trust deed, or other instrument upon real estate when the entire amount of such obligation or obligations is made or is sold to such association. The amount of any such loan shall not exceed ~~60~~ 50 per centum of the actual value of the real estate offered for security, but no such loan upon such security shall be made for a longer term than ~~three~~ five years, provided, that loans may be made in amounts not exceeding ~~75~~ 60 per centum of the actual value of the real estate offered for security, if they are ~~required to be completely amortized within periods not exceeding twenty years by means of substantially equal monthly, quarterly, semi-annual, or annual payments on principal with interest added or on principal and interest combined~~ *made payable within twelve years and provide for reduction by payments of not less than 5 per centum per annum on principal in addition to current interest.* Any bank may make such loans in an aggregate sum equal to the amount of the capital stock of such association paid in and unimpaired plus its unimpaired surplus fund, or equal to 60 per centum of the amount of its time and savings deposits, whichever is the greater: *Provided, that the Federal Reserve Banks of the respective districts may from time to time set such lower percentage of actual value as may be loaned or such lower percentage of capital funds and surplus and/or time and savings deposits as may be loaned against real estate by banks within their respective districts for the purpose of preventing the undue use of bank credit for the speculative carrying of real estate. The Board of Directors of the respective Federal Reserve Banks shall have further power to direct any member bank within its district to refrain from further increase of its loans secured by real estate for any period up to one year, under penalty of suspension of all rediscount privileges at the Federal Reserve Bank; and Provided further, That in computing, etc."*

Explanation

The above amends the provisions with respect to real estate loans to reduce the amount which may be loaned on any property to 50% of its value, provided the loan matures within five years, permitting the loans to be made up to 60% of the value of the property for a twelve year period if they are amortized by substantially equal annual payments. The suggested provisions give the respective Federal Reserve banks power to exercise such control as it is believed is necessary to prevent the use of bank credit for the speculative carrying of real estate. In this connection, Federal Reserve banks are given the same control over real estate as is given to the Federal Reserve Board, in other sections of the Banking Act, with respect to security loans.

Section 325 of the Revised Statutes amend to read:

“The Comptroller of the Currency shall be appointed by the President, on the recommendation of the Secretary of the Treasury, by and with the advice and consent of the Senate, and shall hold his office for the term of five years unless sooner removed by the President, upon reasons to be communicated by him to the Senate; and he shall be entitled to a salary of ~~five~~ *twelve* thousand dollars a year.

Note—Section 10 of the Federal Reserve Act provides that the Comptroller of the Currency shall be an ex officio member of the Federal Reserve Board and shall, in addition to his salary as Comptroller, receive the sum of \$7,000 annually for his service on said Board.”

Explanation

Inasmuch as the changes suggested elsewhere eliminate the Comptroller of the Currency from the Federal Reserve Board, this change is suggested to compensate for the salary of which he would otherwise be deprived.

TITLE III

The Federal Advisory Council endorses and recommends the adoption and passage of Title III of the proposed Banking Act of 1935 (with the changes here recommended), and feels that it will correct many of the operating defects of the present banking law.

The following changes in Title III are recommended, the *italic* portion representing new matter.

Section 314, page 59, change to read as follows:

“Sec. 5199. The directors of any association may, semi-annually, declare a dividend of so much of the net profits of the association as they shall judge expedient; but each association shall, before the declaration of a dividend on its shares of common stock, carry not less than one-tenth part of its net profits of the preceding half year to its surplus fund until the same shall equal the amount of its common capital; *Provided, that any amounts paid into a fund for the retirement of any preferred stock of any such association out of the net earnings of such association for the six months' period shall be deemed to have been an addition to its surplus fund, for the purpose of this section.*”

Explanation

Some banks, as a result of their preferred stock retirement fund, are currently adding an amount to surplus in excess of the required one-tenth of net profits. The effect of the above suggested change would be to give such banks a credit for the amounts paid to the preferred stock retirement fund against the surplus additions required by this section.

Section 328, page 73, beginning at line 24, change to read as follows:

“Sec. 8. No director, officer, or employee of any member bank of the Federal Reserve System shall be at the same time a private banker or a director, officer, or employee of any other bank, banking association, savings bank (other than a mutual savings bank), or trust company except in limited classes of cases in which the Federal Reserve Board may allow such service by general regulations when in the judgment of the Federal Reserve Board such classes of institutions are not in substantial competition *or such service is not incompatible with the public interest.*”

Explanation

This suggested addition adopts the wording of the present Act enabling the Federal Reserve Board to issue general regulations permitting service when, in its opinion, such action is not incompatible with the public interest.