BANKING ACT OF 1935

HEARINGS

BEFORE THE

COMMITTEE ON BANKING AND CURRENCY
HOUSE OF REPRESENTATIVES

SEVENTY-FOURTH CONGRESS

FIRST SESSION

ON

H. R. 5357

A BILL TO PROVIDE FOR THE SOUND, EFFECTIVE, AND UNINTERRUPTED OPERATION OF THE BANKING SYSTEM, AND FOR OTHER PURPOSES

FEBRUARY 21, 22, 26, 27, 28, MARCH 1, 4, 5, 6, 11, 12, 13, 14, 15, 18, 19, 20, 21, 22, 25, 26, 27, 28, APRIL 2, 8, 1935

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BANKING ACT OF 1935

THURSDAY, FEBRUARY 21, 1935

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

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

The CHAIRMAN. Gentlemen, the committee will come to order, please.

I have asked Mr. Crowley, of the Federal Deposit Insurance Corporation, to come before us this morning and discuss H. R. 5357. I assume that he desires to address his remarks mainly to the provisions of title I of the bill, which relates to the Federal Deposit Insurance Corporation.

I am going to desist from making any preliminary statement myself at this time, but if I have the opportunity, I should like to incorporate in the hearings a short preliminary statement of my own.

In deference to a suggestion which Mr. Crowley has made to me, and what I think might be in the interest of time and orderly procedure, I am going to suggest to the committee that they permit Mr. Crowley to make his statement and complete his discussion in a general way before committeemen interrogate him.

You may proceed, Mr. Crowley, if you will.

STATEMENT OF LEO T. CROWLEY, CHAIRMAN OF THE BOARD, FEDERAL DEPOSIT INSURANCE CORPORATION

Mr. CROWLEY. Gentlemen, we have prepared a digest of this bill, together with our recommendations. If it is agreeable to the committee we will pass to each one of you a copy of our report, in order that you may follow the report with me. If you will be kind enough to let us follow through with it and answer your qestions afterward, we would like to do that. We have a number of charts that we would like to present to you. Is that agreeable to you, Mr. Steagall?

The CHAIRMAN. Yes; that will be perfectly all right.

Mr. CROWLEY. Gentlemen, last year I appeared before you and recommended that the provisions of the so-called "permanent insurance plan" be suspended for another year, and that the temporary insurance fund be continued to July 1, 1935. At that time it was stated that we need additional experience before the permanent plan went into effect. We also suggested that, through the administration of the temporary fund, we might gain some knowledge which would indicate desirable changes in the permanent plan. You have asked me to appear before you today to discuss with you the results of our 13 months' experience and study and to explain the reasons behind the proposals which you have before you, and which comprise title I of the Banking Act of 1935.

With your permission, I would like to outline to you in detail the reasons which have motivated our suggestions for changes in the permanent insurance plan. The charts and tables give a vivid picture of the commercial banking structure of the United States. These data cover all insured and noninsured banks, arranged according to total deposit liability size groupings.

They do not include mutual savings banks or private banks.

Ninety percent by number of all of the licensed commercial banks in the United States have been admitted to the insurance fund. Over 98 percent of the total deposits in commercial banks and trust companies in the United States are in banks, the deposits of which are insured. On October 1, 1934, there were only about 1,100 licensed commercial banks, with deposits of slightly more than $500,000,000, which were not insured, while insured commercial banks numbered more than 14,000 on that date, and their deposits amounted to some $36,000,000,000. Mutual savings banks have been excluded from these figures. There are 68 of the 576 mutual savings banks in the fund for mutuals.

We have in our fund 1,928 banks with deposits of $100,000 and under; of banks with deposits of $100,000 to $250,000 we have 3,929; with deposits of $250,000 to $500,000 we have 3,278; with deposits of $500,000 to $750,000, we have 1,531; with deposits of $750,000 to $1,000,000 we have 970; with deposits of $1,000,000 to $2,000,000 we have 1,664; with deposits of $2,000,000 to $5,000,000 we have 1,076; with deposits of $5,000,000 to $50,000,000 we have 647; with deposits of $50,000,000 and over we have 96 banks in our fund.

The banks are broken down in our chart into national banks, State banks, and State member banks, and the insured and uninsured nonmember banks.

For instance, out of 1,091 banks that are outside of the fund, 426 of those have deposits of $100,000 and under, 349 have deposits of $100,000 to $250,000, 169 have deposits of $250,000 to $500,000, 54 have deposits of $500,000 to $750,000, 27 have deposits of $750,000 to $1,000,000, 34 have deposits of $2,000,000 to $5,000,000, 16 have deposits of $5,000,000 to $50,000,000, and 16 banks have deposits of $50,000,000 and over, which make a total of 1,091 banks.

The CHAIRMAN. Does your statement disclose the total of the deposits in each of these groups?

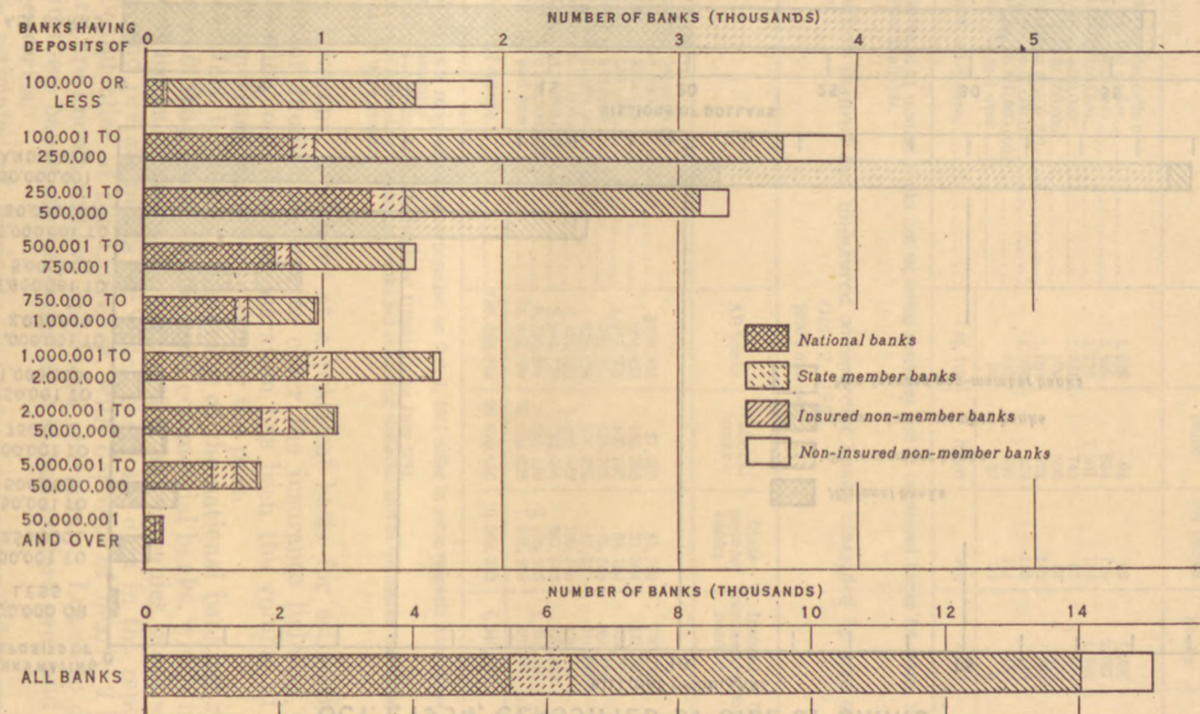
Mr. CROWLEY. Yes, sir.

The next chart that you have there shows that the banks with deposits of $100,000 and under have a total deposit liability of $123,831,000. In other words, 1,900 banks have deposits of $123,831,000.

The banks with deposits of $100,000 to $250,000 have total deposits of $664,493,000, and so on down. The $50,000,000 banks, and over, have deposits of $18,942,000,000.

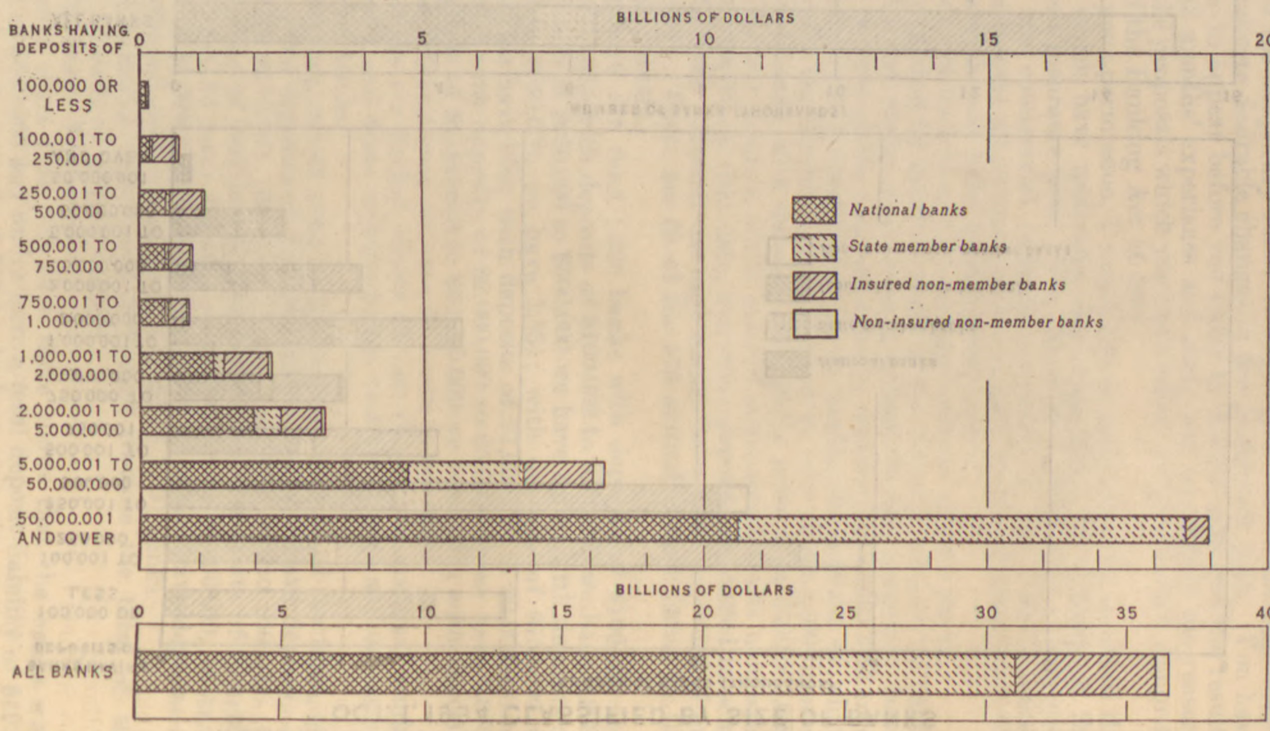
(The charts and tables referred to are as follows:)

NUMBER OF INSURED AND UNINSURED COMMERCIAL BANKS, OCT. 1, 1934 CLASSIFIED BY SIZE OF BANKS



FEDERAL DEPOSIT INSURANCE CORPORATION — DIVISION OF RESEARCH AND STATISTICS

DEPOSITS IN INSURED AND UNINSURED COMMERCIAL BANKS, OCT. 1, 1934, CLASSIFIED BY SIZE OF BANKS



FEDERAL DEPOSIT INSURANCE CORPORATION DIVISION OF RESEARCH AND STATISTICS

Insured and uninsured commercial banks classified by size of bank, Oct. 1, 1934

	All banks	National banks	State member banks	Insured nonmember banks	Uninsured nonmember banks
Banks having deposits of—					
$100,000 and under	1,928	94	22	1,386	426
$100,001 to $250,000	3,929	834	119	2,627	349
$250,001 to $500,000	3,278	1,261	186	1,662	169
$500,001 to $750,000	1,531	741	97	639	54
$750,001 to $1,000,000	970	506	67	370	27
$1,000,001 to $2,000,000	1,664	923	142	565	34
$2,000,001 to $5,000,000	1,076	659	153	248	16
$5,000,001 to $50,000,000	647	380	141	110	16
$50,000,001 and over	96	52	39	5	----------
Total, all groups	[1] 15,119	5,450	966	7,612	1,091

[1] Exclusive of 71 insured banks not reporting statistics and 31 uninsured banks for which no deposit figures were available.

Deposits in insured and uninsured commercial banks classified by size of bank, Oct. 1, 1934

[000's omitted]

	All banks	National banks [1]	State member banks [1]	Insured nonmember banks [1]	Uninsured nonmember banks [2]
Banks having deposits of:					
$100,000 and under	$123,831	$7,265	$1,700	$90,750	$24,116
$100,000 to $250,000	664,493	152,705	21,304	435,381	55,103
$250,001 to $300,000	1,167,228	460,706	68,180	579,700	58,642
$500,001 to $750,000	936,016	455,702	58,545	388,983	32,786
$750,001 to $1,000,000	836,608	437,095	57,331	318,940	23,242
$1,000,001 to $2,000,000	2,324,922	1,300,832	199,540	778,427	46,123
$2,000,001 to $5,000,000	3,242,721	1,982,864	487,542	723,051	49,264
$5,000,001 to $50,000,000	8,250,016	4,691,139	2,118,575	1,216,797	223,505
$50,000,001 and over	18,942,184	10,582,628	7,951,575	407,981	----------
Total, all groups	[3] 36,488,019	20,070,936	10,964,292	4,940,010	512,781

[1] Total deposits reported to the corporation on Oct. 1, 1934 differ in some respects from those shown on published statements.
[2] As reported in Rand-McNally Bankers' Directory for July 1934.
[3] Exclusive of deposits of 71 insured banks not reporting statistics and 31 uninsured banks for which no deposit figures were available.

Mr. Crowley. To arrive at a practical basis for estimating the amount of funds necessary to cover the insurance liability of the Corporation, our first consideration has been the volume of losses which depositors have borne during the past.

From July 1, 1864, the beginning of the national banking system, to June 30, 1934, about 16 thousand commercial banks, which include national banks, State banks, loan and trust companies, stock savings banks, and private banks for which there are data in the reports of the Comptroller of the Currency, with deposits of nearly 9 billion dollars, are known to have suspended operations. Losses to depositors in these banks are estimated at 3 billion dollars over and above all recoveries.

The estimates of losses to depositors in suspended commercial banks are based upon available data which clearly minimize the facts. The figures for national banks are fairly complete and reliable, and are taken from reports of the Comptroller of the Currency. The figures for other commercial banks, however, are incomplete, particularly for the period prior to 1920. Since all failures have not been recorded, bank depositors have suffered losses which have not been recorded. For example, many records of voluntary liquidation by banks ignore the fact that depositors were not paid in full. Then, again, bank reorganizations, in late years, have been based upon the waiving of depositors' claims, while in other cases depositors have voluntarily reduced their claims or made contributions to capital as a means of absorbing losses.

Mr. KOPPLEMANN. Mr. Crowley, do you mean to say that even today there are banks that fail without being reported, private banks or any kind of a bank?

Mr. CROWLEY. What we are talking about is during the last few years.

Mr. KOPPLEMANN. I know, but I wondered whether that situation still exists.

Mr. CROWLEY. I think there are some States in which banks might fail, and we cannot get the information from them.

Mr. KOPPLEMANN. There are still?

Mr. CROWLEY. Yes.

The CHAIRMAN. Inasmuch as that question has been asked, what information have you to support the statement that there have been voluntary liquidations of State institutions, in which the depositors are not paid in full? How do you get information like that?

Mr. FOX. Mr. Chairman, the source of the information is the Federal Reserve Board. They make contacts with the State authorities through their agents in the 12 Federal Reserve districts. If the State authorities inform the agents, we get the information. However, if the State authorities have no control over the banks, as is the case with some private banks, we would not get the information.

The CHAIRMAN. Would it not follow as a matter of course that when a bank became insolvent, to the extent of wiping out its capital structure, and leaving it with its depositors unprotected, there would be a liquidation in the regular way of such an institution?

Mr. CROWLEY. What we are trying to bring out, Mr. Chairman, is that there have been a lot of insolvent banks that have gone to their depositors and made private deals with them, whereby they wrote down their deposits liability in some instances as high as 40, 50, or 60 percent, and when they waived a portion of those deposits, the portion that they waived was used for capital purposes.

Mr. CROSS. Did you get that through the Internal Revenue Department?

Mr. CROWLEY. No; there would be no reason for their reporting to the Internal Revenue Department.

The CHAIRMAN. I was of the opinion that there would be no report of that kind to the Commissioner.

Mr. CROWLEY. There would be no way to have it recorded. The only place you could get it would be through the local bank commissioner, and a lot of them do not keep complete records.

Mr. HANCOCK. What is your best estimate of the losses which have occurred that are not accounted for?

Mr. CROWLEY. Have you any idea what that might amount to, Mr. Fox?

Mr. FOX. No, sir.

Mr. CROWLEY. What we have been trying to do is to find out from the various State departments how much their depositors have lost through waivers, and it has been an almost impossible thing to determine, because they have kept no records of it, but we do know it has been a very substantial sum.

Mr. Reilly. In the case of Wisconsin have you a record?

Mr. Crowley. We have not been able to get that as yet.

Mr. Fox. We are getting a record for the past 4 years. We already have records from 18 States.

Mr. Goldsborough. Have you a record from Maryland?

Mr. Fox. Yes, sir.

The Chairman. Before you leave that, do you attempt to include these estimated and unrecorded losses as a part of the total embraced in your figures?

Mr. Crowley. No. As I understand it, Mr. Chairman, the $3,000,000,000 of loss has been determined from the actual liquidations; is that correct, Mr. Fox?

Mr. Fox. Yes; from the actual figures.

The Chairman. Then there are no figures based on that, so it is not so material.

Mr. Crowley. The charts which I will later file show, by years from 1864 to 1934, the percentage of national and other commercial banks suspending and the ratio of deposits in suspended banks to deposits in active banks. The ratio of deposits in suspended banks to total deposits in all active banks is smaller for national than for other commercial institutions.

In other words, the loss from 1864 to 1934 was considerably less in the national system than it was in the State system.

Our estimates indicate that about 1 billion dollars of the 9 billion dollars which was on deposit in commercial banks that failed during the 70-year period were secured by pledge of collateral or otherwise. Of the remainder, some 6 billion dollars were in accounts of less than $5,000 or constituted the first $5,000 of large accounts. In other words, 6 billion dollars were within the $5,000 limit. Two billion dollars represents the volume of these deposits which were in accounts with balances above $5,000. The estimates of the amount of funds representing balances in excess of $5,000 were made on the basis of figures showing deposits classified by size of accounts in national banks in 1918, in member banks of the Federal Reserve System as of May 13, 1933, and in all insured commercial banks as of October 1, 1934.

For every $100 of deposits in the entire commercial banking system, about 32 cents a year was lost. Of this figure, it is estimated that 24 cents represents losses to depositors with balances not in excess of $5,000, while the remaining 8 cents represents losses to depositors having balances in excess of $5,000. For every $100 of deposits in the national banking system, 21 cents per year was lost as against 42 cents per $100 per year in the State system. The following table summarizes the estimates of losses to depositors in suspended national and other commercial banks during the 70 years ending June 30, 1934.

(The table referred to is as follows:)

Losses to depositors in suspended commercial banks July 1, 1864–June 30, 1934

	All commercial banks	National banks	Other commercial banks
Deposits in suspended banks (millions of dollars)	$8,778.00	$2,715.00	$6,063.00
Secured	1,033.00	184.00	849.00
Unsecured under $5,000	5,762.00	1,675.00	4,087.00
Unsecured over $5,000	1,983.00	856.00	1,127.00
Estimated losses (millions of dollars)	3,113.00	1,015.00	2,098.00
Secured deposits	(1)	(1)	(1)
Unsecured deposits under $5,000	2,301.00	667.00	1,634.00
Unsecured deposits over $5,000	812.00	348.00	464.00
Average loss per year for each $100 of deposits in active banks	.32	.21	.42
Unsecured deposits under $5,000	.24	.14	.33
Unsecured deposits over $5,000	.08	.07	.09

[1] Negligible.

Mr. Crowley. Losses to depositors have been most severe during the periods of business depression. Two-thirds of the losses during this entire 70-year period resulted from bank suspensions occurring during the 4 years ending June 30, 1934. In other words, two-thirds of the losses in the banking system in this country took place from 1929 to June 30, 1934. For these 4 years losses to depositors are estimated at $1.32 per year for each $100 of deposits in the commercial banking system. Comparable losses during the depression of the 1870's amounted to 35 cents, and during the depression of the 1890's amounted to 23 cents. The figures for the early periods understate the losses, but it is apparent that the losses in these earlier periods were not as great in proportion to total deposits as during the past 4 years. The data are summarized on the following tables. The first shows the losses in commercial banks which suspended and did not reopen during the three depression periods; the second compares losses during the 14 years included by the three critical periods, with the other 56 years since 1864.

(The tables referred to are as follows:)

Losses to depositors in commercial banks suspending during periods of crisis, banks which did not reopen

[Federal Deposit Insurance Corporation, Division of Research and Statistics]

	All commercial banks [1]		
	1873–78	1892–97	1931–34
Deposits in suspended banks (millions of dollars)	$85.00	$134.00	$5,356.00
Secured	10.00	13.00	637.00
Unsecured under $5,000	66.00	103.00	3,256.00
Unsecured over $5,000	9.00	18.00	1,473.00
Estimated losses in deposits (millions of dollars)	26.00	43.00	2,142.00
Secured deposits	(2)	(2)	(2)
Unsecured deposits under $5,000	23.00	36.00	1,478.00
Unsecured deposits over $5,000	3.00	7.00	664.00
Average loss per year for each $100 of deposits in active banks	.35	.23	[3] 1.28
Unsecured deposits under $5,000	.31	.19	.89
Unsecured deposits over $5,000	.04	.04	.40

[1] Periods beginning on July 1 and ending on June 30 of the years specified.
[2] Negligible.
[3] If losses of banks which subsequently reopened are included, the average loss per year for each $100 of deposits in active banks is raised to $1.32.

Losses to depositors in suspended banks, July 1, 1864–June 30, 1934, 3 crisis periods contrasted with the remaining years, all commercial banks

[Federal Deposit Insurance Corporation, Division of Research and Statistics]

	70 years, 1864–1934	14 years during 3 crisis periods [1]	Remaining 56 years
Deposits in suspended banks (millions of dollars)	$8,778	$6,084	$2,694
Secured	1,033	716	317
Unsecured under $5,000	5,762	3,738	2,024
Unsecured over $5,000	1,983	1,630	353
Estimated losses (millions of dollars)	3,113	2,269	844
Unsecured deposits under $5,000	2,301	1,578	723
Unsecured deposits over $5,000	812	691	121
Average loss per year for each $100 of deposits in active banks	.32	1.17	.11
Unsecured deposits under $5,000	.24	.82	.09
Unsecured deposits over $5,000	.08	.36	.02

[1] Includes figures for banks suspending during period July 1, 1930, to Mar. 15, 1933, which subsequently reopened.

Mr. Crowley. The experience of the past 70 years indicates that to repay losses suffered by all depositors in our suspended commercial banks, an assessment of 33 cents per $100 of total deposits, or one-third of 1 percent of total deposits in all open commercial banks, would have been necessary. Excluding the losses incurred during the three depression periods—1873–78, 1892–97, and 1931–34—and confining ourselves to losses occurring during the balance of the 70 years, an assessment of one-eighth of 1 percent would have been necessary.

In the past, the number, timing, and geographic concentrations of bank suspensions have been chiefly due to fundamental weaknesses in banking structure and the course of economic events. Suspension of individual banks within the areas affected has reflected, in the main, the quality of bank management. In the future, the magnitude of losses which will result from bank failures will also depend upon the trend of economic events, the changes which may occur in the structure and functions of the commercial banking system, the caliber of the individual bank management, the extent to which the system is reinsured against defalcations, and the quality of the supervision exercised over these banking institutions.

Of course, the future trend of economic events cannot be forecast.

Changing tendencies are now apparent in the structure and functions of commercial banking. On the one hand, the drastic reduction in the number of banks during the past 14 years has greatly relieved the overbanked condition in many communities. On the other hand, new financial agencies, serving specialized needs, have been created, and will compete, to some extent, with commercial banks. The types of credit which may be extended by commercial banks may be subject to varying degrees of risk.

The extent to which the caliber of bank management will improve in the future, over what it has been in the past, cannot be estimated. While it is hoped that a better quality of personnel will develop, it must be recognized that there will continue to be poorly managed banks and that such institutions will eventually succumb. We cannot foretell the extent to which the existence of deposit insurance will influence bank management.

To establish a fair rate of assessment which the banks shall pay for Federal deposit insurance, the hopeful expectations of the future must be tempered by a consideration of the realities of the past. Let me repeat that a premium at the rate of one-third of 1 percent of total deposits would have been necessary to cover all losses to depositors during the past 70 years. A premium at the rate of one-eighth of 1 percent would have covered depositors' losses in all years except those of severe depression.

We are concerned next with the basis of assessment and with the ability of the banks to pay the required amount.

The existing permanent insurance law provides that all insured banks may become liable for an uncertain number of successive assessments. It is not sound deliberately to subject an operating business to an unpredictable liability. The maximum rate and number of assessments should be fixed so that an insured bank may know in advance its potential liability to the Corporation. An annual premium of a known maximum amount constitutes a sound basis for insurance revenue, as it provides a specific payment to cover a clearly defined risk for a definite period of time.

We also believe that payments made by insured banks should be in the form of premiums, rather than through the purchase of stock. As in the case of other insurance companies, receipts from premiums should be added to the reserve funds of the Corporation. Such reserve founds should not be considered an earning asset of the insured banks. The interest received by the Corporation from the investment of reserve funds should not be made on the basis of dividend payments.

It is recommended that assessments be based upon total deposits in insured banks, regardless of whether or not the insurance is limited to $5,000 per depositor. To base assessments solely on the first $5,000 of each depositor's account places an undue burden upon the small banks, since most of the accounts of these institutions are less than that amount. It does not necessarily follow, however, that the greatest risk to the Corporation lies in these institutions. On the contrary, it has been demonstrated frequently in recent years that the consequences of the failure of a large bank may be more disastrous than the failure of a number of small institutions. The closing of a large bank often brings in its wake the failure of correspondent institutions.

The benefits of deposit insurance are not limited solely to the protection of the individual depositor. The entire banking structure of the country is so intimately interwoven that a disturbance in any part of the system may cause repercussions of far-reaching proportions. The benefits which will accrue to the large city banks because of great stability in the country banks are real and tangible.

All banks, large and small, should be required to support the insurance system. Banking is no longer merely a private business proposition. It involves great social consequences. The stability of the banking system affects the economic prosperity of the country. The raising of a sufficient revenue, solely through the levying of premiums against the deposits of those receiving direct insurance benefits will not be a fair distribution of the burden.

Our analysis of the ability of the banks to pay assessments is confined solely to the national banks since adequate data for other institutions are not available. The figures for earnings, profits, and dividends of national banks since 1870, as published by the Comptroller of the Currency, have been used. If the operating result of national banks can be taken as criteria, the banking system as a whole could have paid its losses during the past 70 years without impairing its stability or the payment of reasonable dividends to stockholders.

Operating profits of the banks have been below normal during recent years. The condition is reflected not only in reductions in gross earnings but also in unusually heavy write-offs made necessary by shrinkage in values. As we come out of the depression, losses on existing credits will appear. Banks should charge off these losses currently as they develop. They should not allow them to accumulate as was frequently the case prior to the banking holiday of 1933. These losses may absorb a considerable part of the banks' earnings over the next few years. To ask the banks to bear the entire cost of insurance at a rate comparable to the experience of losses over the past 70 years would subject them to a heavy burden at the present time.

It is probably true that after the period of adjustment has been completed, the banks' earnings will enable them to pay an assessment adequate to cover losses at the rate shown for the past 70 years. To ask them to do so, however, without making some effort to reduce the burden of losses seems to me to be unfair to the banks and to the public, which must ultimately bear the cost. This factor prompts us to ask for specific powers which will reduce these losses so that the insurance plan can be operated upon a reasonable assessment basis.

The following table compares annual averages of earnings, expenses, losses, and profits of the national banks for the years 1918 to 1930 with similar figures for the 6 months' period ending December 31, 1933. If charge-offs during the last half of 1933 had been no heavier than the average for the years 1918 to 1930, the national banks would have shown net profits of more than $1 for each $100 of total deposits, or more than $7 for each $100 of invested capital.

(The table referred to is as follows:)

Earnings, expenses, losses, and profits of national banks averages for 1918–30, compared with 6 months ending Dec. 31, 1933

Items	Amounts per year per $100 of total deposits		
	Average 1918 to 1930	6 months ending Dec. 31, 1933 [1]	Change
Gross earnings plus recoveries	$6.46	$5.18	−$1.28
Interest paid	1.92	1.05	−.87
Other expenses	2.44	2.18	−.26
Net earnings plus recoveries	2.10	1.95	−.15
Losses on loans and investments	.81	3.76	−2.95
Net additions to profits	1.29	[2] 1.81	−3.10

[1] The figures for the 6 months have been adjusted to show a rate per year, rather than for 6 months only.
[2] Deficit.

Mr. CROWLEY. It will be noted that the expenses of operating national banks were considerably lower in 1933 than during the period 1918 to 1930. Most of this reduction was due to a decline in the average rate of interest paid on deposits. About two-thirds of this reduction in interest occurred before the Banking Act of 1933 became effective and reflected the general decline in money rates. One-third of the reduction took place after the passage of the act, reflecting almost entirely the prohibition against the payment of interest on demand deposits. The savings in interest on account of this change in the law amounted to 26 cents for each $100 of total deposits, or more than the premium necessary to cover losses on deposits insured up to $5,000, as indicated by the experience of the past 70 years.

The cost of insurance will not be disproportionately heavy in relation to earning power if paid by banks in proportion to their total deposits. If insurance be limited to $5,000 for each depositor and the cost is distributed among the banks in proportion to their insured deposits, the payments by smaller banks would be nearly double the assessments distributed on the basis of total deposits. In other words, we have over 13,000 banks that are insured 70 percent or greater; and if you place your premium on the insured portion only, it is going to very materially raise the assessment on those 13,000 smaller banks.

We have recommended not only that subscriptions by insured banks to capital stocks of the Corporation be eliminated but also that the Corporation be given the right to allocate to surplus any portion of the some $300,000,000 paid to it by the Treasury and the Federal Reserve banks. If the amounts paid in subscriptions to stock were to be carried in full on the books of the Corporation as capital stock, the Corporation would be unable to pay any losses except out of income, over and above operating expenses, without impairment of its capital. The Corporation would have no surplus; and while it might legally be permitted to spend its capital in meeting its obligations, a substantial capital impairment shown in its published reports would have a most adverse effect upon public confidence. We are therefore recommending that the stock issued by the Corporation to the Federal Reserve banks and the Treasury be without par value, and that the balance be placed in a surplus or reserve account.

Until such time as the resources of the Corporation may be adequate to handle the volume of anticipated losses it would be very unwise for the Corporation to pay dividends. We therefore recommend that the payment of dividends be eliminated.

It is important that the Corporation be given adequate means for increasing the funds at its disposal during critical periods. It is doubtful, however, if at such times the Corporation could borrow from private sources. The United States Treasury is the logical purchaser of these obligations. The Government is vitally interested in the maintenance of the country's banking system. We recommend that the obligations of the Corporation be issued only with the approval of the Secretary of the Treasury, so that any credit which the Corporation may require shall not conflict with the financial policies of the Government.

The success of deposit insurance depends upon the soundness of the insured banks. In my opinion the two major objectives of those administering the affairs of the Federal Deposit Insurance Corporation should be, first, to assist in making the insured banks sound financially and, second, to keep them in sound shape.

During the past year the activities of the Corporation have been chiefly concerned with the first of these problems, that is, the rebuilding of the capital structures of insured banks. In the future, the Corporation should devote a large part of its efforts to the maintenance of sound conditions among the insured institutions.

To maintain sound conditions among all insured banks it is essential that the Corporation have the power to control the admission of banks to the insurance fund. We cannot return to the overbanked condition of 1920 if we wish to have a sound banking structure. The growth of excessive banking facilities was one of the most destructive influences which existed prior to the banking holiday of 1933.

Since the banking holiday much effort has been expended in reorganizing and relicensing banks in order that the frozen funds of the depositors might be released. The accompanying table indicates that more than 2,000 banks have been added to those which withstood the shock of the banking crisis.

(The table referred to is as follows:)

Newly licensed banks grouped according to volume of total deposits by class of bank, July 1, 1933 to Dec. 31, 1934 [1]

[Deposit figures in thousands]

	July 1, 1933 to Dec. 31, 1934					
	Number of banks			Aggregate deposits [2]		
	National	State	Total	National	State	Total
Banks with deposits of—						
$100,000 or under	25	379	404	$2,070	$22,905	$24,975
$100,001 to $150,000	29	222	251	3,624	27,528	31,152
$150,001 to $250,000	131	268	399	25,862	50,956	76,818
$250,001 to $500,000	219	248	467	78,988	87,635	166,623
Subtotal	404	1,117	1,521	110,544	189,024	299,568
$500,001 to $750,000	110	90	200	67,346	55,735	123,081
$750,001 to $1,000,000	58	42	100	50,765	36,665	87,430
$1,000,001 to $2,000,000	76	65	141	104,282	88,732	193,014
$2,000,001 to $5,000,000	44	35	79	131,970	102,133	234,103
$5,000,001 to $10,000,000	16	6	22	113,573	35,067	148,640
$10,000,001 to $50,000,000	5	3	8	91,414	51,860	143,274
Not available	6	88	94			
Total	719	1,446	2,165	669,894	559,216	91,229,110

[1] By "newly licensed" is meant existing banks reopened, banks reorganized, and primary organizations.
[2] Deposit figures for the most part as reported in Rand-McNally Bankers' Directory for July 1934.

Source: Card records of newly licensed banks maintained by the Division.

Mr. Crowley. Under present conditions, the Corporation insures all newly licensed banks which apply for insurance, if they are found to be solvent. Approximately 90 percent of the newly licensed institutions have become insured. The Corporation should be granted the specific power to refuse the admission of new banks into the insurance fund where such admission would weaken the banking system. The Corporation should also be given the specific right to require a higher standard than mere solvency for admission to the insurance fund.

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It is my firm belief that every community which can produce a sufficient volume of deposits to support a bank should receive the advantages of such facilities. There are many localities throughout the United States, however, which can support only one or two banks. To establish a second or third bank in such communities leads to speculative and destructive practices in an effort to earn sufficient income to pay expenses. For the protection of the insured institutions, the Corporation and the public welfare, the admission of banks to the insurance fund should be carefully supervised.

You understand that under our bill all of the banks that are now members, State banks and member banks, automatically come into the permanent fund, without being certified over again. The fact that they are now members automatically washes them into the fund, so that the only thing you are dealing with is the banks that are outside of the fund, or banks that may be chartered in the future.

The CHAIRMAN. It might be well to state in that connection that under the act for the insurance of bank deposits all national banks and State banks of the Federal Reserve system were automatically admitted into membership or participation in the benefits of the Deposit Insurance; were they not?

Mr. CROWLEY. That is correct.

It is for these reasons that we have recommended that the legislation incorporate specific standards to be met by future applicants before admission to the benefits of deposit insurance. These standards have already been recognized by Congress in other legislation.

In the latter part of 1933, banks were admitted to membership in the insurance fund under exceptional conditions. The situation existing at the close of 1933 was critical. The lack of real public confidence in banks was unsettling. Congress, therefore, provided that all solvent banks should be admitted to the insurance fund even though their capital was impaired in a number of instances. However, the Corporation immediately undertook to assist all banks which needed it in rebuilding their capital structures and correcting capital impairments which our examinations had disclosed.

The capital rehabilitation of banks was to be effected either through local contributions or through the facilities of the Reconstruction Finance Corporation. The Insurance Corporation assisted State nonmember banks to rebuild their capital structure. The responsibility for the condition of national and State member banks rests with the Comptroller of the Currency and the Federal Reserve Board, respectively. The Comptroller of the Currency and the Federal Reserve Board had the right to insist that banks under their jurisdiction accept necessary aid. The Corporation, however, had no such power. To accomplish the task of rebuilding the capital of a nonmember State bank which had been admitted to the benefits of insurance, the Corporation could only use the power of rational appeal to the board of directors or to the State banking authorities. Without the cooperation of the State banking authorities the capital structure of nonmember banks would not have been rebuilt.

State nonmember banks which could not obtain local capital contributions were assisted in securing aid from the Reconstruction Finance Corporation. Banks which had already made applications were assisted in complying with the conditions laid down by the

Reconstruction Finance Corporation. The accompanying table reveals the extent of the aid extended by the Reconstruction Finance Corporation to the various classes of banks in this country. While it is true that by the close of 1934 Federal Reserve member banks—State and national—had received almost three times as much Reconstruction Finance Corporation aid as had nonmember banks, in proportion to total deposit liability the aid given nonmember banks was twice as great as the assistance extended member banks.

(The table referred to is as follows:)

Reconstruction Finance Corporation purchases of capital obligations of insured banks

[In millions of dollars]

	National banks	State member banks	Insured nonmember banks (excluding mutuals)	Total insured banks (excluding mutuals)
Total deposits, June 30, 1934 [1]	$19,896	$11,116	$4,746	$35,814
Capital surplus and undivided profits, June 30, 1934 [1]	2,843	1,886	1,005	5,752
Net R. F. C. contribution to capital to June 30, 1934 [1]	384	202	184	773
Ratio R. F. C. to total deposits (percent)	1.9	1.8	3.9	2.2
Ratio R. F. C. to total capital (percent)	13.5	10.7	18.3	13.4
R. F. C. cumulated disbursement to all banks, Feb. 1, 1935 [2]	465	238	256	959
Ratio of item 6 to item 1 (percent)	2.3	2.1	5.4	2.7
Ratio of item 6 to item 2 (percent)	16.4	12.6	25.5	16.7

[1] Call Report of Insured Banks No. 1.
[2] As reported by the R. F. C.

Mr. CROWLEY. In some instances the necessary capital reconstruction had hardly been accomplished when applications were made by the banks to retire the preferred stock or debentures purchased from the Reconstruction Finance Corporation. As has been indicated, the capital reconstruction program was carried out for the purpose of protecting not only the banks but the Insurance Corporation. The capital and surplus of banks constitute a guaranty fund to depositors. They represent a cushion for the liability of the Corporation. When this capital and surplus are exhausted through losses, the depositor must turn to the Insurance Corporation for the payment of his deposits. The Corporation is vitally concerned, therefore, with the amount and condition of the capital and surplus of insured institutions. The reduction of this cushion of safety should be permitted only after obtaining the approval of the Corporation. If banks are allowed to retire this new capital, the rehabilitation, which has been so tediously accomplished, would be of no avail. The Corporation should have the right to control any future reductions in capital by insured banks.

The Corporation should have the right to review all mergers and consolidations affecting insured banks. It is possible that banks which have been refused admission to the insurance fund may be absorbed by insured institutions, thus extending the liability of the Corporation to depositors of the absorbed bank. Under the existing conditions there is no way in which such a subterfuge could be prevented.

In the interests of the depositor the Corporation should have the right to refuse to give its stamp of approval to inequitable or unsound reorganizations. Last year the Corporation was called upon to review more than 700 such plans. Many of those which we have seen are inequitable. The Corporation should have the right to pass upon the justice and soundness of reorganization plans. Depositors have often made tremendous sacrifices without the comparable sacrifice by stockholders and other special groups.

The Corporation now has the right to buy assets of closed Federal Reserve member banks. We have recommended that this right to purchase be extended to operating insured banks until July 1, 1936, whenever such action will avert an impending loss and facilitate a merger or consolidation. It will be to the best interests of both depositors and the Corporation if, through the absorption by the Corporation of a comparatively small loss, a more serious loss will be averted. Furthermore, such a procedure will offer both an incentive and a method for completing the rehabilitation of all insured banks prior to July 1, 1936. The right to purchase assets from operating banks should not be exercised unless in conjunction with a merger or consolidation and only for the purpose of averting loss.

Bank failures are frequently precipitated by defalcations. We, therefore, recommend that the Corporation be given the right to require adequate fidelity and other insurance. Such insurance provides protection to depositors, to bank executives, and to the Corporation. Where a given institution does not carry sufficient insurance, the Corporation should be given the right to contract for such insurance and charge the bank therefor.

A method whereby nonmember banks may withdraw from the insurance fund should be included in the legislation. Banks leaving the insurance fund should give adequate notice to the Corporation and to their depositors. However, such withdrawals should not expose the depositors to a sudden cancelation of the protection afforded them, and the insurance benefits should be extended to the depositors for 2 years after the withdrawal of any bank.

We also believe that the Insurance Corporation should have the right to terminate the insurance of any bank if, after a hearing and after notice to depositors, such action is in the best interests of both depositors and the Corporation. In establishing deposit insurance, Congress has assumed not only a definite responsibility to bank depositors but also a moral obligation for the sound management of banks. If the Corporation finds that an insured bank is engaged in repeated practices detrimental to the depositors, the Corporation should not be placed in the position of sanctioning such practices but should be given the right to terminate the insurance of the bank's deposits without jeopardizing the depositors. For the protection of depositors, we have recommended that in such cases insurance be extended for 2 years from the time that membership in the fund is terminated.

The right of dismissal may seem to be somewhat drastic, but it is hoped that the use of this power may seldom be necessary. As an intermediate step and as a means of notifying the public, it is suggested that the Corporation be authorized to publish either all or such portions of examination reports as it deems necessary. The State supervisory authorities will be advised of the intention to publish all or part of the examination report and only after adequate notice has been served on the executives of the bank concerned will such action take place. This procedure is designed to allow sufficient time for the executives of the bank concerned to correct the practices which jeopardize the safety of the depositors' funds. The Comptroller of the Currency has this right in the case of national banks.

Reports of condition now being issued to the public are confusing because of their inadequacy and lack of uniformity. Considerable efforts have been made to study this question. Conferences have been held with the State and Federal supervisory agencies in an effort to develop standard and uniform reports of condition. In order that the public may be informed as to the status of the institutions with which they do business, periodical statements of condition should be required of all banks.

Revision of the provisions of the law reciting the obligation of the Corporation to pay the insured deposits of a closed insured bank is necessary. As it now stands, the law requires the Corporation to organize a new national bank to act as its instrumentality in paying the insured deposits of every closed insured bank. This procedure must be followed, even though there is not the slightest possibility of the community being able to capitalize the new national bank. Eleven insured banks have thus far closed, but in only one instance were the local people in a position to capitalize the new bank.

This procedure for paying insured deposits has proved unsatisfactory, since it involves needless expense and many unnecessary accounting problems which could be eliminated if the Corporation were permitted to pay its obligations in the same manner as other insurance companies engaged in the commercial field. Accordingly, it is proposed that the organization of a new bank be at the discretion of the Corporation.

Under the present law, where it pays the insured portion of a deposit claim which is larger than $5,000, the Corporation becomes subrogated to the entire amount of the depositors' claim until it is reimbursed for the amount paid out to the depositor. This is manifestly inequitable to the larger depositors. We believe that the Corporation should be subrogated only to that portion of the claim which it pays, the depositor retaining his claim for any insured portion and receiving all dividends payable thereon directly from the liquidating officer. In the case of every closed bank there are some depositors who can never be located by reason of death, disappearance, or change of residence. We believe claims which are not filed within 1 year after an insured bank is closed should not be paid by the Corporation. This suggestion finds ample precedent and will enable the Corporation to close its books on each pay-off within a reasonable period.

The bill before you includes suggestions for clarification of provisions of the existing law about which some doubt has arisen. The adoption of these provisions will facilitate administration.

We recommend that the maximum limit of insurance to any one depositor be retained at the present figure of $5,000. Congress, in establishing deposit insurance, was presumably most concerned with the mass of depositors with small accounts. Our reports cover 51,000,000 accounts, of which over 98 percent are fully insured with the $5,000 limitation. Many of the accounts not fully covered are interbank accounts, public funds, deposits of corporations, institutions, and trust estates. The actual number of individuals with deposits in excess of $5,000 is probably less than 1 percent of the total number of depositors. Out of the 14,000 insured banks, over 9,600 have more than 80 percent of their deposits insured under the $5,000 limitation. To raise the limit of insurance above $5,000 would materially increase the maximum possible liability of the Corporation. If all the deposits were insured, this would be more than doubled. It would be increased from the present 16½ to nearly 30 billion dollars by the permanent plan which now exists in the statute. This tremendous increase in the maximum possible liability of the Corporation would benefit only one out of each hundred bank depositors.

The Insurance Corporation's interest in the sound operation of banks is more tangible and more vital than that of any supervisory authority. Deposits in practically all commercial banks and trust companies of the United States are insured by the Corporation. Bank supervisory agencies have a responsibility to the depositing public, and it is their duty to see to it that the bank laws are properly enforced. The Corporation, however, has a financial liability to these depositors. Its interest in the sound operation of these institutions is one of dollars and cents.

There are two courses open to the Insurance Corporation. It may be a charitable institution which will pay for the mistakes, bad banking, and dishonesty of bankers, in which case the cost of the insurance must be set so high that it will be an injustice to every sound bank. Or, by being placed on a sound basis, the Corporation may be used as an instrument to improve the standards of bank management and reduce the losses to depositors through bank failures. The latter course, which I prefer, requires that the standard of bank supervision throughout the country be improved, that the Corporation be given the right to protect itself against excessive risks, and, finally, that the Corporation be not handicapped by taking into the fund banks which are unsound or by continuing in the fund banks which are mismanaged.

We have a number of charts, Mr. Chairman, and we would be glad to answer any questions.

The CHAIRMAN. I would suggest, Mr. Crowley, that the charts that are pertinent and connected with your statement might well be appended as a part of your statement and published in the hearings at the proper place. Without objection, that will be done.

Mr. FORD. If a bank is put out of the fund, does the bank continue to pay the assessment?

Mr. CROWLEY. Yes, sir. We collect the assessment for this reason: The deposits of that bank remain insured for 2 years. If we put a bank out of the fund we have naturally got to go in there from time to time to look after our interests, and they must pay the premium.

Mr. HOLLISTER. Even if the bank withdraws voluntarily?

Mr. CROWLEY. Even if the bank withdraws voluntarily, they must pay for 2 years. The reason for that is this: That you may put some money in a bank, believing it to be insured, and if it withdraws from the fund tomorrow you may be the victim of a misunderstanding. So we believe the depositors should be given a reasonable protection before our liability ceases.

Mr. HOLLISTER. Isn't it also a protection of the fund? Isn't it true that some banks would like to withdraw from the fund in order to escape responsibility for assessments? That would be a great weakening of the fund, would it not?

Mr. CROWLEY. Correct.

Here is another thing. Banks may come into the fund in order to obtain the psychological effect of having insured deposits. As they go along and find that it is going to cost them a little something they would like to get out. They might believe that they can live outside of the fund. They would like to come in in bad times and get out in good times and have the door swinging both ways for them. That is very unsound. I think, for the sake of the whole banking system, every bank in the United States should be forced to be a member of the Federal Deposit Insurance Corporation. Then you would have uniformity all the way through.

Mr. REILLY. Don't you think there is going to be little opposition amongst the banks, except the large banks?

Mr. CROWLEY. The cost of the insurance that we have recommended to the small banks is very nominal. To 13,000 banks it is a very nominal sum. There will be no excuse, in my opinion, for the smaller banks getting out of the fund on account of the cost of this insurance, because it is not excessive.

Mr. CROSS. It is the big banks, you think, that are asking to get out?

Mr. CROWLEY. I do not believe it is. If this corporation were properly set up and properly sold to the depositors, I do not think many banks could live outside of this fund, and I think that is the way it should be.

Mr. KOPPLEMANN. I am very much interested in what you said a moment ago, that every bank ought to be compelled to belong to the Insurance Corporation. You know, of course, the difficulty we have had in my State, Connecticut. Is there anything in this law which would either compel the banks to come in, or make it so attractive that they would come in?

Mr. CROWLEY. There are only 1,100 banks outside of this fund now.

Mr. KOPPLEMANN. I am specifically interested in Connecticut, and in the Nation as a whole, because of the difficulty we have had.

Mr. CROWLEY. I think that whole question is going to be answered when we get our permanent law. If it is a law that we can all get behind and support and sell to the depositors, and if the cost is not excessive, I do not believe the banks of very many States can afford to stay out of the system.

Mr. KOPPLEMANN. Is not the real reason they did not want to come in, this feature of examination, which they look upon as an interference?

Mr. CROWLEY. You do not get so much objection to the examination from a good bank. Our experience indicates this, that the objection to examination comes from the fellow who should be examined often. Your better institutions do not object to regulation.

Mr. KOPPLEMANN. What I am trying to get at is how we are going to get these 1,100 banks in. Have you got anything in the law on that?

Mr. Crowley. No; but I think we have quite a few applications before us now, have we not, Mr. Fox?

Mr. Fox. Yes; we have.

Mr. Crowley. We have been in operation 15 months, and we have some 8,760 State banks which are insured. There are only 1,100 licensed banks outside of the entire system.

Mr. Kopplemann. I believe the depositors throughout the Nation are 100 percent for this thing, except those who have been told, as they were in my State, that it is a terrible thing, and because they do not have the facts, they believe that statement.

Mr. Crowley. We have had some opposition from the bankers, because there were doubts in their minds. For instance, they had an unlimited liability hanging over them. I think if that and some other features were straightened out you would get the cooperation of a great many of your financial institutions—especially if you give to this Corporation some regulatory powers, so that it might have a part in holding up your banking system.

Mr. Goldsborough. I have noticed in several banks a sign reading, "The deposits in this bank insured by the Federal Deposit Insurance Corporation." That creates the impression that all the deposits are insured. Is there anything in this bill which would require those signs, when they are put up, to show what the limitation is?

Mr. Birdzell. Yes. I think you may have an erroneous impression of the effect of the present sign. The present sign that we have adopted shows the amount right on the sign.

Mr. Goldsborough. I did not mean that the sign of the Federal Deposit Insurance Corporation was misleading, because I was talking to a Congressman the other night, and he said that in his territory the signs all disclose the amount of the insurance, but I want to say that I have seen this misleading sign and it does not seem to me that it ought to be allowed.

Mr. Birdzell. From the very beginning we have used the utmost care to prevent advertising being put out that would be misleading to the public in that respect.

Mr. Hancock. Mr. Crowley, what would be the annual return to your insurance fund, based upon one-twelfth of 1 percent of the total?

Mr. Crowley. About $30,000,000, Congressman Hancock, per year.

Mr. Hancock. What would the assessment amount to?

Mr. Crowley. About $30,000,000, and income from the investment would amount to about $9,000,000.

Mr. Hancock. Under the proposed new bill, is the levying of that assessment mandatory or discretionary?

Mr. Crowley. We have the right to reduce it, but not below 50 percent. In other words, we have a refunding provision in there, after we get our reserves built to a certain point.

Mr. Hancock. Is it your purpose and intention to levy an annual assessment every year?

Mr. Crowley. Yes; and that would have to be, because you will have to build your reserves for the future, in order to take care of some unforseen obstacle. If you do not do that, but only try to assess in times of difficulty, you are going to create additional hardships when banks are already subjected to as great a load as they can carry.

Mr. HANCOCK. I know that you have been making an exploratory inquiry into this subject, and I am interested to know, as a result of the figures and reports you have got, whether it is true that 1 percent of the people in this country own and control 60 percent of the deposits in the banks?

Mr. CROWLEY. I think that 800,000 individuals and corporations control about 65 percent of the deposits.

Mr. REILLY. Corporations too?

Mr. CROWLEY. They are included in depositors.

Mr. GIFFORD. You said a good deal about the impairment of the capital. When the R. F. C. provides a new capital structure, is it easy for the banks to withdraw and repay the R. F. C.? Can you explain to the committee what the conditions are they have to meet before they are allowed to repay? Do you want to have something to say about it?

Mr. CROWLEY. Yes. Let me say this: We have gone out in the last year and have aided, with the help of the Reconstruction Finance Corporation, in strengthening very nearly 3,500 out of some 7,800 State banks in this country not members of the Federal Reserve System. The difficulty is this, that we go out and we work with the stockholders and directors and everyone, getting that money in the bank. A lot of these banks seem to confuse liquidity with capital position. In other words, because their deposits are increasing, although they may not have any capital to speak of, they feel that they should be able to pay back the Reconstruction Finance Corporation. What we want is this, that after doing this great job that has been done, these banks should not be permitted to again weaken their capital structures by repaying the R. F. C. unless some local contribution is made, or unless earnings place the banks in such a position that they will have sufficient capital to form an adequate cushion for the protection of the depositors and this Corporation. These banks should not be allowed to undo the constructive work of the past 15 months.

Mr. GIFFORD. As I understand it, many banks have come and applied to the R. F. C., in order to get this capital structure, because they were forced to mark off and mark down a considerable fund, and to meet that contingency they felt it necessary to add to their capital structure, but when that contingency seemed to have passed, and the bank was in perhaps better shape, they desired to get rid of the R. F. C., because the public at large felt that if they had to apply to the R. F. C. they necessarily must be involved. When they have gotten out of the condition that the examiner has forced them to remedy, are you going to resist their dismissal of the R. F. C.?

Mr. CROWLEY. I do not think we would object, provided they really have corrected that condition.

Mr. GIFFORD. Isn't it a case of resisting sometimes, because there is another second examination, one by you and one by the national bank examiner? Doesn't that defeat them?

Mr. CROWLEY. No. There is no duplication in Federal examinations. We do not examine a national bank, nor do we examine a State member bank. We take the examination report of the Comptroller and the Federal Reserve.

Mr. GIFFORD. I had assumed that you did, and by this talk this morning had suggested that you wanted the power to refuse. Are you going to take another examiner's word for the condition?

Mr. CROWLEY. Are you talking about banks coming into the fund?

Mr. GIFFORD. Yes.

Mr. CROWLEY. With regard to the requirement for banks coming into the fund, the Comptroller and the Federal Reserve may use the same yardstick as we are expecting the State banks to use, for admission to this fund.

In putting the banks out of the fund, we notify the Comptroller or the Federal Reserve or State supervisor of the condition that exists, and we give him 90 days time in which to make the correction. If it is not made we serve notice on the bank and give the bank the right of hearing.

As far as the capital-rebuilding program of the national banks is concerned, that has been done exclusively by the Comptroller. We have done it with the State nonmember banks only.

Mr. GIFFORD. Don't you realize that the public at large have the feeling that when the R. F. C. comes to the rescue of a bank it assumes more than 51 percent of the control? You realize that?

Mr. CROWLEY. That is not true. If you mean control of the individual bank.

Mr. GIFFORD. Yes.

Mr. CROSS. On the question of examinations you said you always accept the Comptroller's examination of a national bank and the Federal Reserve's examination of a member bank.

Mr. CROWLEY. That is right.

Mr. CROSS. But in this bill you ask for authority to make an examination, with the consent of the Comptroller and the consent of the Federal Reserve.

Mr. CROWLEY. That is done for this reason, that we are asking for the right to purchase assets in the case of consolidations and mergers. Suppose you had a national bank that was in some difficulty. We want the right to go in with the Comptroller and see if there is anything we might be able to do.

Mr. CROSS. You do not contemplate a general request to the Comptroller and to the Federal Reserve for examination of the institutions?

Mr. CROWLEY. No, sir.

Mr. FORD. Where the R. F. C. has purchased $100,000 of capital stock of a bank, in order to strengthen its structure, and in the course of 6 months they feel that they want to repay that, wouldn't it be a good idea to permit them to repay it, when capital is secured in the district to replace that sum?

Mr. CROWLEY. Let me say this to you gentlemen, that banks do not improve their position materially in 6 months' time.

Mr. FORD. Whatever the period would be.

Mr. CROWLEY. Oh, I agree with you—either through earnings or an improvement in conditions, or local contributions. Does that answer your question?

Mr. GIFFORD. Don't you understand that when there are three or four banks in one community, and all receive assistance from the R. F. C., but one is allowed to divest itself from the capital structure of the R. F. C., the public then begins to think that that bank may be a little bit stronger than the other two? Do you think that the public is very tender in its viewpoint of the strength of the local banks these days?

Mr. CROWLEY. That may be true, but, as a matter of fact, what are you going to do if you have three banks and the impairment of one of them was less, and through its own local contributions or its own earning capacity it put itself in shape so that it could go on by itself? The Government can only stay in these banks until the banks are able to carry on themselves.

Mr. GIFFORD. That is what I asked you in the first place, if you were going to attempt to resist their repayment of the R. F. C.?

Mr. CROWLEY. No; I think Mr. Jones and everyone would be glad if the banks could pay back a billion dollars tomorrow, without weakening the banking structure, but we do not want them to pay it back if it is going to mean a weakened situation.

Mr. HANCOCK. The chairman of the Federal Deposit Insurance Corporation has made a very able, interesting, and comprehensive statement here, and one that deserves the best thought and study of our committee. I am wondering if he will be available to come back to us from time to time.

The CHAIRMAN. Oh, yes.

Mr. CROWLEY. Surely.

Mr. HANCOCK. To discuss this report and statement after we have had a chance to absorb it?

The CHAIRMAN. Surely.

Mr. DIRKSEN. The question is perhaps speculative, but here is a thought that was suggested to me last summer, when we were liquidating one of our banks in East Peoria, that probably one of the best insurances of good banking comes from the fact that the bankers look after each other somewhat. In other words, they are just as much interested to see that their neighbor indulges in good banking practice, because if the losses entailed should appreciate year after year it would mean that sometime or other your insurance premium would have to go up.

Mr. CROWLEY. That is right.

Mr. DIRKSEN. However, the banks in Wisconsin in the aggregate would have no way of looking after or having contact with the banks in Illinois.

Mr. CROWLEY. That is right.

Mr. DIRKSEN. Suppose, as time goes on, you find that a geographical classification of these losses discloses that they are infinitely higher in one State than in another. I have heard bankers raise the point that they are heartily in favor of this insurance, but if it should be developed that there were losses in other areas over which they have no control or with which they had no contact, it would constitute an unjust penalty upon them in that particular area. Has it ever occurred to you that at some time or other it may be necessary to think of classifying these insurance rates on the basis of the geographical areas? It would involve a lot of work, I know, but the equity involved must be considered.

Mr. CROWLEY. I do not think that would be a practical thing for the corporation, at least until the whole banking system is almost foolproof, for this reason, that the thing that is the best security for the corporation now is the diversification of risk which is spread over the entire country.

For instance, if you put the Middle West in a class by itself, and they have a drought like this last year, and they must stay on their own, you are going to make insurance for those banks so expensive that it is going to be almost prohibitory for them to belong to the fund.

As I see this thing, the bankers have got to take this viewpoint, that we had an almost complete collapse of the banking system in March 1933. You can hear people say, "We were still able to stay open" but the fact remains that the banking system, including the New York banks and other Federal Reserve member banks, had, for all practical purposes, broken down. The interest which the banks should have in the Federal Deposit Insurance is to help it build a banking system that will remain independent and sound. None of us can justify a continuance of our kind of banking system, (and I am an advocate of our present banking system) if we are to have a reoccurrence in 10, 15, or 20 years of the situation which existed in 1933.

Mr. GOLDSBOROUGH. Why does it require a recurrence? Why should you have to do it twice to prove it?

Mr. CROWLEY. I believe that the Federal Deposit Insurance does offer the vehicle for the correction of the banking system of this country. I am not talking about monetary control; I am talking purely of supervision.

Mr. GOLDSBOROUGH. In the last analysis, the Federal Deposit Insurance Corporation has access to no more money than the banking system itself has access to, and the banking system itself only has access to about $7,000,000,000, which is the entire capital, surplus, and undivided profits of all the banks, so that in the last analysis the Federal Deposit Insurance Corporation can do absolutely nothing except act as one means of maintaining the confidence of the people in the integrity of the banks, and thus avoid runs on the banks.

Mr. CROWLEY. Yes.

Mr. GOLDSBOROUGH. That is the truth of the situation.

Mr. DIRKSEN. At the present time one who goes to a bank and makes a time deposit can under no circumstances withdraw that money, even though he may waive all interest thereon. I understand that is embodied in regulation Q.

A man went into a small bank in my district, and he wanted to place $1,200 on time deposit, for 90 days. He said, "A contingency may arise whereby I might need the money. Can I get it out before that time in such a case?" They said, "No." He said, "Suppose I waive the interest?" They said, "You cannot get your money anyway." He went across the street and put his money in Postal Savings. He can put his money in the Postal Savings and if any portion of the money is there up to the interest pay day, he can even get interest, and get new certificates for the balance of his money. It occurs to me that there is a disparity between the obligation imposed by regulation Q and the practice of the Postal Savings System.

Mr. BIRDZELL. That is correct.

Mr. DIRKSEN. They ought to be brought into uniformity, because it is affecting these small banks. And it is not necessarily the fact that the bank loses income from the small deposit, but it is a fact that a man goes out of that bank and he says, "There is something wrong with this bank", and he does not realize the implications of regulation Q, and once he gets to talking to his neighbors, he impairs some of the local confidence in the bank, because of that lack of consistency in these systems at the present time.

Mr. Crowley. I do not think ours in inconsistent. I think ours is consistent, and theirs is inconsistent.

Mr. Dirksen. You mean the Postal Savings?

Mr. Crowley. Yes.

Mr. Dirksen. I agree with you, but I agree with you also that the practice ought to be uniform, and the Postal Savings should be compelled to do precisely as you do.

Mr. Birdzell. There is a feature of the law that you may be familiar with, which provides that where Postal Savings are permitted to be withdrawn without the service of the notice required by the Banking Act of 1933, no interest shall be paid except interest accruing prior to the effective date of the banking act. But notwithstanding that, apparently they are paying interest up to the date of withdrawal.

Mr. Dirksen. Precisely, and even if they did not pay interest it would only remedy one-half the problem, because a man could still go and deposit and withdraw the deposit, which he cannot do now under regulation Q.

Mr. Birdzell. Your statement is correct, I believe. Attention should be given to that matter, because there is some unfair competition between the Postal Savings and the banks. That is particularly true now, when the banks are paying low rates of interest.

The Chairman. Of course, many people hold the view that if you insure all deposits in private banks the Government should not set up and maintain a deposit institution in competition with them. It is contrary to sound public policy, and the necessity for it has been removed, and there is no excuse for it. That is what we attempted in the Banking Act of 1933, which has not been followed as was contemplated by the framers of the act, to at least require that the Government, insofar as it competed with the banks in the matter of deposits, should maintain a purely savings system and not regular checking accounts.

It might be well to state in that connection, I think, that we have quite a number of communities, and you might say sections of the country, where the banking facilities have been, for the time being at least, swept away, so that the only depository left for the citizen was the Postal Savings System. So that difficulty confronts us in undertaking to deal with that problem, but for my part I think we should in some way legislate on that subject.

Mr. Crowley. It will help eventually to correct a part of your banking trouble when the Postal Savings deposits are permitted to go into your small banks. They would get that volume of business that may be helpful to them, so that they may be able to make some money.

Mr. Dirksen. May I make one observation on the table on page 16 of Mr. Crowley's report? I see that in the first column, from 1873 to 1878, the deposits were $85,000,000 and the losses $26,000,000, so the loss was approximately 30 percent. From 1892 to 1897 the deposits were $134,000,000 and the losses $43,000,000, which was 32 percent. Then the deposits from 1931 to 1934 were $5,356,000,000 and the losses $2,142,000,000, which was a loss of about 40 percent.

I am merely remarking the facts, because at the bottom the average loss per year for each $100 of deposits of $1.28 seems disproportionately so much lighter than 30 percent and 40 percent.

Mr. CAVICCHIA. That is because it takes in a greater part of this.

Mr. DIRKSEN. That is probably true.

Mr. WOLCOTT. I am given to understand that a man may have a deposit guaranteed up to $5,000, and his wife may have a deposit guaranteed up to $5,000, and there is no question about those. Is the joint account, in addition to those guaranteed up to another $5,000?

Mr. BIRDZELL. Yes.

Mr. WOLCOTT. Is a bona fide trust account, as a part of that savings division, subject to this insurance?

Mr. BIRDZELL. That is an account held in another capacity.

Mr. WOLCOTT. I say "bona fide" to distinguish it from a mere creation of a trust fund to avoid the purposes of the act.

Mr. BIRDZELL. Under the terms of the law, in paying off a bank we have to combine all of the deposits of the particular claimant which he holds in the same capacity and the same right. If he holds them in different capacities—for instance, you may maintain a bank account in your bank in your private capacity, and you may be a member of a partnership that also has a bank account in that same bank.

Mr. WOLCOTT. I know, those are separate.

Mr. BIRDZELL. They are separate. If you and your wife have a joint account, that is an account held in a different right. It may be all collected by your wife, or may be all collected by you while the bank is operating, and we have the problem of offsets, and the same law that applies in solving the problem of offsets in the closing of a bank must apply and work harmoniously with regard to the insurance. We must treat each one separately.

Mr. WOLCOTT. Let us work that out in a practical way. Assume that a man and his wife have $20,000 between them, and the man has $20,000 in bank, in a joint account between himself and his wife, with the feeling that upon his death his wife will not have to administer his estate, or probate his estate, but she can go down and avoid any such probation by merely drawing that money out as a joint depositor. Then comes along the F. D. I. C., and my understanding is that they can take that account and divide it up, so that the deposit will be divided $5,000 to the husband, $5,000 to the wife, and $5,000 in a joint account, with the possibility of another $5,000 in a trust account.

Mr. BIRDZELL. No; as long as the account is in the name of the husband and wife, no matter what the amount is, it is treated as one deposit, but it will be treated separately from any other account of the husband.

Mr. WOLCOTT. My point is this: John Jones has $5,000 in the bank, and John Jones and Mary Jones, his wife, have another $5,000 in a joint account. Are both of those accounts insured up to $5,000?

Mr. BIRDZELL. The first being an individual account, and the other being a joint account; yes.

Mr. WOLCOTT. The same thing follows if Mary Jones has another $5,000 in her name?

Mr. BIRDZELL. Exactly.

Mr. WOLCOTT. So he can take this $20,000 that they had in the original account, and split it up, $5,000 in his own name, $5,000 in her name, $5,000 in their joint names, and then $5,000 in the bona fide trust account?

The CHAIRMAN. They could not do that after the bank had failed.

Mr. WOLCOTT. I am saying that in that manner it would be possible for him to insure the total of his $20,000.

Mr. BIRDZELL. If it is done merely as a cover, so as to enable a man to get more insurance on his own money, we would pay him $5,000.

Mr. GOLDSBOROUGH. In that case the burden of proof would be on the Deposit Insurance Corporation.

Mr. BIRDZELL. Yes.

Mr. WOLCOTT. I know all the intricacies of the chancery practice, and I know you could split it up in different banks, but my point is on the face of it are those accounts insured, or upon the failure of that bank or the closing of that bank must the individual go into chancery and by suit against the Insurance Corporation, or something of that nature, prove that they were bona fide separate accounts?

Mr. BIRDZELL. If the information we get, upon going in to pay off the bank, indicates that there has been an attempt to increase our insurance liability to one owner of a deposit, using simply a joint account, or some other device to cover up his ownership, we would investigate that before we would pay the claim, and if we found enough evidence to satisfy us that there was a subterfuge for the purpose of increasing the insurance of one depositor, we would decline to pay it.

The CHAIRMAN. The law specifically makes the test the individual ownership.

Mr. BIRDZELL. Individual ownership.

The CHAIRMAN. Without objection, we will take a recess until 10:30 o'clock tomorrow morning, and Mr. Crowley, we would like to have you and Judge Birdzell back tomorrow morning at 10:30 o'clock.

(Whereupon, at 12:30 p. m., the committee adjourned until Friday, Feb. 22, 1935, at 10:30 a. m.)

BANKING ACT OF 1935

FRIDAY, FEBRUARY 22, 1935

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

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

STATEMENTS OF LEO T. CROWLEY, CHAIRMAN FEDERAL DEPOSIT INSURANCE CORPORATION; AND L. E. BIRDZELL, GENERAL COUNSEL FEDERAL DEPOSIT INSURANCE CORPORATION—Continued

The Chairman. The committee will come to order. We will continue the hearing on H. R. 5357.

Mr. Crowley, I would like to ask you two or three questions.

Did you give the figures showing the amount of insurance in banks that have failed since the passage of the Deposit Insurance Act?

Mr. Crowley. We have that here, Mr. Chairman. Do you wish the figures for each bank, or the total?

The Chairman. I do not care about having it broken down.

Mr. Crowley. The deposits in 11 banks that have failed amounted to $2,890,000, and of that amount the estimated net amount for which depositors were insured was $1,765,000; the secured deposits, and those subject to offset, amounted to $935,000. The uninsured balance amounted to $190,000. In other words, of total deposits amounting to $2,890,000 in failed insured banks, all but $190,000 were fully protected.

The Chairman. The amount of deposits insured for which your corporation was responsible amounted to $1,765,000?

Mr. Crowley. Yes, sir.

The Chairman. How much would you say, of that amount, will represent losses, if you can estimate it, by the Deposit Insurance Corporation?

Mr. Markham. We only have estimates of anticipated recoveries on the nine insured banks which failed during 1934. These banks had total deposit liabilities of $1,938,000. The estimated net loss to the F. D. I. C. amounts to about $356,000.

The Chairman. Do you mean to say that you will disburse to depositors to make good their losses, above what you will receive, the sum of $356,000?

Mr. Markham. Yes, sir.

Mr. MARKHAM. Of the $2,890,000, the offsets and the amount of the security that the depositor has pays everything but $190,000.

The CHAIRMAN. What will you pay to depositors? Your net disbursements, or what we might term your "final losses" in the Corporation down to date, amount to how much?

Mr. CROWLEY. It is impossible for us to tell you that because all we can do is to estimate.

The CHAIRMAN. That is what I am asking for, an estimate.

Mr. CROWLEY. We have estimated, I think, that in the case of the nine banks that suspended during 1934 the net losses to the Federal Deposit Insurance Corporation will be something like 40 percent.

The CHAIRMAN. I can understand you can only give us an estimate, but that is what I want to get.

Mr. CROWLEY. I think that is about correct, that it is about 40-percent loss that we anticipate.

Mr. CROWLEY. All of the claims of depositors in the 11 banks that were closed, with the exception of about $460,000, have already been paid. All but about $50,000 or $60,000 will eventually be paid, according to our estimates.

The CHAIRMAN. They have been paid up to now?

Mr. CROWLEY. $2,430,000, including offsets settled and secured claims paid.

The CHAIRMAN. All I want to ascertain is, first, the total amount of deposits in banks insured that have closed down to date.

Mr. CROWLEY. That is $2,890,000.

The CHAIRMAN. What portion of that amount of deposits was insured?

Mr. CROWLEY. All except $190,000, when you add to our insurance offsets and secured deposits. The net insured deposits amounted to $1,765,000.

The CHAIRMAN. That is the amount of deposits to be covered by insurance?

Mr. CROWLEY. That is correct.

The CHAIRMAN. For which you were responsible. That is the total of your actual liabilities?

Mr. CROWLEY. That is right.

The CHAIRMAN. And of that your estimate is that you will actually lose 40 percent?

Mr. CROWLEY. We will recover 60 percent.

The CHAIRMAN. That is the same thing, is it not?

Mr. CROWLEY. Yes.

The CHAIRMAN. The losses will be 40 percent?

Mr. CROWLEY. Yes.

The CHAIRMAN. That will be about what amount?

Mr. MARKHAM. $356,000 in nine of the banks.

The CHAIRMAN. There were 11 of them that failed?

Mr. CROWLEY. That is right.

The CHAIRMAN. How many of those failures were normal or legitimate failures, and how many of those failures were due to defaults?

Mr. CROWLEY. I think six of them were due to defalcations.

The CHAIRMAN. Those figures are correct?

Mr. CROWLEY. That is right.

The CHAIRMAN. So we have had five bank failures other than those due to defalcations since the effective date of the Deposit Insurance Corporation Act?

Mr. CROWLEY. Let me say this: There are three banks that I think will pay 100 cents on the dollar.

The CHAIRMAN. How many failed insured banks will not pay 100 cents on the dollar and were not closed on account of defalcations?

Mr. CROWLEY. There are four. For example, we have a little bank with $40,000 deposits, which is so small that they put it in liquidation because they could not make any money.

The CHAIRMAN. Did you have any actual loss in that?

Mr. CROWLEY. Yes; I think we may have a small loss.

The CHAIRMAN. You have already accounted for three banks in which you have no substantial loss.

Mr. CROWLEY. Take the bank in Pittsburgh that closed. They had some $700,000 in Postal Savings accounts. They took collateral that might be helpful to us, which was necessary to use for Postal Savings. Those depositors were protected by collateral that was taken from the assets of the bank. It weakened us to that degree.

Every time they post collateral for public funds, or what not, they only weaken our position that much more.

The CHAIRMAN. I believe you said yesterday that your earnings had amounted to about $9,000,000 down to this time; is that correct?

Mr. CROWLEY. They are running about 9 million, between 22 and 23 thousand dollars a day.

The CHAIRMAN. Taking your losses down to date, your net balance will show a profit of something approaching 8½ million dollars?

Mr. CROWLEY. No. They will before the overhead is deducted; after the overhead is deducted, they will still show a substantial profit. This corporation could be wound up today and pay its losses and return to the Federal Reserve bank and to the Government their money plus a return on their investment.

The CHAIRMAN. And a substantial return?

Mr. CROWLEY. That is correct, sir. You understand, there were some suspensions outside of our fund; there were 47 banks that failed outside of the fund.

The CHAIRMAN. You had made that statement yesterday, as I recall, that there were 47 failures outside of the Insurance Corporation.

Mr. CROWLEY. Yes.

The CHAIRMAN. In that connection, to make those figures clear, you might state how many banks are uninsured.

Mr. CROWLEY. We have 1,100 banks that are operating in this country today that are uninsured.

The CHAIRMAN. And out of the 1,100 banks you had 47 failures outside of the Corporation, and of the total number inside the Corporation you had the number to which you had already testified?

Mr. CROWLEY. That is correct.

The CHAIRMAN. Mr. Crowley, I want to ask you what your present resources are for the protection of depositors?

Mr. Crowley. We have $140,000,000 from the Federal Reserve banks and $150,000,000 from the Treasury, which has been subscribed in the form of stock. We also have $41,000,000 from the banks themselves. So we have approximately $330,000,000, and we have that invested in Government securities, with the exception of about $15,000,000 that we carry on hand for any normal expenses that we might have.

The Chairman. You have the right and the privilege and the authority under the law to expand your capital three times?

Mr. Crowley. By borrowing.

The Chairman. By issuing obligations?

Mr. Crowley. That is correct, Mr. Chairman.

The Chairman. So you have potential resources of about $900,000,000, which would give you four times the amount of your capital?

Mr. Crowley. That is correct.

The Chairman. Which would be 1,200 million dollars?

Mr. Crowley. Yes.

The Chairman. In addition to that, under the act passed in 1934, the amendatory act of last year, you have also the right to borrow $250,000,000 from the Reconstruction Finance Corporation.

Mr. Crowley. That is correct, sir.

The Chairman. Summed up, it means that your Corporation is equipped practically to the amount of a billion and a quarter dollars at this time?

Mr. Crowley. There is a question, Mr. Chairman, whether the $250,000,000 that we have the right to borrow from the Reconstruction Finance Corporation should not be included in our borrowings of three times the amount of our capital.

The Chairman. How do you get that? The original act gave you the right to expand your capital three times.

Mr. Crowley. That is right.

The Chairman. We attempted and I thought we had supplemented that last year in the bill passed at that time giving you entirely separate authority to borrow a quarter of a million dollars from the Reconstruction Finance Corporation.

Mr. Birdzell. This is the situation, Mr. Chairman. The law under which we are operating does not provide for a Government guarantee of either the principal or the interest of our debentures which we may issue to the extent of three times our capital.

The Chairman. I know that.

Mr. Birdzell. Because of that fact we suggested that that guaranty be given. It was in the bill that was under consideration last year and was stricken out in the Senate. When the bill was ultimately passed, however, it was not passed quite in the form that you now have in mind, Mr. Chairman.

It was passed in this form, that as to the debentures that might be issued by our Corporation, our Corporation could call upon the Reconstruction Finance Corporation to purchase at par to the extent of $250,000,000. That is a sort of substitute for Government guarantee, to provide us with a par market for our debentures up to that amount.

I think if you will turn to the provision of the act where that is found you will be impressed with the fact that the $250,000,000 is part of the debenture authority of the board of directors, and not in addition to that.

The CHAIRMAN. In any event, you have about twelve hundred million dollars?

Mr. BIRDZELL. That is right.

Mr. CROWLEY. In our proposal we are asking for the right of issuing three times the amount, which will give us $1,200,000,000. We say nothing about the 250 million, but it is still available from the Reconstruction Finance Corporation.

Mr. FORD. I wanted to make one observation. The banks pay this premium.

Mr. CROWLEY. That is right.

Mr. FORD. As a matter of fact, the depositors pay it.

Mr. CROWLEY. Of course, the depositors, like the consumers of anything, ultimately pay the expense.

Mr. FORD. They have cut out the interest on the unused dollars, and since they have quit paying interest that really make the depositor pay for his own protection.

Mr. CROWLEY. That does not affect the rank and file of the depositors. The average depositor never got anything on his demand deposits.

Mr. KOPPLEMANN. Further on the banks that the chairman was talking about, what, under the present law, or under the bill proposed that is before us, are you empowered to do about rehabilitating many of these closed banks.

Mr. CROWLEY. There is the possibility that in the 1,100 licensed uninsured banks a very substantial number of those may be brought into our fund. There are some that are staying out because they do not wish to join.

Mr. KOPPLEMANN. But what I specifically would like to know is whether or not under the old law, or under the new bill as proposed, you have the power to help these banks get back on to their feet.

Mr. CROWLEY. No; we have no legal power to force them to do anything. With the help of the Reconstruction Finance Corporation we have been able to aid them.

Mr. KOPPLEMANN. Have you done so?

Mr. CROWLEY. We have already rebuilt the capital structure, with the help of the Reconstruction Finance Corporation, of about 3,500 insured State banks in this country.

Mr. KOPPLEMANN. I mean after they are in trouble.

Mr. CROWLEY. They were in trouble when we got them.

Mr. KOPPLEMANN. I am talking about 11 closed banks that were insured.

Mr. CROWLEY. We have not any authority.

Mr. KOPPLEMANN. No authority to keep them going. You see what I am trying to bring out, whether or not this act even goes further than merely guaranteeing deposits, whether it does not also save the banks.

Mr. BIRDZELL. Under the existing law we could not, if we would, purchase any assets or loan any money to a nonmember bank, and of the 11 banks that have closed there were only 2 member banks. So we could not, if we would, go into those banks and rehabilitate them ourselves, except as to member banks. In this bill provision is made for something like that to be done.

Mr. DIRKSEN. Does the $41,000,000 that has been referred to represent the income from the deposit fund?

Mr. CROWLEY. No; it represents the assessment of one-fourth of 1 percent on insured deposits against the banks. The members of our fund pay an assessment. They have paid us $41,000,000.

Mr. DIRKSEN. Under the original law, could you still issue stock to the Federal Reserve bank?

Mr. CROWLEY. Yes; you could offer stock to the Treasury, or, under the set-up that now exists, you could authorize——

Mr. DIRKSEN (interposing). The original law provided that the Federal Reserve banks could subscribe to the extent of one-half of their surplus, on the first of January 1933.

Mr. CROWLEY. They have done that.

Mr. DIRKSEN. Then you have discretionary power to require only the payment of one-half of the subscription?

Mr. CROWLEY. We have required the payment of the entire subscription.

Mr. DIRKSEN. It has been paid entirely?

Mr. CROWLEY. It has been paid entirely; yes, sir.

Mr. GIFFORD. You have used the expression recover immediately.

Mr. CROWLEY. We have started to pay off to depositors in closed insured banks, Congressman, within 10 days from the time the bank closed.

Mr. GIFFORD. You have made no new suggestions?

Mr. CROWLEY. We have made some suggestions that are purely administrative.

Let me explain that to you. There is a little bank in Montana that closed. They are way off in the country. We had to go way up in the hills and bring the people down to get their money. Under the present law we must carry on the expenses of continuing that bank, and it may be that all the depositors except three or four were paid. We are asking for the right to bring the balance of the affairs of the bank into Washington so that we might complete the tag-end of those payments from our office here.

Mr. GIFFORD. Then I notice that you want some proof from depositors that a deposit in a bank that you may find is really one deposit, is held for the benefit of one person.

In the future you may want written proof that a certain number of deposits may be held for the benefit of one person, under different names, unless it were proven to be a trust deposit.

Questions asked you yesterday related to deposits carried as trustee, or in a joint account.

I thought I noticed a recommendation in reference to the matter of determining whether there were not various deposits in a bank of only one individual.

Mr. BIRDZELL. There is nothing specific on that further than this. It provides for the claim agents of the Corporation being able to take proof to determine the ownership of the different amounts of money.

Mr. GIFFORD. My question was leading up to that.

Mr. BIRDZELL. We will not find occasion to use that provision of law in any great number of cases, because we get practically all our information from the books in the banks. These proofs of claims are made up and then the depositors are asked to come in and get their money. All that remains to do is to reconcile with the depositor's passbook.

Mr. GIFFORD. I am certain that there is a recommendation there that seemed to be an attempt to prove that certain people might divide their accounts in the same bank for the sake of being insured under the $5,000 limit.

Mr. BIRDZELL. Would that be under the definition of insured deposits?

Mr. GIFFORD. I cannot recall.

Mr. GOLDSBOROUGH. How much in the way of income is derived from one-twelfth of 1 percent?

Mr. CROWLEY. About $30,000,000.

Mr. GOLDSBOROUGH. As I understand it the law provides that the assessment may be lowered, but there is no provision in the proposed act under which the assessment can be raised.

Mr. CROWLEY. That is correct.

Mr. GOLDSBOROUGH. On what theory do you feel that it would not be wise to place in the proposed act some provision permitting the Insurance Corporation to raise that contribution from one-twelfth of 1 percent to such amount as might be necessary?

Mr. CROWLEY. This is my own personal viewpoint about that. I think that in building a fund the insurance of deposits, the first responsibility is to correct some of the mistakes or weaknesses in our banking system. In other words, I do not believe we are justified in charging to the bank system of this country the mistakes of the past. This Corporation should be given sufficient authority to eliminate a great many of the past mistakes.

There is a question in my mind as to whether we are justified in taking from a bank a large percentage of its income, or leaving it liable to an assessment which might jeopardize the soundness of that particular institution. To subject a bank to an additional assessment at a time when they are having about all the difficulties that they can encounter themselves may not be a wise policy.

Mr. GOLDSBOROUGH. That is the time when the Insurance Corporation can be of service to the depositors in banks.

Mr. CROWLEY. I think that the Government now has a direct responsibility in connection with our banking system. I think it has a responsibility to the Federal Deposit Insurance Corporation, and to the depositors. I believe that if we are going to build this fund over a period of years, that in addition to the income you get from the banks, you must have a way to build up a sufficiently large reserve. If we have a recurrence of the conditions that existed in 1907 or 1893, we will then have a cushion that we may fall back on out of which to pay losses.

I am not disturbed particularly at the losses of this Corporation in the next, 3, 4, or 5 years. Because of the rebuilding program and a recovery of business which will restore values, losses will not be great in the next 3 or 4 years.

I think over a period of 10 years this fund should build a substantial reserve.

Mr. Goldsborough. You mean the act should be amended to provide for a Government contribution?

Mr. Crowley. I do not care whether it is a Government contribution or income from some other source.

Mr. Goldsborough. I have no objection to it; I am just asking the question.

Mr. Crowley. I think where we go into the field of insuring deposits our first responsibility is to keep this Corporation solvent so that it can at all times meet its demands. Otherwise, I think confidence in banking would be broken down entirely.

Mr. Goldsborough. Personally, I have no fear about that for the next 20 years.

But there is another consideration, and a very serious one, in my mind. This Corporation, in the minds of the public, is a Federal organization, a Federal deposit-insurance corporation; and unless it has a dual responsibility, the title is just as misleading as the title of the Bank of the United States in New York. It simply deceives the public.

I personally see no objection whatever to amending this proposed act so as to give the Corporation the right to raise this contribution from the banks from one-twelfth of 1 percent to one-fourth of 1 percent.

For a long while the banks will be afraid to make loans; the examinations are going to be rather strict; but we have given the banks in the last few years $13,000,000,000, and we are continuing to issue bonds and give them more billions of dollars.

As they wax strong and arrogant, and as business is resumed, and as they begin to brush the examinations aside, as they will in time, it will become necessary to fortify this Corporation and serve notice on the banks that they have the bag to hold if they go too far, as I see it.

I believe if the public knew that this is a one-twelfth of 1 percent limitation, and that the limitation was absolute and the Corporation could go no further, I think it would interfere very seriously with the morale of the public. That is my opinion—that they are bound to give way in a short time.

Mr. Crowley. Congressman Goldsborough, I think that for the psychological effect on the depositors they must have confidence in this Corporation. Depositors must have confidence that the fund is sufficiently large and that the Corporation is well managed. If they lose that confidence, that is where the difficulty will be. The great contribution which we have made is the establishment of confidence in the minds of the depositors.

Mr. Goldsborough. One other thing: When the time comes to sell the debentures, aside from whatever the Reconstruction Finance Corporation may think, what would be the justification in the market for those debentures?

Mr. Crowley. I would say that if it got to the point where we had to issue debentures up to three times the amount of our capital there would be no open market for them at all. By the very nature of things, if we had such a situation that we would have to issue our debentures up to the limit, there is only one place where we could go to get that aid, and that is from the Treasury.

Mr. GOLDSBOROUGH. That is my opinion, and that is the reason I asked you the question.

Mr. CLARK. I want to say one thing in regard to the first point that Mr. Goldsborough made. I think it is a point well taken, that the Corporation should have the administrative power to raise the rate.

I want to state right here that I think of all the "new deal" agencies that have been set up this Corporation is the finest and has been handled in the finest manner, administratively. In the 15 months you have been in existence you have done pretty nearly a superhard job; and I for one would be willing to trust the administration of this Corporation to them, and give them administrative latitude, so that they could, if necessary, raise these premiums or assessments, and I think the public has more confidence in the work you have done than in the work that has been done by practically any other agency that has been set up in the last 2 years.

I am thoroughly convinced of that, both so far as the administration is concerned and in the way you have done it.

I think, personally, I would like to have you consider whether you think such an amendment as Mr. Goldsborough proposes would have a bad effect, because it seems to me it would have a good effect in giving you the administrative authority to raise the assessment, if the times and conditions demanded it.

Mr. FORD. The reason I asked the question as to whether or not the depositors were actually paying the insurance was with the idea of making a suggestion along the lines that Mr. Clark has made. But it seems that the banks, of course, will tell you, "Of course, it is all right to insure the deposits, but we pay the bill."

As a matter of fact, the bill is paid by the people whose money is in the bank. Quite a number of those deposits did not draw interest at any time. But there are also quite a number of them that did heretofore draw interest, and they have cut down on their normal interest. Where they used to pay 4 percent, they have cut as low as 2½ percent; so that in the long run, if the banks are paying the bill, I think the Deposit Insurance Corporation should have a broader latitude in reference to that assessment, so that they can raise it, instead of one-twelfth of 1 percent to one-sixth of 1 percent.

Mr. CROWLEY. You appreciate, of course, Mr. Congressman, that we have changed the way of determining our assessments.

Mr. FORD. Yes.

Mr. CROWLEY. We propose to assess on total deposits. A number of your larger banks are only insured up to 26 percent, while a vast majority are insured 70 percent or more.

I think that if the Deposit Insurance Corporation is going to bring about good banking, it is not going to do that through paying out losses. I think that the protection that it is going to afford will be brought about through studying and correcting a great many of our ills. I can foresee that, over a number of years, with this Corporation properly conducted you would have a minimum number of bank closings.

In other words, if we have the power to protect ourselves, there are going to be very few forced liquidations in this country; and if we are careful in the way we recharter banks—if we are careful in the way we conduct ourselves—the Federal Deposit Insurance Corporation might become the greatest vehicle in the Government for the rehabilitation of our whole banking system.

The CHAIRMAN. Mr. Crowley, under the act now proposed, the large banks will have, of course, to pay a premium of one-twelfth of 1 percent, based on all their deposits now?

Mr. CROWLEY. That is correct.

The CHAIRMAN. So that, whether the general banking structure is sound or not, these individual banks will realize that their liability is limited; and they will have no incentive to try to keep the banking structure on a legitimate basis.

On the other hand, if they realize that when they encourage speculative activities, which are always unloaded on those who know least about business, that their assessments are going to be increased, it seems to me that it would be a great restraining influence on those institutions.

Mr. CROWLEY. Well, I do not think——

The CHAIRMAN. It would influence them to conduct themselves in a very different way than they did in the period of 1925 to 1929.

Mr. CROWLEY. I do not think, Mr. Chairman, that the assessment is going to be the thing that might prevent the recurrence of that sort of thing, for this reason: Suppose that you double the assessment in some institutions, I do not believe that that would be a sufficient disciplinary measure to prevent speculation.

The CHAIRMAN. Those institutions are the ones that have prevented a provision like that going into the law. There could not have been any other reason why it has not become law. Is not that correct?

Mr. CROWLEY. I think that is——

The CHAIRMAN. They are the ones who do not want that provision in the law.

Mr. CROWLEY. Well, I think this, Mr. Chairman, that your fund must be kept sound. I think that the Deposit Insurance Corporation must have sufficient income to pay the losses.

The CHAIRMAN. That does not answer it.

Mr. CROWLEY. If it is necessary to give us the power to make the additional assessments, if that becomes necessary in order to keep the insurance fund sound, we should have authority to do that.

Mr. FORD. But that assessment cannot be of any particular effect in directly controlling an institution which wants to engage in unsound practices.

The CHAIRMAN. I did not mean that, but they can have the banks which are responsible, for speculations——

Mr. FORD. Any form of insurance tends to remove much of the incentive to observe sound practices.

The CHAIRMAN. Those banks, which are responsible for speculation, and which pass on their securities to the smaller banks, are the banks who under this proposed law have the greatest amount of insurance assessment to pay; and my theory is that if those banks know that assessment is not going to be increased, and there is not the tendency on their part to keep it straight. That is what I had in mind.

Mr. JONES. But the general proposition is that wherever you give insurance carelessness and speculation will actually increase, unless have strict supervision. We have that exemplified in the automobile business. For instance, the man whose automobile is insured becomes careless, even if the rates are punitive, so that in my State certain localities have to pay more than other localities. We do not even have a flat rate.

The CHAIRMAN. Is not that the general principle? Upon your theory we ought to abolish the Deposit Insurance Corporation entirely.

Mr. FORD. The rates have gone up comparatively; and in some localities I think it is very difficult to—let me discuss this off the record.

Mr. HOLLISTER. Might I ask a question? Following out this principle, the desire to certain banks to get this insurance and the objection of certain other banks, is it not true that—or, let me ask you, rather, what kind of banks, as a general rule, object to the principle, or the possibiliy, of unlimited assessment?

Mr. CROWLEY. Well, I believe that all the banks, large and small, object to the unlimited liability. I do not believe that you should have an unlimited liability. I do not thing that Congressman Goldsborough, when he refers to unlimited liability, has in mind an entirely unlimited liability but the right to call for a second assessment in the event it becomes necessary.

Mr. HOLLISTER. Or a third or a fourth?

Mr. CROWLEY. Then you would be getting into an unlimited liability. Congressman Goldsborough only wants to give the Corporation the right to call for an additional assessment in any one year.

Here are the types of bank from which you would get your objections. There is the fellow who does not want any supervision at all.

Then, there are the fellows who feel that they do not want to contribute anything to general banking recovery or the reestablishment of confidence. In other words, they are willing that the other fellows should reestablish this confidence and feel that they will benefit by it as they have in the past. There are a great many business men who will not join trade associations. They want the other man to rebuild by his efforts and want to reap the benefits they have not helped to bring about.

Other banks are afraid of the cost of this thing. They are not in sympathy with the plan.

Now, my answer is this: The man who does not want it on account of the supervision is the man whose depositors need the protection. The man who is unwilling to come in and assist in rebuilding the banking system should be compelled to do it.

And the larger banker, who believes that he can live by himself, if he will only analyze what happened to him in 1933, will realize this: When we have trouble in the Northwest, that disturbance will gradually work east, and, at some time or other, may result in the breakdown of the banking system.

So, I say, if we could pass a law that would compel every bank in this country receiving deposits to become a member of the Federal Deposit Insurance Corporation, that would be the greatest contribution that you could make; and, when that was done, the Corporation should be given powers that would enable them to protect themselves.

Mr. HOLLISTER. I agree with you 100 percent.

Mr. CROWLEY. If we can build up this thing and get the depositors to take the position that they will only do business with a bank that has deposit insurance, then we will have gone a long way toward correcting the evils in our banking system.

Mr. GIFFORD. In line with what Mr. Hollister has said, there are, in my section of the country especially, a very great number of mutual savings banks, who are doing a very safe banking-deposit business, and who look with a great deal of concern on this proposition that they have got to insure the deposits in other sections of the country, where the banking is weaker. They do not look with very much feeling of happiness on the prospect that they will have to pay the losses on weak and improperly managed banks in other sections.

Mr. CROWLEY. What State do you come from, Mr. Congressman?

Mr. GIFFORD. It is my good fortune to come from the wonderful State of Massachusetts.

Mr. CROWLEY. Well, you have had a pretty good banking system in your State, but we have 47 other States; and I think it has been proven in the past that no State can live by itself. We are trying to take a national viewpoint.

Mr. GIFFORD. I am not opposing your viewpoint, but I am trying to reflect to you the feeling of those bankers in the United States who feel that they have a pretty good—let me discuss this a moment off the record.

Are the Massachusetts mutual savings banks under this?

Mr. CROWLEY. No; they are not.

Mr. GIFFORD. Why are they not under it?

Mr. CROWLEY. They have a fund of their own.

Mr. GIFFORD. Do you say that is improper?

Mr. CROWLEY. I do not believe that any State fund that we have analyzed up to date is successful or sound. I think that under any crisis it would not be a success.

Mr. GIFFORD. Will you explain to the committee, to save me from having to explain it further, why it is that the mutual savings banks of Massachusetts prefer to insure themselves rather than to come under this Federal deposit-insurance plan? Tell the committee what you found to be their condition.

Mr. CROWLEY. Well, in the first place, you have 2 State deposit-insurance funds in the East. You have 1 in New York and you have 1 in Massachusetts. Now, neither one of those funds, in our estimation, are insurance funds at all, because of the fact that, by their very nature, they are insuring in a limited area. If banks in those systems had any loss of any great size, they would have to assess one another. They have no capital structure to speak of and they would have no way of paying out losses if they were to have any large demand upon them.

Secondly, mutual savings banks have restricted withdrawals as demands became heavy.

That is what has happened in your mutual savings bank systems, and that is why your mutual savings bank losses are less than the losses in the commercial field, because they restrict their withdrawals. That is the reason why in Massachusetts they have a fund that they call the insurance fund, but which, in realty, is not a fund that will stand analysis as to its soundness.

Mr. GIFFORD. Now, will you answer my question? What reason have they given you for their refusal to join the Federal Deposit Insurance Corporation?

Mr. CROWLEY. The only reason we have from Massachusetts is that they have a fund of their own.

Mr. GIFFORD. And you challenge that fund as not being a sound fund?

Mr. CROWLEY. Correct.

We have made analyses of the funds set up in the past. The outcome of a great many of them has been disastrous, because you cannot have adequate insurance where the banks are going to insure each other in such a limited area. It is just unsound.

The CHAIRMAN. Is not this the fact about it: Any insurance system for success depends upon a spread of the risk?

Mr. CROWLEY. That is correct, Mr. Chairman, you must also have an adequate capital structure.

The CHAIRMAN. Well, not necessarily a capital, because we have mutual insurance systems, do we not? Mutual insurance is really the cheapest system of all, is it not, for the simple reason that it does not require any capital structure? They simply pay what losses they have when they occur, and there is no waste. Is not that the mutual plan?

Mr. CROWLEY. That is correct; but I much prefer having a reserve that you can fall back on. You should not have to fall back upon special assessments for ordinary losses.

The CHAIRMAN. I am not speaking about that, but I am just speaking about the principle of insurance; and the mutual insurance is the cheapest insurance there is, if you acknowledge the liability and propose to make good.

In connection with what Mr. Gifford has said, our history shows, does it not, that the attempts to set up insurance systems for deposits in the several States have failed?

Mr. CROWLEY. Yes.

The CHAIRMAN. Because of the fact that the units were too small?

Mr. CROWLEY. That is right.

The CHAIRMAN. You do not have now an epidemic of yellow fever all over the United States, like we used to have in certain centers. The same principle is illustrated by the San Francisco fire. Now, in such cases the losses are absorbed by diversifying?

Mr. CROWLEY. That is correct.

The CHAIRMAN. And what you are doing with the banking system under the Federal Insurance Deposit Corporation is for the purpose of protecting the depositors by spreading the risk throughout the country?

Mr. CROWLEY. That is right.

The CHAIRMAN. This happened, did it not, Mr. Crowley, during the period of distress: The mutual savings banks and the big banks and everybody else ran to the Federal Government, with their hands up for assistance?

Mr. CROWLEY. Except Massachusetts. The mutual savings banks in Massachusetts did not.

Mr. GIFFORD. I want to challenge the chairman's argument. Massachuetts and New England claim that within themselves they have that greatly diversified situation, where they can invest in those diversified things, while in those great agricultural areas they are limited in the investments they can make to a certain kind of investment only. So it does not mean solely geographical diversification.

Mr. CROWLEY. Mr. Congressman, let me say this to you: I am awfully sorry this discussion has gotten down to districts or regions, because it is rather embarrassing, but your Massachusetts and New England mutual savings banks made the same mistakes, the same proportion of mistakes, perhaps, as the banks in other parts of the country.

Some of your New England banks went out into the Northwest and Southwest for investment in mortgages. They were looking for larger yields. They were looking for 8 or 10 percent returns on farm mortgages; and, naturally, now they have a large percentage of assets that——

The CHAIRMAN. They went into the Southeast and Southwest, too, as well as the Northwest.

Mr. CROWLEY. A very large percentage of their bonds are not productive of income.

Mr. GIFFORD. I challenge that statement also.

The only trouble with our mutual savings banks in Massachusetts was that they had over 7 percent, which was their legal limit; and I will say to you, as to our mutual savings banks which were closed up, that there was an edict went forth from Washington——

Mr. CROWLEY. Do you mean to say that the mutual savings banks could have continued right on paying without any restrictions?

Mr. GIFFORD. Oh, no; they would have to go on for 3 months. In fact, there was an order received by them to withhold deposits.

Mr. CROWLEY. I cannot go into the details of that; but let me say this——

The CHAIRMAN. Let me interrupt you. It should be said right here—and I do not say this in criticism or unkindness—the fact remains that big banks, railroads, and even life-insurance companies, finally came to the Federal Government for a place of refuge and for assistance; and the Government had to open up the Treasury of the United States in order to enable them to carry on. That is the record, is it not?

Mr. CROWLEY. I do not pretend to know much about insurance. But I do know that, with very few exceptions, the banks, the mutual savings banks, and all of them, were very happy to have the pressure taken off on March 6, 1933; and that, perhaps, while they will not directly say this, yet a lot of them have benefited more by having had Federal deposit insurance than, perhaps, they will admit.

Furthermore, Mr. Congressman, in reference to the banks taking aid from the Reconstruction Finance Corporation, it is true that in the very beginning a few banks did take capital aid from the Reconstruction Finance Corporation to be helpful; but the vast majority needed every dollar they could get from that source. If it had not been for the R. F. C. and the F. D. I. C., your banking system never could have recovered. There was nowhere else that the banks could go to get the capital aid which was necessary.

And I may add a little off the record.

Mr. FORD. Would not this little couplet apply:

When the devil was sick, the devil a monk would be;
When the devil got well, the devil a monk was he.

Mr. CROWLEY. Yes.

Mr. GIFFORD. That little pleasantry does not cure the situation. Now, I ask sincerely, if the mutual savings bank does not join the Federal Deposit Insurance Corporation, there is a reason for not doing so and there must be a fear of the thing? New England has a feeling that no matter what the Federal Government does, we will pay very greatly in excess of what we ever get; and I think it is right to bring out here that, if they have that fear, there is a real foundation for it.

Mr. CROWLEY. Of course, Mr. Congressman, there are always bound to be differences of opinion as to questions of that sort.

The CHAIRMAN. Mr. Crowley, I want to ask you another question. You gave us yesterday an estimate of the burdens that would have been necessary to meet to take care of the losses to depositors in commercial banks during the 70-year period since the passage of the National Banking Act; and you gave us the comparative losses as between national banks and State banks.

The fact is that until recently there have not been many serious efforts at strict regulation and supervision as to State banks?

Mr. CROWLEY. That is correct, sir.

The CHAIRMAN. It is a fact, however, that in most of the States now we have developed systems of regulation and supervision that represent marked improvement and progress.

Mr. CROWLEY. Well, I think that there has been considerable improvement in the supervision of the State banking systems; but in many respects there is still a long way to go.

The CHAIRMAN. That is what I am asking you. It is a very different story from what it was during the first 50 or 60 years of our banking experience; so that same condition would not be reflected in the future?

Mr. CROWLEY. I think that is correct, Mr. Chairman.

The CHAIRMAN. It could not be. Now, I want to ask you another question. You estimated in that statement, as I remember it, that one-third of 1 percent would have taken care of all the losses, for banks of all types, during that 70-year period; and that one-eighth of 1 percent of the deposits would have covered all losses, exclusive of periods of panic.

Mr. CROWLEY. That is right.

The CHAIRMAN. Those figures, of course, are based upon operations which were, in the first place, without effective supervision—certainly as to the State banks?

The CHAIRMAN. And without modernized regulation as to the national banks?

Mr. CROWLEY. That is correct, Mr. Chairman.

The CHAIRMAN. And they also represent the experience of a period during which there was no insurance of deposits.

Mr. CROWLEY. That is correct.

The CHAIRMAN. So that, for the future, great allowances should be made for the improvements we have made in regulation and supervision and, also, for the operation and effect of successive deposit-insurance funds, should there not?

Mr. CROWLEY. That is correct, Mr. Chairman.

The CHAIRMAN. Now, what is the percentage of losses since the effective date of deposit insurance, as to banks that have been insured?

Mr. CROWLEY. To answer your question will take quite a little figuring. We had some thirty-six billions in deposits and we have had $2,847,000 of deposits in closed insured banks. It will take quite a little figuring to get the exact percentage of loss in insured banks.

The CHAIRMAN. The losses will be $356,000, will they not?

Mr. CROWLEY. Yes.

Mr. REILLY. Well, certainly no one anticipated those losses, with the exception of the activities of the Corporation, so that, as far as I am concerned, the amount of the losses which have accrued up to this time do not afford at all a basis for the actuarial experience required in order to estimate what the assessments should be.

The CHAIRMAN. I agree fully with that.

Mr. REILLY. Let Mr. Crowley take just a minute on that question.

The CHAIRMAN. I want to ask you another question.

Mr. REILLY. I want him to answer my question.

Mr. CROWLEY. Mr. Congressman, perhaps I had better make sure what you have in mind. You asked me what question?

Mr. REILLY. I asked whether the amount of the losses that have accrued up to this time, since the inauguration of the Federal insurance system, afford any adequate basis for establishing the actuarial experience required to estimate what assessments will be required.

Mr. CROWLEY. I get it now.

It is quite true that we should not have had, and we have not had, normal losses yet. But the success of this Corporation depended upon the rebuilding of your banking system. If that had not been done, you would have had no Federal Insurance Deposit Corporation, because the demand would have been so great that the Corporation would have become insolvent and you could not have reestablished confidence.

Now, I do not believe that for some time the banking system of this country has been in better shape than it is today, and that means that we are starting out on quite a clear basis, Mr. Congressman. I think that the income should be determined by our experience of the past, so that we may build reasonable reserves for the future.

Mr. GOLDSBOROUGH. I am in accord with your statement, but, in view of the fact that in these other estimates of percentages, which we are undertaking to bring down to date, we have our experience recorded in figures, I think that the picture should be completed by giving the percentage of losses by totaling the deposits since the Federal Insurance Deposit Corporation Act became effective. If you have not those figures now, you may insert them in the record. I realize that they may require considerable calculation; but let us complete the picture.

Mr. CROWLEY. Mr. Congressman, will you take my statement and turn the pages to the chart entitled "All Commercial Banks, 1865–1934."

Mr. GOLDSBOROUGH. Let me make a suggestion. We have been over all of that. All I want is that you take a pencil and figure out this percentage of losses for the record, so that the figure will be available to us. You can do that. All I want is to have those figures in the record to complete the picture.

Mr. CROWLEY. We will put that in the record for you.

(See p. 27 of hearings of Feb. 28.)

Mr. WILLIAMS. Is it not a fact that prior to the bank-failure epidemic, prior to this panic, that bank losses were very nominal throughout the history of this country?

Mr. CROWLEY. You mean after the washing-out of the weaker institutions?

Mr. WILLIAMS. No; I mean beginning before this panic, that the bank failures for a period of 25 or 30 years had been practically nominal?

Mr. CROWLEY. They have always been reduced after such periods. It is just like anything else; you wash out your weaker people; you have losses and have destitute people in the community. That same thing is true in the effect of the recent readjustments.

Mr. WILLIAMS. Do you have any figures of the losses to bank depositors in national banks from the beginning?

Mr. CROWLEY. Will you please answer that, Mr. Thompson?

Mr. WILLIAMS. I refer to the national-bank situation.

Mr. THOMPSON. We estimate that the losses to depositors will amount to about $1,000,000,000. We can only give you a figure that is partly estimated, inasmuch as the liquidation of the banks that are still in the hands of receivers has not been completed. We have had to take the value of the remaining assets and estimate what the total recoveries will be.

Mr. WILLIAMS. What proportion was the wash-out you spoke of, of the banks that did not reopen? What percentage of the banks closed have been allowed to reopen?

Mr. CROWLEY. Do you mean what percentage did not reopen, Mr. Congressman?

Mr. WILLIAMS. You know, we have overdrawn this matter of bank failures, stating that the banks immediately after that time should make such a remarkably good showing and then, in the next breath, saying that they were in an awful condition.

Mr. CROWLEY. The thing that has happened to your banking system has been the rebuilding of confidence and, also of capital structures. For instance, the Reconstruction Finance Corporation has invested $1,000,000,000 in the capital structures of banks and, in addition to that, there has been, I presume, four or five hundred million dollars in local contributions to capital structure.

Mr. WILLIAMS. Oh, I know there has been a lot of this overdrawn—this scare that the banks were in such terrible condition.

Mr. CROWLEY. What was the capital structure of all the banks in the country? About $6,000,000,000 on June 30, 1934. I think you will find that, with everything that has been contributed, there has been, perhaps, a billion and a half dollars, or over, put into the capital of our banking system since 1933. This has been used chiefly to write off losses rather than to increase the book capital of the banks.

Mr. WILLIAMS. But weren't there a lot of these banks that, if they had been let alone, could have worked themselves out?

Mr. CROWLEY. There are always banks which, if let alone, might be able to work themselves out.

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Mr. GIFFORD. Now, we in New England, let alone, we are working ourselves out.

Mr. CROWLEY. The assets are improving, Mr. Congressman, all the time.

Mr. WILLIAMS. Right in that connection, while they are talking, Mr. Chairman, how many of these banks altogether opened up without any assistance? Most of them were able to open after what we called the bank holiday. How many of them opened, what proportion of them at least, opened without help from some source?

Mr. CROWLEY. There were 15,000 banks, Mr. Williams, and between five and six thousand have been given aid by the Federal Government; and that does not include some banks that have made their own contributions to the reestablishment of capital structure.

Mr. WILLIAMS. I was wondering if you had the figures of those banks whose capital structure was built up by local capital, independently of the Government.

Mr. CROWLEY. I do not think we have that figure; but we are assembling it and will have it soon.

Mr. WILLIAMS. The question that I was interested in was from the other end of it. You might say what was the number that were able to reopen without any help.

Mr. CROWLEY. I would say possibly 50 percent, Mr. Congressman.

Mr. BIRDZELL. May I make this contribution, further, to complete that thought? Many of the reorganized banks have been capitalized quite largely by their depositors, through waivers of deposit liability or the conversion of deposit liability into preferred stock, or something of that kind, so that some of the banks that were reopened in reorganized fashion really had depositors' losses included in their capital.

Mr. WILLIAMS. Yes; but that is the same thing as building up their capital structure through local contributions.

Mr. GIFFORD. The banks in my section all reopened, but, after the reopening they were forced to create a larger capital structure simply to mark off temporary losses that represented merely temporarily decreased values, and many of these 5,000 banks that they talk about having had Government aid got money from the Reconstruction Finance Corporation that they did not need at all, just to allay the fears of the people.

Mr. CROWLEY. You mean by that, Mr. Congressman—what do you mean when you refer to "temporary losses"?

Mr. GIFFORD. Well, our banks claim that the bank examiners were so severe that they demanded mark-downs or charge-offs of so much that they have to have a larger capital to offset that.

Mr. CROWLEY. Do you mean that they made them take out bond depreciation and things of that nature?

Mr. GIFFORD. I know of particular real-estate matters where the examiners required mark-downs for temporary losses.

Mr. WILLIAMS. Let me ask this question in that connection: In the temporary fund that is now established for nonmember banks, what percentage of those banks that are in the fund were permitted to come in without building up and strengthening their capital structure?

Mr. CROWLEY. The national banks and State member banks, you understand, came in automatically.

Mr. WILLIAMS. That was not the question. I asked about the nonmember banks. Were they permitted to come in without building up or strengthening their capital structure?

Mr. CROWLEY. We have some 8,000 nonmember State banks, and we have rebuilt or have in process of rebuilding close to 4,000 of these banks.

Mr. WILLIAMS. In other words, only half of them were able to come in without rebuilding their capital structures?

Mr. CROWLEY. That is right.

Mr. CLARK. Following out that line of inquiry: you said that 50 percent did not need help to reopen because of the confidence the public had in them. Isn't that correct, that a large part of them had to have help because confidence had to be reestablished, rather than the financial structure? If everyone had reopened automatically and the public had been in the frame of mind it was just before the holiday, there is no way of knowing what percentage of the 50 percent could have withstood the shock?

Mr. CROWLEY. The first thing you had to do was to reestablish confidence.

Mr. CLARK. And then, after you did that, 50 percent could reopen; and in 1933 we had approximately 6 billions of capital in our banking structure?

Mr. CROWLEY. That is correct.

Mr. CLARK. And there were approximately 31 billion dollars that we set up in the form of liquid assets. That made a total collectible, assuming the capital was sound, of 37 billion dollars and there were 57 billion dollars of deposit liabilities. That left 20 billion dollars actually frozen.

Now, had those banks at that time had the rediscount privilege, of taking a large part of their frozen assets to some place where they could have gotten money on them, as a matter of fact, we would not have had much more than 5 billion dollars of frozen stuff in the banking system.

Just roughly and approximately, how close is that to correct?

Mr. CROWLEY. Of course you would have been able to have postponed this thing by loaning the banks money.

When the Reconstruction Finance Corporation was originally set up it was with the idea of lending money to the banks in order to meet that withdrawal. But the way it worked out, on account of the whole economic crash, it in reality only preferred one depositor over the other. When the banks finally did have to close the assets of many of them were pledged for bills payable, and the depositor who was an unsuspecting individual was left with the frozen assets.

There is only one thing that rediscount is good for; that is, to take the place of liquidity; but it can never take the place of soundness.

Mr. CLARK. I understand that; but the terrible crash might have been held off.

Mr. CROWLEY. You might have carried it along for a while; but throughout the whole economic system the values were shrunk so much that the assets in fact were not there. You might have had all the rediscount privilege that you wanted; but, if you did not have the values there, it would not have prevented the crash. At best you would merely have deferred it.

Mr. WILLIAMS. If they had had a chance to rediscount this paper on real estate and other securities that ordinarily are good securities, would not that have kept the values from shrinking, the fact that they had that privilege?

Mr. CROWLEY. You mean the forced liquidation that forced values down?

Mr. WILLIAMS. Yes.

Mr. CROWLEY. That always has a tendency to force values down.

The CHAIRMAN. Gentlemen, we cannot finish today, and we want to put other witnesses on the stand to go over the technical features of the bill; and I have an idea that we might meet again about Tuesday morning and resume this discussion, and unless there is something to interfere with that we will adjourn.

Mr. BROWN. I would like to just get a little more information on section 8.

In your statement, Mr. Crowley, you said that a rate of approximately one-third of 1 percent would cover all losses that have occurred during the past 70 years to depositors. What I am interested in is this: How do you arrive at one-twelfth of 1 percent as being an adequate figure? I assume, of course, that you take into consideration the fact that you are speaking of all losses on page 19 of your statement; whereas, in the bill, in your recommendation, you are speaking of losses on deposits of $5,000 or under. But is a rate of one-twelfth of 1 percent adequate in view of the experience of the past 70 years?

Mr. CROWLEY. I do not think that the banking experience of the past 70 years is necessarily a fair criterion, for the reason that I do not believe this Government should assume the responsibility of the supervision of the banks if our system should be the same as it was throughout the last 70 years.

In other words, I do not believe that our banking system is correct if we are going to have the same proportionate amount of losses as in the past.

Now, we will not have those losses if we do not let our banking system build back to that 30,000 banks again. One of the biggest defects in our banking system has been that we have had too many banks, and we have had a great many banks that could not employ the proper kind of management.

We arrived at the one-twelfth of 1 percent in this way: we do not believe that one-twelfth of 1 percent will build large enough reserves for the Deposit Insurance Corporation for the future, but the earning capacity of the banks right now is very low. We are interested, first, in the banks having sufficient income themselves so that they may take their losses currently and so that they may build reserves for the future. That is the greatest protection to the Deposit Insurance Corporation.

I would rather give up 50 percent of our income and have the proper supervisory powers than to have $5,000,000 or $10,000,000 more income and not have the proper supervisory powers. I think the success of this thing comes back to, first, the proper safeguards for this corporation to protect itself. The banks must pay a fair share of this income. A contribution from other sources to help to build our reserves might be considered.

Mr. Brown. Assuming that we are unable to improve the banking system, then what, based upon the experience of the last 70 years, should the rate be in order to be adequate? In other words, what percentage would it have to be to cover losses up to $5,000 deposits, on the basis of the experience of the past 70 years?

Mr. Crowley. Take out, if you will, those last 4 years.

Mr. Brown. Yes; take those out.

That is, for all banks.

Mr. Crowley. One-eight of 1 percent will take care of all deposits except those in banks which closed during the years of banking crises.

Mr. Brown. No. That is for all deposits. That is not for the deposits of $5,000 and under.

Mr. Crowley. It is one-tenth of 1 percent for the deposits of $5,000 and under.

Mr. Brown. That is one-tenth of 1 percent instead of one-twelfth of 1 percent?

Mr. Crowley. That is right.

Mr. Brown. It strikes me that your figures are very reasonable.

Mr. Clark. I do not want to go back to your original point, but I wish that Mr. Crowley would be so kind as to confer with his associates and, when he comes back Tuesday, tell us if he would have any objection to such an amendment as Mr. Goldsborough proposed and which was mentioned for discussion, whereby, in addition to the fixed liability at one-twelfth of 1 percent, the Deposit Insurance Corporation might, at any time when, in its discretion, the Corporation decided that it was necessary, levy an additional assessment of one-twelfth of 1 percent in any one year.

Frankly, I want to go along with the Corporation just as far as I can, because of the views that I have expressed, and I would like to know, at your next appearance here, whether your Corporation would or would not be interested in the amendment proposed by Mr. Goldsborough.

(Thereupon, at 12:30 p. m., the committee adjourned until Tuesday, Feb. 26, 1935.)

for the corporation to protect itself. The banks must pay a fair share of this income. A contribution from other sources to help to build our reserves might be considered.

Mr. Brown. Assuming that we are all able to improve the banking system, then what, based upon the experience of the last 70 years, should the rate be in order to be adequate? In other words, what percentage would it have to be to cover losses up to $5,000 deposits on the basis of the experience of the past 70 years?

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Mr. Brown. No. That is for all deposits. That is not for the deposits of $5,000 and under?

Mr. Crowley. It is one-tenth of 1 percent for the deposits of $5,000 and under.

Mr. Brown. That is one-tenth of 1 percent instead of one-twelfth of 1 percent?

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(Thereupon, at 12:30 p. m., the committee adjourned until Tuesday, Mar. 12, 1935.)

BANKING ACT OF 1935

TUESDAY, FEBRUARY 26, 1935

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

The committee met at 10:30 a. m., Hon. T. Alan Goldsborough presiding.

Mr. Goldsborough. The committee will come to order. Judge Birdzell, Mr. Steagall is out of the city this morning, which is the reason why I am occupying the position that he usually occupies.

Judge Birdzell, you will proceed in your own way, please; and it seems to me that it would be better for you to complete your statement, and if it is agreeable to the members of the committee, we will have it that way.

Mr. Williams. I think that that would be the most satisfactory way of handling it, the more orderly way.

Mr. Goldsborough. All right, Judge.

STATEMENT OF L. E. BIRDZELL, GENERAL COUNSEL, FEDERAL DEPOSIT INSURANCE CORPORATION

Mr. Birdzell. Mr. Chairman and gentlemen of the committee, we have reached a stage in the insurance of bank deposits where we contemplate going onto a permanent basis, and we are at some advantage now in planning for permanent deposit insurance because we have had more than a year's experience with deposit insurance under the provisions of existing law, which provided for temporary insurance.

We thought that we would be remiss in our duty if we did not bring to your committee all of the information that has become available to us by reason of our experience with the temporary plan; and we thought, too, that we would be remiss in our duty if we did not bring to you gentlemen suggestions for legislation which in our opinion will improve the plan for permanent deposit insurance as outlined in the Banking Act of 1933.

In all of our consideration of the matter, we have been brought repeatedly to the conclusion that Congress planned wisely in planning for permanent insurance, and when you consider the conditions in which the permanent insurance provisions of the Banking Act of 1933 had to be framed, frankly we marvel at the completeness of the plan that was written into that law.

I have circulated to the members of the committee a parallel print containing in one column the proposed act as contained in title I of the proposed banking act of 1935, and in another column the provisions of the existing law.

If you have read that print carefully and made comparison, I think you will be impressed with the fact that we have followed very closely the plan of the existing law in outlining a plan for permanent insurance in the proposed law. There are places where it would seem that we had taken out of the existing law subsections and completely rewritten them, but if you will follow the text in the instances where that appears to have taken place, you will find that, after all, we have followed very closely the ideas as they were expressed in the existing law.

I want to tell you very briefly why we considered that it was necessary to make the number of changes that are proposed to be made in this proposed act. In the first place, when we consider this legislation we must consider it from a historical standpoint. The deposit-insurance features of the Banking Act of 1933 were features that were written into a bill that was under consideration prior to that time, known as the "deposit liquidation act." It provided for a deposit liquidation-corporation, which was to be capitalized by a Federal Government subscription, and also by subscriptions to the stock of that corporation by the banks which were members of the Federal Reserve System. That corporation was to be authorized to loan money upon the assets of closed banks, and to purchase the assets of closed banks, the primary purpose being to provide for the liquidation, and speedy liquidation, of those banks in the interests of the depositors.

Upon that structure was really superimposed the provisions for permanent deposit insurance. That act had contemplated application only to Federal Reserve member banks, and consequently when the insurance features were added, it was at first contemplated that only Federal Reserve member banks would be insured. Later the provision was made for extending the insurance to nonmember banks voluntarily; that is, they could come in by voluntary application.

It was contemplated that a deposit liquidation corporation could be conservatively operated, and consequently it would be in a position to make money—that is, it would make a fair return upon the capital employed in that particular business. Consequently provision was made that it should pay to the Federal Reserve member banks a dividend on the capital thus employed.

I think, gentlemen, that you will probably agree that if you were considering a corporation to insure deposits in banks generally, and limited to that, at the expense of the banks, or at cost to the banks, that you would not have had in mind any provision for dividends on the stock that would be purchased by the banks in that same corporation, because they would get the benefits of it automatically as the costs were kept down.

So the dividend provisions of that act are not strictly applicable to a corporation that limits its functions to the insurance of bank deposits.

Since that act was intended to apply to banks which are members of the Federal Reserve System, and since permanent insurance was provided according to a certain schedule whereby all deposits would be insured in some amount—you are familiar with the schedule: $10,000 insured 100 percent, up to $50,000 insured 75 percent, and above $50,000 insured 50 percent—provision was made in that law for subrogation rights of the corporation in case it went in and paid off a closed bank, paying out to the depositors according to that schedule, and that law provided that if the corporation paid off the depositors in the closed banks, the corporation should succeed to all of the rights of the depositor against the closed bank.

So, you see, the corporation would enjoy the right to subrogation to the extent of all of the claims of depositors against the closed bank.

Now, during the progress of the passage of that law there was added to it, as you know, subsection (y), which provided for the insurance of bank deposits in a temporary fund which should be operative prior to the time when the permanent plan would become operative, and that insurance was limited to $2,500, and subsequently increased to $5,000.

There was no change made with respect to those provisions of law embracing the rights of the corporation to be subrogated to the rights of depositors upon paying off, but I think you will agree with me that a subrogation provision that gives to the corporation the right to be subrogated to the entire claim of the depositor against the closed bank, where all of his deposit is insured to some extent, is not appropriate and should not be applied where we are only insuring his deposit to a limited extent, as $2,500 or $5,000.

So it was necessary to change the subrogation provision of the existing law. In fact, you gentlemen may remember that in the act passed last June, provision was made for changing that subrogation feature, and it was approved by the House, but, unfortunately, it was stricken out in the conference, and never became a part of the law. I indicate that history to you, that we have deposit insurance superimposed upon a corporation originally intended to be a deposit liquidation corporation. I give you that history so that we may better have in mind the necessity for some changes if the functions of the corporation are to be limited to insurance, as we think they should be.

You gentlemen may recall that last year, when the extension of the temporary plan was under consideration, the Corporation was pointedly asked by gentlemen on this committee why it had not exercised its functions as a liquidation corporation, because both functions were expressed in subsection (a) of that bill, and you will recall that the Corporation presented to your committee, I think, satisfactory evidence that the liquidation function, so far as the banks were concerned, was being performed quite satisfactorily by the Reconstruction Finance Corporation. All of the money was being advanced on the strength of the assets that it was thought could be advanced upon a sound basis, but to make assurance doubly sure your committee recommended the amendment of the Reconstruction Finance Corporation Act, which would authorize that Corporation to proceed with liquidation loans upon a more liberal basis than it had in the past, and the recommendations of your committee became a part of the law.

So that the liquidation end, as applied to banks that had already closed, is practically taken care of now by the Reconstruction Finance Corporation, and for that reason subsection (a) has been changed by the omission from it of that language which was especially applicable to the function of loaning money to member and nonmember banks that had closed for the purpose of making those funds available to depositors.

Now, I do not know in what manner you gentlemen may desire to consider this act; that is, whether you want now to take the time to go through it section by section, but I can very briefly, I think, indicate to you the main changes that have been made, and then I will be very much pleased if I might be of any further assistance to the committee by way of answering any questions that may occur to you.

I just explained the reason for the omission in subsection (a) of the provisions relating to the loans to member banks.

Mr. Sisson. What section is it you are referring to?

Mr. Birdzell. That is on the first page, subsection (a).

The next section deals with the management of the Corporation, and is changed in one respect. Our Corporation is operated by a board of three directors. The Comptroller of the Currency is one director. The Chairman of the Corporation spends all of his time directing the affairs of the Corporation, and frequently the Comptroller may be at some remote part of the country when it is necessary to have a meeting of the board; and in order to have a quorum, it is sometimes necessary to wait until the Comptroller's return or, possibly, call in the Deputy Comptroller.

Sometime ago I furnished to the board of directors an opinion to the effect that in the absence of the Comptroller the Deputy Comptroller could function, but that opinion is based upon inference, and it ought to be provided expressly in the law that in the absence of the Comptroller a Deputy Comptroller may function in his stead as a member of our board.

The remainder of what material you find on page 4 and page 5 consists of definitions, and those definitions have been made with a view to convenience in constructing the remainder of the act, to remove any ambiguity, and so forth. I think it is not necessary to point that out, except that that is all new matter, and it is there for the purpose of facilitating the drafting of the remainder of the act.

I do want to call attention to paragraph 11 on page 5, where we have defined the term "deposit":

> The term "deposit" means the unpaid balance of money or its equivalent received by a bank in the usual course of business and for which it has given or is obligated to give unconditional credit to a commercial, checking, savings, time, or thrift account, or which is evidenced by its certificate of deposit, and trust funds as provided in paragraph (5) of subsection (h) of this section, together with such other obligations of a bank as the board of directors shall find and shall prescribe by its regulations to be deposit liabilities by general usage.

Then there is a proviso which I am skipping here, and then it is provided:

> The board of directors may by regulation further define the terms used in this paragraph.

All that there is in the existing law by way of defining deposits is simply the use of the term "deposit." We have questions arising, for instance, as to whether or not the uncollected funds of a bank that on a given reporting day may amount to many hundreds of thousands of dollars in the case of a large bank are a deposit.

You are familiar with the fact that as items are deposited in a bank for collection they are deposited under an arrangement whereby, while credit is immediately given, that credit cannot be drawn upon until the item is completely collected. Is that a deposit as of that time or is it only conditionally a deposit?

We have seen fit to clarify that in this expression here by considering only the credits which have been made unconditionally.

Uncollected funds at any particular date are not a deposit liability, although it may be more or less appropriate that reserves be calculated on such funds.

For our purposes, the uncollected items are not considered deposits, and we thought it well to have that definition in the law, but we think that Congress cannot, in an enactment of this character, so define the term "deposits" as to cover every conceivable situation.

In the existing law we are referred to the definition of "deposits" according to the Federal Reserve Board. The Federal Reserve Board defines deposits for purposes of fixing reserve requirements. Under this provision, our definition of "deposits" may be independent of the definition of the Federal Reserve Board.

Take an item like cashiers' checks, for instance. If we said that a cashier's check is a deposit, maybe we would be imposing by definition artificially and arbitrarily on given types of transactions. If a bank issues its cashier's check to pay its rent, for instance, the one to whom that check is issued may have no account in that bank at all, and the account upon which it is drawn is the account of the bank itself. There is no reason why a cashier's check given for a purpose like that should be considered a deposit liability.

When it comes to paying off the deposits of a bank, a cashier's check, however, may be purchased by a depositor and used by him the same as he would if he had purchased a draft. In that event, that type of cashier's check should be considered a deposit liability upon the closing of the bank and also for purposes of assessment. I give you that merely to show you that it is necessary to have some leeway for the board of directors to define deposits within the terms of the law, and it would be extremely difficult to put all of the definition into an act of this sort.

Mr. WOLCOTT. You say in this provision: "The board of directors may by regulation further define the terms used in this paragraph."

Do you not think it would be better to qualify that to the extent that you just mentioned?

Mr. GOLDSBOROUGH. Would it be feasible for you to defer that inquiry until he gets through with his statement?

Mr. BIRDZELL. Do you want me to answer that?

Mr. WOLCOTT. No; go ahead.

Mr. BIRDZELL. The next change that I would call your attention to is the change that you will find on page 8.

Under the existing law, it is the duty of the Comptroller of the Currency, in the case of national banks and of the Federal Reserve Board in the case of the Federal Reserve member banks, to certify those banks as being solvent in order to qualify them for membership in the permanent fund.

In view of the work that has been done by way of building up capital structures, and in view of the character of supervision of the banks in the national bank and Federal Reserve system, we have thought that that provision is now altogether unnecessary. However appropriate it might have been if this act had been put into effect a short while after the banking holiday, we think it is no longer necessary, and so all banks which are members of the Federal Reserve System now come into the fund without any further certificate on the part of the Comptroller or on the part of the Federal Reserve Board.

The State banks, nonmembers of the Federal Reserve System, that are now members of the fund, likewise come in on the strength of the examinations previously had and on the strength of their membership in the temporary fund.

Under the existing law, the nonmember banks, to qualify for membership in the permanent funds, would have been required only to have subscribed for stock. In the new set-up, since we are not providing for any dividends on stock—we are not providing for bank ownership of stock at all—they come into the permanent fund automatically.

Then, with respect to banks coming in subsequently, if a bank be not a member of the Federal Reserve System, if you will look on pages 8 and 9 you will find that provision is made for banks which are not members of the system to come in, and as to national banks which may not be members of the fund, they come in on the same basis. National banks which are not members of the temporary fund are national banks located in the Territories, for instance, in Hawaii and Alaska. These are national banks which are not members of the Deposit Insurance Corporation and not members of the Federal Reserve System.

Mr. HOLLISTER. Did you not skip new matter on page 6? You are taking this up consecutively, are you not?

Mr. BIRDZELL. Yes.

Mr. HOLLISTER. You were discussing the definitions ending up on page 5. Did you not skip all of that matter on page 6, with respect to the capital stock?

Mr. BIRDZELL. Did you have something that you wanted to inquire about on that?

Mr. GOLDSBOROUGH. May I say that Judge Birdzell exlained that he would just go over this in his own way.

Mr. BIRDZELL. I was only calling attention to some of the main features.

Perhaps I should say a word with respect to that change in the capital structure of a corporation.

Mr. HOLLISTER. I do not want to interrupt your flow of thought.

Mr. BIRDZELL. I think it is well to call that to your attention.

Mr. HOLLISTER. I thought that you might explain the whole thing as you went along.

Mr. BIRDZELL. Provision is made on page 6, at the bottom of the page, for doing away with the dividends on the stock, and a capital set-up is provided, whereby the capital stock of the corporation is treated as consisting of the shares subscribed for prior to the effective date. That includes the $150,000,000 subscription by the Federal Government, and the $139,000,000 subscription by the Federal Reserve banks. That stock is declared to be of nominal or no par value, and provision is made for the exchange or reissue thereof, and the consideration received for the capital stock may be allocated to capital and to surplus in such amounts as the board of directors shall prescribe, and such stocks shall have no vote and shall not be entitled to the payment of dividends.

The class B stock, the stock for Federal Reserve banks, was not entitled to dividends under the existing law, but the Government stock, the $150,000,000, plus the class A stock which would be subscribed for by the banks upon becoming members of our corporation, would be entitled to dividends, and those are the features that are changed.

The provision made for the allocation of the capital to capital and surplus is, we think, appropriate in view of the fact that these funds are supplied for the use of the Corporation for insurance purposes, and if a time should come when it would be necessary to utilize some of the surplus funds of the Corporation in meeting losses, we would not want the Corporation to be operating with an impaired capital, and that could be avoided through proper allocation.

Now, in making provision for the entry of new banks or newly applying banks into the Deposit Insurance Corporation, provision is made for the board of directors passing upon the qualifications of those banks for membership in the Corporation. That, we think, is a very necessary provision in the interest of having the Corporation function upon a sound basis. Through that, of course, reasonable protection ought to be given to the insurance funds of the Corporation.

A different test is laid down in this law from that laid down in the existing law. This law, as it will come into effect, we anticipate, much more than a year after the temporary plan started in operation, could appropriately provide that the banks have sound capital. The test of solvency laid down in the emergency period in the original act was a test of solvency for an emergency period where banks were permitted to insure their deposits without regard to the existence of a sound or legal capital structure.

If you will turn to page 9, in the middle of the page, paragraph 2, you will find this language:

> Before approving the application of any such State nonmember bank, the board of directors shall give consideration to the factors enumerated in subsection (g) of this section and shall determine, upon the basis of a thorough examination of such bank, that its assets in excess of its capital requirements are adequate to enable it to meet all of its liabilities as shown by the books of the bank to depositors and other creditors.

Likewise, the fore part of that deals with certificates by the Comptroller with regard to a national bank, and he must likewise certify to the Corporation with respect to a newly chartered national bank and the same factors are to be enumerated in the certificate that is to be given. These factors to be considered by the board of directors and the Comptroller are the financial history and condition of the bank, the adequacy of its capital structure, its future earnings prospects, the general character of its management, the convenience and needs of the community to be served by the bank, and whether or not its corporate powers are consistent with the purposes of this section.

That follows largely the provisions of the present national bank law with respect to the chartering of new national banks by the Comptroller of the Currency. Mr. Crowley has already explained in his statement the practical necessity for some such requirement as that.

The next section, or, rather, the paragraph on page 10, deals with the assessment. The assessment rate prescribed there is one-twelfth of 1 percent upon the total amount of liability of the insured bank for deposits, using the term deposits as used in the previous section, which I read to you a moment ago. That is based on the average at the close of business on the last days of June and December, and those dates are chosen by reason of the fact that there is always a call by the Comptroller of the Currency on those two dates. It is convenient, of course, to have the certificates to our Corporation based upon those same calls.

The assessment plan provided in the existing law should be contrasted with this. Under the existing law banks becoming members of our Corporation and insuring their deposits are required to subscribe for stock in the amount of one-half of 1 percent of their deposit liability. They must pay immediately one-half of that, which makes one-fourth of 1 percent on their entire deposit liability. Thereafter there are no stated payments to be made.

The obligation for further payments is expressed in this fashion: As the banks close, it is the duty of the Corporation to set up on its books an account wherein it will place the estimated debit balances. When any bank closes the Corporation is required to make an estimate of the ultimate amount of loss and that will be a debit balance. There is provision for the adjustment of that debit balance. Later on, if there is a greater loss than anticipated, more is charged to it; if there is less, a credit is given, and when the aggregate of those debit balances reaches one-fourth of 1 percent of the deposits in all of the banks that are insured, another assessment is levied of one-fourth of 1 percent.

So that the successive assessments under the existing law cannot be anticipated. An assessment would be made on the first of July of this year, and there might not be another one for 2 years, or there may be another one in 10 months.

Under this proposed plan an assessment is fixed at a certain figure. It is due at a certain time and the payments are to be made at a certain time.

Mr. Dirksen. Does the last portion of that subsection contemplate a different rate for mutuals than for other banks?

Mr. Birdzell. It contemplates giving to the Corporation the power to prescribe a different rate for mutuals. You gentlemen who listened so patiently during our hearings last year will remember that very frequently the question of how this proposal or that would affect mutual savings banks, and their attitude, came up. I remember that you listened very patiently one day to the president of the National Association of Mutual Savings Banks, and I think that we all became impressed at that time with the fact that mutual savings banks did create more or less of a problem in relation to any activity of this sort, and the problem is to deal with them in a way that is fitting to their particular function.

To illustrate, in the Banking Act of 1933, you made mutual savings banks eligible for membership in the Federal Reserve System, and yet I think that there are no advantages to be gained by membership in the Federal Reserve System that can be enjoyed by mutual savings banks when they become members of the System. I think that you gentlemen were generally impressed with that a year ago.

Furthermore, the type of investments of mutual savings banks, and the character of their supervision, have been such in this country that it has been asserted—I am not an economist and I am not asserting this in an authoritative way—but it is asserted by some that on account of limitations as to investments and on account of the character of supervision of mutual savings banks, and the type of business that they do, they are a favored risk. I am not saying that Congress ought to recognize that they are a favored risk from an insurance standpoint, but possibly, in view of their characteristics, it is proper to allow them to be considered in a class by themselves, separate and apart from commercial banks, and to give a limited discretion to a board that is constantly confronted with the problems presented from that particular group——

Mr. FORD. Might I make an observation there?

Mr. GOLDSBOROUGH. Mr. Ford, it was agreed when we began that we would postpone the question until he had finished.

Mr. BIRDZELL. The thought is that there are limitations with respect to the character of their investments that do not obtain with respect to commercial banks, and on account of that the mutual savings banks have argued that they have a more favorable experience than the commercial banks with respect to failures. I am not expressing any opinion as to whether or not the arguments of the mutual savings banks in that respect are sound. That is for the economists and the statisticians to consider.

There is one provision in that subsection dealing with the assessments that I want to speak of. That is on page 12 with regard to trust funds. You may have noted earlier that in defining "deposits" express reference was made to trust funds as elsewhere defined and provided for, and that reference is here on page 12.

We have found the banks quite concerned, and, of course, we have been seriously concerned, with the problem as to the protection of uninvested trust funds. Many national banks have trust departments. Many trust companies do a trust business exclusively, and some of the trust companies do both a trust business and a banking business. In the transaction of their business, there will be on hand at any given time a considerable volume of cash that will be uninvested. They say that that cash is trust funds, and not a deposit, but if a bank closes, I fear the situation would be the other way from the standpoint of the patrons of that trust company.

From the beginning we have required banks to report as deposits any amount of trust funds that were on hand and uninvested, because we felt that in the event of a closing we would be liable for those deposits.

Now, among trust companies, in doing their ordinary business, it is the practice of many of them to establish relations with commercial banks, so that they will deposit large amounts of money, uninvested trust funds, in those commercial banks. That relationship is not like the ordinary correspondent relation of one bank with another, one commercial bank with another, and, furthermore, in the event of the closing of a bank, that fund cannot properly be treated; that is, that particular kind of deposit cannot properly be treated as belonging to one depositor because it belongs to all of those who are patrons of the trust company and who under their various interests would be entitled to that cash.

So that we have provided here for the insurance on trust funds in a way that we think meets that situation. If a trust company be a member of our Corporation, and if in the transaction of its trust business it has idle funds which it places with some bank, that bank, being the bank where those funds are deposited, should report the entire amount of those deposits, and in the event of anything happening to the bank where such funds are deposited, we should look to the trust company, likewise a member of our Corporation, to establish a beneficial ownership of those various trust funds in that individual bank. Provision is made for the bank paying the assessment on those trust funds, and in event of the failure of a bank containing such funds, we will look to the various trust estates in the trust company to determine the ownership and extent of the claim that may be made on the closed bank.

I could outline that more in detail, but I think that that is enough to give you an idea.

Now, there is a discretionary power, or, rather, a power of a supervisory nature, expressed at the bottom of page 12, in paragraph 1 of subsection (i). It reads, in part:

> Wherever the board of directors shall find that an insured bank or its directors or trustees have continued unsafe or unsound practices in conducting the business of such banks or have knowingly or negligently permitted any of its officers or agents to violate repeatedly any provision of this section or of any regulation made thereunder, or of any law or regulation made pursuant to law to which the insured bank is subject, the board of directors shall first give to the Comptroller of the Currency in the case of a national bank or district bank, to the authority having supervision in case of a State bank, and also to the Federal Reserve Board in case of a State member bank, a statement of such violation by the bank for the purpose of securing a correction of such practices or conditions. Unless such correction shall be made within such period of time not exceeding 120 days as the Comptroller of the Currency, the State authority, or Federal Reserve Board, as the case may be, shall require, the board of directors, if it shall determine to proceed further, shall give to the bank not less than 30 days' written notice of intention to terminate the status of the bank as an insured bank, fixing a time and place for a hearing before the board of directors or before a person designated by it to conduct such hearing, at which evidence may be produced—

and so forth.

I read that to you to show you how the board proposes to secure corrections of dangerous practices in banks. In the first place, I call your attention to the fact that we do not deal directly with the bank. If we have a complaint as to the practices of a State bank, while we have a report of that bank, a report of the examination upon which the complaint may be based, we take that up with the State supervisory authority in an attempt to get a correction from there, but we are not altogether dependent for our protection upon the action of the State supervisory authority, for, obviously, if the correction should not be made, the Corporation ought not to be subject to the continuing hazard of the operation of that bank. So provision is made whereby the Corporation, after ample time for correction and after hearing, can terminate the relations of the bank with the Corporation.

Provision is made, of course, for the continuing protection of the depositors, even after the bank shall have terminated.

Mr. DIRKSEN. Is not 2 years a rather long time for that?

Mr. BIRDZELL. Possibly it is; it may be a little longer time than is needed, although we think we would rather err on the side of having the time too long than too short, because any law of this sort ought to be so constructed that it will deal absolutely fairly with depositors, and we can conceive of cases where depositors might not be able to obtain information with reference to the status of the bank within any short period of time.

I think that we can pass those provisions, for our present purposes at least, because this discussion is apt to become altogether too long.

There is one change that I would like to call attention to, on page 15, in the fourth paragraph, subsection (j). Provision is made there that when suits of a civil nature at common law or in equity may be brought in which the Corporation shall be a party, they shall be deemed to arise under the laws of the United States, and the district courts of the United States shall have original jurisdiction of all such suits; and the Corporation as defendant in any such suit may, at any time before the trial thereof, remove such suit from a State court into the district court of the United States. That is for the purpose of securing uniform interpretations of any provision of this act of Congress.

There is a similar provision with respect to the Federal Reserve banks.

Another feature that perhaps I should have mentioned earlier, but it is appropriate to mention it here, is that the existing law was constructed upon the principle that apparently did not contemplate examinations of banks by the Corporation, because it was to be limited in the first instance to banks which are members of the Federal Reserve System. When Congress provided for the temporary insurance, in (y), it authorized the Corporation to examine the nonmember banks in order to admit them into the temporary fund, and it authorized them to examine those banks as often as it might deem necessary for its own protection.

Now that we contemplate a permanent insurance extended to nonmember banks, it is of course appropriate that there be an express provision in the permanent act authorizing the examination of banks, so that is provided for in the eighth paragraph, which enumerates the powers of the Corporation, where before it was contained in subsection (y). There is further provision made in paragraph 2, below that, on page 16.

Then, on page 17, there is express provision for access by the Corporation to the examinations made by the Comptroller of the Currency, and also to the reports of examinations of any Federal Reserve member bank.

There is one other provision that I want to speak of, on page 18, in subsection (1). If you would read the existing subsection (1) and the new subsection (1), you would find that they are practically the same, although on account of the other changes that had to be made with reference to stock; for instance, there were frequent references to banks which are class A stockholders, and that reference runs all through subsection (1), eliminating provisions for class A stock made it necessary practically to rewrite subsection (1), but the present subsection (1) is to all intents and purposes the same as the original. The language is much the same, with the exception that the subrogation right which I explained a moment ago is expressed differently in the proposed subsection (1). Upon paying the insured deposit liability to a depositor, we are subrogated only to that portion of his rights against the bank which he would have had by virtue of the deposit which we paid to him.

An illustration would, of course, make that clear. I have a $10,000 deposit in a bank that has closed. This Corporation can only pay me $5,000 on account of that deposit. What rights shall I give to the Corporation in order that I may get my $5,000 insurance? Shall I give the Corporation my rights arising on the whole $10,000, or only with respect to the $5,000?

Under the terms of this act that we are suggesting, I give my rights only to the extent of $5,000, and I retain the right to dividends as to the remaining $5,000. Under the existing law, I would have to give all of my rights to the Corporation in order to secure my insurance.

Then one other significant change is made with reference to the means of making available or the vehicle for making available the insured deposit liability to the depositors. We use a term here that we call a transferred deposit. We authorize a transferred deposit credit to be set up either in a new national bank or in any other insured bank in the locality, giving to the board of directors a discretion to utilize an existing bank in the community rather than to do the artificial thing of setting up a new national bank in the community. If the board does set up a new national bank, it is operated just the same as the new national bank would be operated under the existing law, and the board has the same discretion with reference to whether it shall receive deposits or not, with reference to whether it shall be capitalized or not, that it has under the existing law.

Now, the subrogation right that we speak of is expressed on the top of page 20, if you are interested particularly in that.

One further feature with regard to the pay-off provisions generally. Under the existing law, there is no limitation, apparently. We may find it difficult to find a depositor determined to make a claim. In fact, we have had to advertise already for depositors to come in in some instances and make their claims. We should not be subjected to a continuing liability. We step in at the closing of the bank, and we are ready and anxious to pay out the insured deposit liability in that community so that the community will scarcely realize that there has been a bank failure, but we ought not to be subject to a continuing liability of those who do no come in within a year's time and file claims with us.

So provision is made for a year's statute of limitations, and that does not mean, of course, that the depositor loses all of his rights if he does not come in and claim his share. He loses all of his right to insurance, but he still has his claim against the bank, and if we are the receiver of that bank, we will have to treat him the same as other creditors are treated.

Now, it seems to me that I have covered all of the principal changes.

Do you think of anything more that I ought to touch on, Mr. Crowley?

Mr. CROWLEY. I think that you might explain to them a little more in detail about this liquidation in pay-off, the reason we want to bring it in here, to shut off that expense.

Mr. BIRDZELL. Yes. Mr. Crowley reminds me of one change in connection with the pay-off feature that I should have commented upon, but which I omitted to mention.

Where, under the existing law, we set up a new national bank, there is just one thing that we can do with that bank, and that is to keep it alive for 2 years. To keep it alive for 2 years may involve a lot of useless expense. After that bank has served its purpose, and paid off 90, 95, or 99 percent of the insured liabilities in that community, we ought to be given discretion to fold it up and say to the people that have not come in, "You may present your claim at the district office of the Federal Deposit Insurance Corporation", because we have offices in most of the Federal Reserve districts, or we ought to be able to say to them, "Present your proof to the head office of the Insurance Corporation." There is no need, in other words, of requiring that this bank shall be kept in operation for 2 full years, so provision is made here whereby as soon as the active period is over in that locality, if there is no further need for that institution there, we can deal with it in the manner that I have just indicated in the interest of reasonable economy.

Mr. HANCOCK. Is that what you propose in the new act?

Mr. BIRDZELL. Yes.

Mr. HANCOCK. I thought that you were asking Congress to relieve you——

Mr. GOLDSBOROUGH. Let him finish his statement, please.

Mr. HANCOCK. I should not have asked that question now, but I have such a different impression from him about that, that I thought he might be mistaken about it.

Mr. BIRDZELL. I hope that I have made it clear that we may operate a pay-off in a particular case without setting up a new bank at all.

Mr. HANCOCK. You did not make that clear.

Mr. BIRDZELL. If I did not make it clear, I want to do so. When I spoke of the transferred deposit, I said that the transferred deposit may be set up either in a new bank or in an existing insured bank. If, for instance, the community is one where there may be a desire to set up a State bank, or where there may an existing, operating State bank that is insured, we can set up in that existing, operating State bank, or in a new State bank that may be at once capitalized and become insured, transferred deposits to the credit of all of the depositors in the old bank, and to the extent of the insured amount of their deposits—that can be done, and that is a new feature. There is one other feature that Mr. Crowley suggests.

The act as it is proposed will become effective upon its approval, which will mean that immediately the permanent plan may be put into effect; but provisions are inserted in the act that will enable every bank, whether it desires to come into the permanent plan or not, to have the benefit of insurance on its deposits until July 1st, as provided in the existing law. In other words, while this act may become effective as a permanent insurance plan immediately upon its approval, any bank that is not a member of the Federal Reserve System that desires to withdraw may do so upon giving notice within 30 days after approval, but its deposit will continue to be insured until the 1st of July of this year.

One other provision with respect to Federal Reserve membership. Provision is made in the existing law whereby nonmember banks may enjoy the benefits of insurance in this Corporation until July 1, 1937, without becoming members of the Federal Reserve System. Our experience up to date with insured banks is a strong indication to us that two types of banks, at least, which we have in the fund, will not find it to their advantage, except for some wholly artificial reason, to ever become members of the Federal Reserve System, and those two types of banks are mutual savings banks and Morris Plan or industrial banks.

So we propose in this act to amend the provision with respect to Federal Reserve membership so as to exclude Morris Plan banks, industrial banks, and mutual savings banks from that requirement; and that will mean simply this, that commercial banks desiring to continue insurance after July 1, 1937, will be required to join the Federal Reserve System.

Mr. DIRKSEN. May I ask a question at that point?

Mr. GOLDSBOROUGH. I would like to proceed in accordance with seniority, on one side and then the other. Mr. Hancock.

Mr. HANCOCK. I am not sure that he is through.

Mr. GOLDSBOROUGH. Are you through?

Mr. BIRDZELL. Perhaps I ought to comment on this, that there is one provision of law—it is paragraph 5 on page 32—under which we can require banks to protect themselves against loss through insurance—fidelity insurance, burglary insurance, and that sort of thing. It reads:

> Each insured bank shall provide such protection and indemnity against burglary, fidelity, and other similar insurable losses 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 banks.

We can give you an illustration of a bank in operation today wholly by reason of the fact that it does have burglary insurance. A large amount of money was taken from that bank. The insurance company is contesting the claim. We looked into the claim, and we think that it is a good one against the insurance company, but the company contends that it is not liable for more than about one-eighth of the loss. If they are not liable for the loss, that bank is insolvent today.

In view of the fact that its deposits are insured, and in view of the fact that the bank's attorneys and we feel that that bank has a fair prospect of recovering from the insurance company, that bank is operating today.

We think that we are entitled to whatever protection can reasonably be required of banks against losses that we know to be rather of frequent occurrence—defalcations, burglary, and the like.

We have also made provision in here to protect State banks against robbery, and so forth, where those banks are members of this Corporation. You gentlemen would be surprised, perhaps, to know that in a number of instances officers operating State banks have written in to us and suggested that some provision ought to be in the Federal law which will operate as a deterrent to bank robbers, because they say that their local authorities are absolutely at a loss to deal with those situations and that bank robbers take advantage of that and consequently rob the State banks, with almost immunity from prosecution.

The experience is different with regard to the Federal Reserve member banks, and the insured banks want to be given the same protection that is accorded now to the Federal Reserve member banks, so that the criminal features of the law in that respect have been extended to cover insured banks.

Now, I would be glad, indeed, if I may assist the committee any further by answering questions that might be based upon any feature of the proposed act.

Mr. GOLDSBOROUGH. Mr. Hancock, have you any questions that you want to ask at this time?

Mr. HANCOCK. I do not know. What is the pleasure of the committee as to proceeding? How much longer are we going to sit?

Mr. GOLDSBOROUGH. We will proceed to half past 12, I presume, unless there is some objection on the part of the committee.

Mr. HANCOCK. There are two or three questions that I would like to ask Judge Birdzell.

I am very frank to say that I have not given the time and thought to this proposed legislation that I do intend to give to it; but based upon the statement made the other day by Mr. Crowley with respect to the amount of assessment on the banks, as I understand the new law, the Corporation would have the right to levy an annual premium of one-twelfth of 1 percent on the total deposit liabilities. Is that correct?

Mr. BIRDZELL. The act itself does that.

Mr. HANCOCK. Is that discretionary with the Board?

Mr. BIRDZELL. No; that is the assessment rate that is prescribed in the law. There is provision, however, that would give the Board a discretion to lower the assessment at some future time, if experience seemed to warrant it.

Mr. HANCOCK. What do you mean, exactly, by lowering the assessment, Judge?

Mr. BIRDZELL. Suppose, for instance, that we went on for 2 or 3 years and added very materially to our reserves through assessments collected, and suppose that we had added, we will say, $75,000,000 to our funds available to meet losses. Suppose further that we had had favorable experience all the way through; and suppose that we should come upon a day when the banks were not earning, so that they might complain—this assessment would take substantially, you see, 1 percent on the entire capital of the bank; and suppose that they would say, "Your reserves are up; your experience is favorable; it is a hardship for us to meet this; can you not reduce the assessment for this particular year?" or for a particular 6 months' period. It is collected in two installments.

Mr. HANCOCK. Under the law, how much could you reduced?

Mr. BIRDZELL. Not more than 50 percent.

Mr. CROWLEY. Let me say something about that to Congressman Hancock.

I do not think that this provision, where you might have a right to reduce the assessment, could be hoped to be operative for a great many years. The Corporation should build up its surplus. I do not think that the board would look with favor toward reducing the assessment in the event it got a surplus of only $75,000,000, because I do not think that is adequate.

Mr. HANCOCK. The point that I am trying to bring out is that I got the impression the other day, from the statement presented by Mr. Crowley, that it was the judgment of the Corporation that the banks should not be responsible for all of this insurance protection.

Mr. CROWLEY. I think that that is correct, Mr. Congressman.

Mr. HANCOCK. That is the phase of this that I want to discuss with you, to find out how much protection you think should be furnished by the banks and what contingent liability you think should exist against the Government.

Mr. CROWLEY. I think this, Mr. Congressman, we must correct the evils of the past. If we are going to have the same loss ratio that we have had in the last 12 years, then I do not believe that the banks can carry that load themselves. I cannot conceive of this Congress or any other Congress not recognizing the necessity of correcting some of the abuses of the past. If we can correct and strengthen our banking system, then the amount that might have to be asked from some other source may be a very nominal amount, maybe nothing at all. If, however, we are to have a crisis again like we had in 1933, this fund could not take care of the demands upon it. I think that the losses of this fund will be nominal in the next few years. In the meantime, the Corporation should continue to build its surplus, so that in 10 or 20 or 25 years from now, if you have trouble like we had, perhaps, with some of our smaller communities, our fund would be sufficient to take care of the demands without calling on the banks for an additional burden at a time when they are under as heavy a load as they can carry.

Mr. HANCOCK. I, of course, appreciate the splendid purpose behind your viewpoint there, but what I am thinking about is this, that your statistical department has evidently made exhaustive studies in order to arrive at a fair assessment, and one that would be protective, and it seems to me, from my recollection of your statement the other day, that you said that to protect the depositors in all failures that had occurred from 1864 to 1934, it would have required an assessment of one-third of 1 percent, and to eliminate from that period what we might term the panic years, it would have required one-eighth of 1 percent.

Mr. CROWLEY. That is right.

Mr. HANCOCK. Now, you arrive at an assessment of one-twelfth of 1 percent.

Mr. CROWLEY. As I understand it, if you eliminate the periods of depression, I think that our figures show that one-tenth of 1 percent would take care of those losses on a $5,000 limit.

Mr. HANCOCK. I fully appreciate the wisdom and desirability of keeping the rate as low as possible to prevent it from being burdensome to the banks, especially today, but now we are engaged in writing a permanent law, and the suggestion has been made here that it is not the purpose of the fund to protect the depositor. Am I correct?

Mr. Crowley. I do not think that is correct, Mr. Congressman. What I really said was this, that if we were to be given certain supervisory powers we could protect ourselves. You might go back to 1920, when you had 30,000 banks. We lost nearly 15,000 banks from 1920 to 1933. A great many of our overbanked conditions have been washed out.

If we do not make the same mistakes as before and do not let this overbanked condition come back again, and if we can protect ourselves by going into a weakened institution and perhaps buying the assets or absorbing losses in order that mergers can be brought about, we are going to get away with a much lower loss. If we are given power to protect ourselves from loss, then I believe that this corporation can get along with a reasonable income. On the other hand, if we are just going to drift as in the last few years, then I do not believe you can assess against the good banks sufficient money to take care of the weaker banks without crippling the capacity of the good banks to write off their losses currently.

When it is all said and done the strength of the fund depends upon the banks being so well run and their earning capacity being sufficient to allow them to take their losses currently in place of letting them accumulate. I think everyone will agree that a good many banks permitted their losses to accumulate. Some of these banks even paid dividends, whereas they should have written off their losses.

I think that this fund should eventually build a sufficiently large surplus so that in the ordinary regional depressions—not a depression like 1933—this fund could pay its losses promptly without making an assessment against the Government or the banks.

Mr. Hancock. I notice that in the new act you propose to vest discretion in the board of directors with respect to the allocation of your capital fund—and I am just asking these questions in order that we may have a record before us. I am wondering if, in making that request, there is an implied suggestion that a situation might arise whereby you would prefer to resort to that fund in paying your losses rather than to levy an assessment?

Mr. Crowley. No. Our assessment of one-tenth of 1 percent or one-twelfth of 1 percent will bring us in from 30 to 39 million dollars a year. Supposing that during the first 2 years, before you built up any surplus, you should have a serious failure. If we were to pay that loss, we would pay it out of capital and immediately have an impaired capital. I do not think it makes any difference to the Government whether they have a no-par-value stock or $100,000,000 capital and $200,000,000 surplus, or whether they have that all in capital, because that money was given to us for the purpose of aiding us in paying losses. Only to have the income from that money, while it is helpful, is not enough. In other words, the psychological effect of our Corporation would be better if eventually we had $100,000,000 capital and $500,000,000 surplus——

Mr. Hancock. Yes; I understand that thoroughly.

It was my impression that, to begin with, that capital fund was not to be used to pay losses. Is that correct?

Mr. CROWLEY. I do not know what else they gave it to us for, then.

Mr. HANCOCK. My understanding was that it was more or less for back-log or reserve.

Mr. CROWLEY. It if was not a reserve for losses, what was the purpose of giving it to us?

Mr. HANCOCK. Under the original act, of course, you had the right to expand three times the amount of the capital structure.

Mr. CROWLEY. Yes; but when you get to the point where you are expanding and borrowing, that does not create confidence. That you would only do in case of dire necessity.

Mr. HANCOCK. Surely the capital upon which you expand your credit should be the last thing that you would touch.

Mr. CROWLEY. That is the reason why we are asking for a reduction in the capital, so that we do not touch that capital. That is the reason why we do not want to impair our capital.

Mr. HANCOCK. What is going to happen to the amount of $139,-000,000 that we took away from the Federal Reserve banks and allocated to your Insurance Corporation?

Mr. CROWLEY. Well, as I see it, it does not change their position any. One hundred thousand dollars worth of stock in a corporation that is worth $100,000, and that has no surplus, or $100,000 in a corporation with $10,000 capital and $90,000 surplus, does not affect the real value of our investment.

Mr. HANCOCK. You probably did not catch my point. I understood that a trade arrangement had been made whereby the Federal Reserve System would sell its stock to the Treasury Department. Do you know anything about that?

Mr. CROWLEY. I do not recall.

Mr. HANCOCK. Is it not a fact that the Federal Reserve System has sold $20,000,000 of that stock to the Treasury?

Mr. CROWLEY. That is in your industrial loan act of last year.

Mr. HANCOCK. That was an indirect way that they had of doing it. Just one other feature at this time, Mr. Crowley.

One of the most important and attractive features of this act to me, to begin with, was when our chairman emphasized that under the law, in event of a failure, the Corporation would immediately set up a new institution, so that the business of the community could go along smoothly. I recognize that there may be times when to do that would be futile, when it would be improper, and when it would be unwise, but I think that it would have a very serious effect if the board here should decide, as a matter of policy, not to carry out the original provision with respect to that section. Of course, there would be no sentiment in a community to set up a new bank on the failure of a bank, but in time every community would want the assistance of this Corporation in building up a new banking structure in that community, and I do hope that this board will not act arbitrarily in that matter in worthy cases.

Mr. CROWLEY. I do not think there is any doubt but what the board is sympathetic with the idea of giving to every community a bank as long as that community needs that bank. Let me tell you what our experience in the past has been. For instance, we paid off at Pittsburgh. Pittsburgh already has a great number of banks.

We have stayed there for several months now, and an expense is accumulating against us every day. We went into Indiana and we paid off an institution there. That community has sufficient banks all around it. There are a great many instances in the cities where you have two or three banks and where two banks can take care of that community well.

Mr. HANCOCK. I know that the board has been acting wisely and has done splendid work, but can it not be assured in some way that where there is only one bank in a community, the Corporation would always replace the closed institution?

Mr. CROWLEY. Let me say to you that I think you have to take some of this on the faith of the Corporation. The Corporation now has operated for some 15 months, and I think the great majority of the small bankers feel that we have been very sympathetic with them in trying to understand their problems. You men are here every single year. If the Federal Deposit Insurance Corporation gets too autocratic in some of these things, you men will immediately put something in the law to stop that abuse.

Mr. HANCOCK. Nothing that I have said has suggested that I feel that way.

Mr. CROWLEY. I understand that.

Mr. HANCOCK. Now, here is one other point that I want to clear up, and then I am through.

Could not some arrangement be made with the insured member banks whereby they would agree with the Corporation that the unexpended balances in trust funds were actual trust funds, and not deposits?

Mr. CROWLEY. Judge, that is your end of it.

Mr. HANCOCK. I have had a number of complaints from North Carolina on that particular point. Why would it not be proper and perfectly legal for the officers of a bank to enter into an agreement with you which would clarify the question as to whether they actually constituted deposits or not?

Mr. BIRDZELL. Then, if the bank should fail, and the owner of those funds should come to make claim against the Corporation, what would we say to the owners of the funds?

Mr. HANCOCK. You would just say what the bank officers had said to you.

Mr. BIRDZELL. Yes; but——

Mr. HANCOCK. If they had enough confidence to put their money in the bank that was manned by those officers, they certainly ought to be forced to rely on their agreement.

Mr. BIRDZELL. But it is not the agreement of the depositor. It would be the agreement of the bank, and the depositor would be in the position of having his claim unsatisfied. It would be hard for him to distinguish between what he had coming from the bank in the shape of uninvested trust funds and what he had coming from the bank on his savings account. Furthermore, there would come a time when it would have to be otherwise treated.

Take this situation: Say that it is a national bank that operates a trust department. The trust funds may be deposited from the trust department into the commercial department of the bank, and they may be utilized just as all other funds of the bank are utilized, in channels of commerce. Now, when the funds are placed at the disposition of the commercial department of the bank, or when they might be deposited in another bank, certainly the persons that are beneficially interested in those funds should be entitled to protection, and certainly also they become deposits just like all other deposits in the bank, and they are used as such.

Mr. HANCOCK. That is all.

Mr. GOLDSBOROUGH. Mr. Hollister.

Mr. HOLLISTER. With respect to the issue of notes and debentures of the Corporation, the existing law provides that they may issue two or three times the amount of the capital.

Mr. BIRDZELL. Yes.

Mr. HOLLISTER. They are not guaranteed by the Government, although they are tax exempt.

Mr. BIRDZELL. Under the proposed law they would not be.

Mr. HOLLISTER. Is that in the proposed law?

Mr. BIRDZELL. Yes; that is in the proposed law, although I did not cover it.

Mr. HOLLISTER. That is what I thought, that there is no guarantee whatsoever of that kind, either in the existing law or in the new law.

Mr. BIRDZELL. But the Treasury is authorized to purchase them.

Mr. HOLLISTER. The Treasury is authorized to, but the Treasury might not purchase them. But there is no guaranty by the Government of those debentures?

Mr. BIRDZELL. You are correct.

Mr. HOLLISTER. Under the existing law, where there is a provision that three times the amount of capital may be issued in bonds and debentures, those debentures can be sold to better advantage because of the unlimited assessment provision, for as long as losses may be assessed continually against the banks, there can always be built up a protection in the Corporation for those who buy the debentures.

Mr. BIRDZELL. That is correct.

Mr. HOLLISTER. But under the proposed law, with a limitation of one-twelfth of 1 percent a year, it is difficult for me to see the possible market of those debentures outside of the Treasury. Here you have a debenture that is not guaranteed by the Government, even though it is nontaxable. Under a set of disastrous circumstances your capital aud surplus might be completely wiped out.

Mr. BIRDZELL. There is a further market provided for those debentures, the Reconstruction Finance Corporation, to the extent of $250,000,000.

Mr. HOLLISTER. Yes; but that would require action by the Government. I am not saying that it is wrong, but I am merely trying to get at the change in the whole idea. The original idea was a debenture which was a sound proposition for private capital, because of the fact that it had behind it the whole banking system of the country, under the unlimited assessment idea. Now you have a debenture which it seems to me has no private market whatsoever, but is solely valuable insofar as the Reconstruction Finance Corporation or the Treasury would care to invest.

Is not that the case?

Mr. BIRDZELL. Yes.

Mr. HOLLISTER. It really ceases to be a private obligation to be sold in the market.

Mr. Crowley. It is true that if we had to issue debentures to private borrowers up to three times the capital, undoubtedly the condition would be such that you could not find a ready market. It might be possible that you had $300,000,000 in securities and that you might only want to borrow $50,000. Of course, you could sell debentures on that kind of a collateral provision.

Mr. Hollister. Of course, the theory in selling debentures would be to get additional funds in order to satisfy the demands of the Corporation, and if conditions should arise where it would appear to be necessary for the Corporation to sell debentures, under the new law it seems to me that the average private investor, when he would realize that the only thing back of these debentures is the possibility of collecting one-twelfth of 1 percent annually, would say, "Notwithstanding the nontaxable feature, that is hardly a thing that I am interested in."

Mr. Crowley. That is true if you had a critical situation.

Mr. Hollister. But would you be selling them unless you had a critical situation?

Mr. Crowley. No; unless you would be doing it for some short-term borrowings. Suppose that you had $3,000,000 in securities and the market might be temporarily down. That would not affect your borrowing as long as you had adequate collateral. However, if we got to a point where we had an emergency, and we had to issue 4 or 5 million dollars of debentures at that particular stage, I do not believe that the open market would absorb those debentures unless you had the Government guarantee. The fact that the Secretary of the Treasury would come to our rescue if we had that kind of a condition, however, gives us some confidence.

Mr. Hollister. I am not presenting the view that it is wrong. I am merely trying to bring out that, after all, if such debentures under the new law should be issued, some kind of governmental agency, the R. F. C. or the Treasury, would have to take them.

Mr. Crowley. We have $250,000,000 that the R. F. C. have earmarked for our corporation.

Mr. Hollister. On page 5, in section 11, as to obligations payable outside of the United States, that affects only a few banks and is put in there because of the foreign competitive situation, is it?

Mr. Birdzell. It affects banks that have European branches, or branches in outlying possessions, like Puerto Rico.

Mr. Hollister. Was that not included in the bill that passed the House last year, but which never got through the Senate?

Mr. Birdzell. No; that is the old law.

Mr. Hollister. Section 11, on page 5?

Mr. Birdzell. Where is the provision that you are referring to?

Mr. Hollister. The proviso at the bottom, which reads:

> *Provided*, That any obligation of a bank which is payable only at an office of the bank located outside the States of the United States, the District of Columbia, and the Territories of Hawaii and Alaska shall not be a deposit for purposes of this section or be included as a part of total deposits or of an insured deposit.

Mr. Birdzell. That was in the omnibus bill, which did not get through.

Mr. HOLLISTER. And that is there because, if they had the cost of the insurance to add to their operating cost, they would be in a bad competitive situation in a foreign country?

Mr. BIRDZELL. Yes; that is the purpose of that, if I understand your question, and that provision there is consistent with the provision in last year's omnibus bill.

Mr. GOLDSBOROUGH. Mr. Williams.

Mr. WILLIAMS. To my mind, there are two very fundamental things in this bill.

First, I am thinking about what you are going to do with some 8,000 nonmember banks that are not in the permanent insurance plan, and which will not be under the provisions of this bill.

In the second place, there is the question of a limited liability.

Now, it is not contemplated, is it, that there will come a time when these insurance deposits will not be paid in full?

Mr. CROWLEY. You mean that these funds will not be sufficient?

Mr. WILLIAMS. Yes.

Mr. CROWLEY. It is my honest judgment that if you will give to this Corporation the supervisory powers that we have asked for, that this Corporation should be able to keep itself solvent, barring unforeseen accidents.

If this country cannot operate a banking system so that the depositors will not suffer losses that may break this Corporation, then there is something distinctly wrong with your banking system and your monetary system. That calls for a corrective measure far beyond the powers of the Federal Deposit Insurance Corporation.

Now, I believe that this Corporation can operate and pay to depositors their losses with any kind of normal conditions.

Mr. WILLIAMS. That is perhaps true.

Mr. CROWLEY. I hope it is true.

Mr. WILLIAMS. I am not so much concerned with the power of the Board to reduce this assessment as I am with the power to raise it in case it is necessary, in order to take care of the liabilities of the Corporation.

Mr. CROWLEY. You understand that while the Corporation would look with favor on all of the revenue that you can give us, nevertheless you cannot have an unlimited liability or a liability so large that in times of stress you may weaken your entire banking structure.

Mr. WILLIAMS. Then your whole system, at the very time that it is needed the most by the depositors of the country, breaks down?

Mr. CROWLEY. I think that is where supervision comes in—to prevent that.

Mr. WILLIAMS. You have the supervision which will do it.

Mr. CROWLEY. Correct.

Mr. WILLIAMS. But why not, if you say that you can administer the law in such a way as to prevent those losses by the discretion and the power that is in the Board, increases the assessment in case it is necessary?

Mr. CROWLEY. I think that there is a danger that deposit insurance might break down the private initiative of men who are trying to operate these institutions. We have a great many banks that we are insuring almost 100 percent. Men operating these banks will not have the same incentive as those which are operating banks only 5, 10, or 15 percent insured.

Mr. WILLIAMS. Of course, you agree that we do not need any insurance as long as there are no bank failures.

Mr. CROWLEY. I think that you will always have a certain number of bank failures, but it is like anything else—like your hospitals or your railroads or anything. If you have an epidemic in Washington where everyone in Washington is sick, your hospitals are not large enough to care for them. You cannot build this fund large enough to pay out 16 or 19 billion dollars overnight.

Mr. WILLIAMS. Then it is based upon the idea that you may have a condition where you could not pay out?

Mr. CROWLEY. I think everyone will agree that we could not pay out our entire liability at one time.

Mr. WILLIAMS. What other contingent funds have you in mind if the assessment fails? What else would you do?

Mr. CROWLEY. We have our right to borrow from the Treasury. That is all we have.

Mr. WILLIAMS. You are assuming, now——

Mr. GOLDSBOROUGH. You do not mean the right to borrow? You mean that the Treasury is authorized to loan if necessary?

Mr. WILLIAMS. You mean that under this act the borrowing power is confined to the Treasury Department alone?

Mr. CROWLEY. And to the $25,000,000 from the R. F. C.

Mr. WILLIAMS. Under this act, are private individuals permitted to lend you money on your debentures?

Mr. CROWLEY. Yes; they are permitted to do it.

Mr. WILLIAMS. If they want to?

Mr. CROWLEY. Yes; if they want to?

Mr. WILLIAMS. If there is a private field for the investment, they are permitted under this law to invest in your debentures?

Mr. CROWLEY. That is correct.

Mr. WILLIAMS. You have that power?

Mr. CROWLEY. That is right.

Mr. WILLIAMS. What is the purpose of allocating the capital structure of that institution to surplus?

Mr. CROWLEY. I do not think that allocation of capital has anything to do with the right of borrowing.

Mr. WILLIAMS. It is the intention to use that in case of need to pay the losses?

Mr. CROWLEY. Yes. We may take——

Mr. WILLIAMS. The idea back of it is that the money that is received from the Federal Reserve banks and from the Treasury should be used as a reserve fund to pay these losses, rather than from the banks themselves?

Mr. CROWLEY. That is correct.

Mr. WILLIAMS. Now——

Mr. CROWLEY. Let me answer that. I think the Government, when it licenses a bank and establishes a banking system, assumes a responsibility to the depositors, and when it created this Corporation I think that it assumed a responsibility for the protection of the depositors. I do not believe that any man argues that we should continue to permit losses to occur as has been the case in the last 12 years.

Mr. WILLIAMS. Nobody will contend that, I think, but you expect, by reason of your regulatory powers, and by reason of reports made to you, and your inspections, to regulate, within reasonable grounds, the banking activities of the country and to prevent these failures?

Mr. CROWLEY. But, Congressman, we do not guarantee to prevent failures entirely. We hope to reduce the number of failures.

Mr. WILLIAMS. That is so, and the very purpose of all this insurance, according to my idea, should be to guarantee, in case of failure, the payment of the depositors in full.

Mr. CROWLEY. I think that is correct, but I do not see any way in the world that you can draft a bill or that you can give us sufficient funds, so that you could say that at all times, regardless of whether you have a complete collapse of your banking system, this Corporation could pay the losses of all depositors.

Mr. WILLIAMS. Could you conceive of a complete collapse in the banking system of this country now, under the supervision of your Corporation and of the Federal Reserve system?

Mr. CROWLEY. All that I can say to you is this: I believe that under our rebuilding program, the banks as a whole are in the best shape that they have been in a great many years. With the proper kind of supervision we should not have the losses that we have had in the past.

Mr. WILLIAMS. Now, merely to furnish a factual background, there are about thirty-six billion and a half in deposits now, are there not?

Mr. CROWLEY. That is correct.

Mr. WILLIAMS. What part of that is in time deposits?

Mr. GOLDSBOROUGH. Would it be agreeable for you gentlemen to come back tomorrow morning?

I want to say to the members of the committee that there is a gentleman here from California who has to go back tonight, and he and Mr. Ford have both asked that he be allowed to put a statement in the record.

Mr. Adams, will you come up here, please?

It is very important, Mr. Adams, that the members of the committee get to the floor of the House as quickly as possible, and I am wondering if you could limit your statement to 10 minutes, and then give to the members of the committee the written statement which you left with me the other day.

STATEMENT OF EDSON F. ADAMS, PRESIDENT FARMERS AND MERCHANTS SAVINGS BANK, OAKLAND, CALIF.

Mr. ADAMS. I think that I would have to read the statement, Mr. Chairman, in order to make it clear. If I did not do that, I do not think that they would grasp it.

Mr. GOLDSBOROUGH. You will proceed, then.

Mr. ADAMS. It appears quite necessary at this time that the Banking Act of 1933 and Federal Deposit Insurance Act be amended covering certain important matters as they now injuriously affect banks doing a strictly savings bank business and, also, mutual savings banks of the Middle Western and Pacific States which are not numerous enough to protect themselves by establishing a savings-deposit guarantee under State authority, as has been done in the State of New York.

Briefly, the main changes requested in the present laws are as follows:

First, savings banks, doing no commercial business, and mutual savings banks should be placed in a class or group by themselves instead of being required to join in guaranteeing deposits in banks doing all types of banking.

Second, savings banks should be granted the right to obtain interest on deposits with approved commercial banks of reserves and surplus funds awaiting the demand for savings bank loans.

Third, savings banks and mutual savings banks should not be forced to join the Federal Reserve System to obtain insurance, since they do no commercial business, and, therefore, are not able to avail themselves of its facilities.

Fourth, savings banks in the West should be granted the right to allow depositors to use checks against short-notice savings accounts, in order to protect their term-savings accounts against competitors. State savings banks in California have had this right for many years.

As to savings banks guarantee of all types of deposits, if the country is to have permanent-deposit insurance, the great criticism of the present act is that all banks are put together in one group, when their methods of business are, in many cases, diametrically opposed, some pay interest on practically all of their deposits, while others pay no interest on any deposits and therefore require entirely different handling of their resources.

It appears there should be two or three Federal Deposit Insurance Corporations, based on the actual liability involved, instead of one, with separate officers and garuanties for each corporation representing each group of banks, and with provision for representation on its board of directors; the commercial banks being placed in one group, the departmental banks in one group, and the strictly savings banks and mutual savings banks together in a separate group. In this way each member of each group would be insuring its own type of business, which would be the only fair way to handle it. Insurance for savings banks would command a very low rate compared with commercial and other types of banks. In California all savings-bank loans can be made only on the highest type of security and the classes of security and the conservative margins required are plainly stated in our bank act.

It is neither fair nor just to mutual savings banks and strictly savings banks, as operated under western conditions, to link them with departmental banks, commercial banks, and trust companies, where money is shunted from one department to the other, as the opportunity offers to play with the savings of savings depositors. Nor is this all. In many banks property taken in under foreclosure is thrown into holding companies owned by the bank's stockholders and manipulated so as to hide the fact that the bank is carrying property taken for debt, thereby weakening the bank and deceiving the public.

Real savings banks, operated as such, are a boon to the man or woman of small means. Conditions in the West are different from those in the Eastern States, hence codes, rules, and regulations should vary in each Federal Reserve district to conform to existing conditions or customs not in conflict with good savings-bank practices.

This is so not only in banking but also in other lines of business: For example, the first N. R. A. chief in California found that codes prepared to cover eastern conditions did not fit those in the West.

National banks under several administrations have been receiving the individual savings of the people and issuing savings passbooks showing deposits and the money so received credited to the depositor as a savings deposit, but here it ends. In practice, from here on, the money so received is put into and mingled with the other funds of the national bank, a commercial institution.

In a national bank the people's savings deposits can be loaned on notes of hand at will be the officials of the bank, and, if they choose, without any security whatsoever to protect the loan except the personal responsibility of the recipient of the loan.

In the interest of safety the money so deposited by savings depositors should be loaned without the borrower first putting up ample approved security to secure the money so loaned. In California the law governing State banks requires that no money received from savings deposits be loaned either by strictly savings banks, mutual savings banks, or by a savings department of a departmental bank except on ample and approved security. These provisions are apparently entirely ignored in the National Bank Act.

Mr. Goldsborough. I do not believe that it will be possible for the members to stay, and each member has a copy of the statement that you are reading, Mr. Adams, and I am going to suggest, sir—and I want to be of every service that I can to you and your institution—that you just insert your statement into the record. I can assure you that every member of the committee will read it.

You have seen how they are leaving. I do not believe that you can hold them.

Mr. Wolcott. I am staying here merely out of courtesy to you, and I would prefer to read this in my office, if you are just going to read it. I understood that you were going to comment on it as you went along.

Mr. Adams. No; the comments are all in it, but I have some additions, in regard to other things.

Mr. Wolcott. My opinion is that that which is written you could put in the record without reading. We have some important legislation on the floor.

Mr. Goldsborough. The members of the committee really do have to go on the floor, and, of course, if you were in a position to wait, we would be very happy to hear you in full. We are extending to you this courtesy because you have to get back to California.

Mr. Adams. I can wait until the end of the week, if there is no opportunity now.

Mr. Goldsborough. I am not sure about it after Friday. On Thursday we will have to have the home loan bill on the floor, and I do not know what will happen.

I can assure you that you will receive just as much consideration if you will just allow that statement to go into the record. This committe is not going to overlook reading your statement.

Mr. Adams. I will tell you: I would like to submit copies of the letter from Mr. Parker S. Maddux, who is the president of the San Francisco bank——

Mr. Goldsborough. Yes, sir; without objection, it will be inserted in the record.

Mr. Adams. And also from Mr. Richard M. Tobin, who is the president of the Hibernia Bank, San Francisco.

Mr. GOLDSBOROUGH. Without objection, they may go into the record at this point.

(The letters referred to are as follows:)

THE SAN FRANCISCO BANK,
San Francisco, Calif., February 6, 1935.

EDSON F. ADAMS, Esq.,
President Farmers & Merchants Savings Bank,
Oakland, Calif.

DEAR MR. ADAMS: You have exhibited to me a statement which you propose to submit to the chairman and members of the Banking Committee of the House of Representatives at Washington. In this statement you suggest four main changes to be made in the present banking laws of the United States.

The purpose of this letter is to assure you and the committee that this bank is favorable to all of the suggested changes.

Hoping that you have a pleasant and successful trip to Washington, I beg to remain,

Very truly yours,

PARKER S. MADDUX, *President.*

HIBERNIA BANK,
San Francisco, Calif., February 4, 1935.

Mr. EDSON F. ADAMS, *President,*
Farmers & Merchants Savings Bank, Oakland, Calif.

DEAR MR. ADAMS: I have carefully read the draft of your proposed "Statement to the chairman and Members of the Bank Committee."

The four objectives which you cite on the first page are all excellent, and I approve especially of the first three.

With best wishes for your success, I remain

Yours very truly,

RICHARD M. TOBIN.

Mr. ADAMS. I might say, in connection with these letters, that the San Francisco Bank has savings deposits of $151,224,000, and total resources of $167,847,098. They have 36,731 term savings accounts and also special savings accounts with checking privileges, 5,800; making total savings accounts 42,531.

The Hibernia Bank has savings deposits of $87,422,625, and the total resources are $98,593,230. They have 69,889 savings accounts.

The bank of which I am president, the Farmers & Merchants Savings Bank, has savings deposits of $7,877,094.96, and total resources of $8,385,636.68. We have 10,117 term savings accounts and 19,042 term school savings accounts and 2,317 special ordinary savings accounts, with checking privileges, making total savings accounts 31,476. In this bank, the percentage of deposits covered by Federal deposit insurance is 85 percent.

The Zion's Savings Bank & Trust Co. are also desirous of having some relief, as is shown by their letter to Mr. Frank B. Lanham, special representative, Federal Deposit Insurance Corporation, Washington, D. C. Their savings deposits amount to $13,103,232.13.

Mr. CAVICCHIA. May I suggest that the gentleman be given time to hand to you any other communications that he wants inserted in the record. If he does not have them now, he may hand them in later in the day.

Mr. GOLDSBOROUGH. That will be entirely agreeable, if there is anything else.

Mr. ADAMS. I would like to call your attention to this, that, of course, I have some other things here which go to support my proposition.

Mr. GOLDSBOROUGH. I am inclined to think that the mutual banks are going to be taken care of in this legislation. I do not believe that you are going to find any fault with that.

Mr. ADAMS. I am not a mutual. We are a stock bank, you understand, and we have been left entirely out of this bill. The only people that are referred to in this bill at all are the mutual savings banks and nobody else, and that puts us in California and in the West in a bad position. The Zion's Savings Bank & Trust Co., in Salt Lake City, are, as I have just indicated, in the same position.

Mr. WILLIAMS. Can you not come into the Federal Savings and Loan Insurance Corporation?

Mr. ADAMS. No, sir; not unless we join the Federal Reserve System, and we have no business in the Federal Reserve System. We can do no business with them.

Mr. WILLIAMS. I think that you are in error about that. The law permits any institution that can qualify to come in.

Mr. ADAMS. We have already joined in the temporary deposit insurance, you understand.

Mr. GOLDSBOROUGH. And you think that your assessment should be reduced?

Mr. ADAMS. Not necessarily, but we do not want to be made liable for all classes of banking.

Mr. WILLIAMS. I am talking about the Federal Savings and Loan Insurance Corporation. I do not know whether you understood me. The act passed last year by this Congress authorized building and loan institutions and savings banks of the country to have an insurance plan. What is the reason that the institution that you represent cannot come into that plan if it wants to?

Mr. ADAMS. Because we are not a building and loan institution, as their type of business is entirely different from that of a bank. The business which we do is of the same character, exactly, as the mutuals, only that we have stock instead of a mutual association.

Mr. WILLIAMS. But it includes not only the building and loan associations but the savings banks and mutual banks as well.

Mr. CAVICCHIA. As I understand it, Mr. Williams, the language of the act that you are referring to states "and other financial institutions", which opens the door to this type.

Mr. WILLIAMS. It not only does that, but it mentions the very class of institution about which he is talking.

I think, Mr. Adams, that you will find that out upon investigation.

Mr. ADAMS. We have not been able to find that, and if we have to be brought in the Federal Reserve System, then we have to become a departmental bank, and we do not want to.

Mr. GOLDSBOROUGH. Let me see if this suggestion will be helpful to you: If you will insert what you have there in the record, and then have an amendment drawn up which meets with your views and hand that to Mr. Ford, he can then offer it, and we will consider it with other amendments.

Mr. ADAMS. I will do that, Mr. Chairman, but I wanted to say this, that you talked of national banks today, and they have savings deposits amounting to $6,053,020,000, and those savings deposits can be loaned out on unsecured notes, and there is nothing to prevent that, not a thing, and they are doing it, and we do not want to be tied to the tail of that kite, because we do not consider it a safe way of handling of savings deposits.

I have been in business for 40 years, and I think I know something about it.

Mr. GOLDSBOROUGH. Prior to today, I thought that your idea was that your assessment should not be as great as the assessment of a commercial bank.

Mr. ADAMS. It would not be under ordinary circumstances, if you took the liability into consideration.

Mr. WILLIAMS. As I understand you, you want Congress to set up another corporation, or an insurance company, simply to take care of the class of institutions that you represent?

Mr. ADAMS. No. This could be done by classifying us, possibly, with the mutuals, the outside mutuals which you brought in in your last amendment.

Mr. GOLDSBOROUGH. If your bank is really in the same class with the mutuals, insofar as your liabilities are concerned, I am certain that this committee will deal very justly with any amendment which may be offered, and I presume that you will want Mr. Ford to offer it, because, as I understand it, you only have 3 or 4 of these institutions in the United States.

Mr. ADAMS. There would be a great many in the United States, if they had the opportunity.

Mr. GOLDSBOROUGH. I understood you to tell me that there are two in California and one in Utah.

Mr. ADAMS. What I said was that the two banks in California had endorsed my propositions.

Mr. WOLCOTT. Are you under State supervision?

Mr. ADAMS. Under State supervision.

Mr. CAVICCHIA. I think that that matter could be taken care of by Mr. Ford, who is a member of this committee.

Mr. ADAMS. Yes. Shall I submit this?

Mr. GOLDSBOROUGH. Yes; and it will be inserted in the record and printed, and your amendment should be prepared and introduced, I presume, by Mr. Ford, from your State.

Mr. ADAMS. You mean these additional things?

Mr. GOLDSBOROUGH. Yes. They will be inserted in the record. Just hand them to the reporter.

The remainder of the statement is as follows:

By combinations and other manipulations, banks incorporated principally for commercial business have acquired the people's savings deposits, sometimes in amounts almost double their commercial deposits. In one instance, in a published statement, a national bank has approximately 260 millions in commercial deposits and approximately 460 millions in savings deposits, all dumped into the same pot and these savings deposits can be handled and loaned commercially, with all the attendant risks of commercial banking, while mutual savings banks and savings banks doing no commercial business, when loaning their deposits, must require ample security for all loans made. This condition of facts shows very clearly that banks having only saving deposits should be put in an independent group by themselves and not be forced to participate in guaranteeing unsecured loans of commercial banks.

As to interest on reserves of savings banks in correspondent banks, under the provisions of the Banking Act of 1933, mutual savings banks are allowed to receive interest upon their deposits (sec. 11, par. (b.)).

The Legislature of the State of California in 1933, with the approval of the State superintendent of banks, amended the State bank act. General provisions section 21 (1). This section practically follows section 19 of the Federal Reserve Act but allows savings banks to receive interest on their deposits with commercial banks.

SECTION 21. (1) No bank shall, directly or indirectly, by any device whatever, pay any interest on any deposit which is payable on demand: *Provided*, That nothing herein contained shall be construed as prohibiting the payment of interest in accordance with the terms of any certificate of deposit or other contract heretofore entered into in good faith which is in force on the date of the enactment hereof; but no such certificate of deposit or other contract shall be renewed or extended unless it shall be modified to conform herewith, and every bank shall take such action as may be necessary to conform herewith as soon as possible consistently with its contractual obligations: *Provided, however*, That this section shall not apply to any deposit of such bank which is payable only at an office thereof located in a foreign country, and shall not apply to any deposit made by a savings bank, nor to any deposit of public funds made by or on behalf of the State, or of any county, city and county, city, town, municipality or other public or municipal corporation of the State of California, with respect to which payment of interest is required under State law. * * *

There are 594 mutual savings banks in the United States, as of June 30, 1932, and they are located in the following States:

New England States 379, total resources	$3,711,220,000
Eastern States 195, total resources	7,047,074,000
Middle Western States 16, total resources	220,708,000
Pacific States 4, total resources	155,140,000
Total	11,134,142,000

It will be noted that 574 are located in the New England and Eastern States, with resources of $10,758,294,000, while the Middle Western and Pacific States have only 20, with total resources of $375,848,000, or approximately 3½ percent of the total resources of the mutual savings banks in the United States.

A law giving to the mutual savings banks of New England and Eastern States special privileges by not allowing strictly savings banks in the rest of the country to receive interest from commercial banks upon their deposits is unjust and unsound. In order to operate savings banks conservatively, so they will be able to pay withdrawals without affecting their loaning ability, it is very essential that they maintain sufficient balances in cash with banks duly authorized by the State banking department, as depositories. Unless a savings bank has the right to receive some interest from its depositories, the tendency would be to operate with as little cash as possible, in order to meet the interest to savings depositors, costs of operation, and other demands of the savings bank business. Under certain conditions of the money market, this might at times cause the hurried investment in securities and possibly would encourage loaning on a poorer type of real-estate security.

As to savings banks as members of the Federal Reserve System, the Federal Reserve System was inaugurated to develop the commercial banking resources of the country. Savings banks, properly operated, have practically nothing in common with the Federal Reserve System and it would be a great injustice to force them to join that System. They are not able to discount their loans with the Federal Reserve bank and therefore do not receive the main benefit accruing to commercial banks which are members of the System.

As to savings banks' depositors being allowed the use of checks to withdraw funds, the Federal Reserve bank, having in mind solely commercial business, would probably classify checking accounts against a certain class of savings accounts, on which checks are used as a convenient form of withdrawal, as being commercial business which would not be the case, as no commercial loans are made at all by savings banks in the State of California. It has been found in California, under western conditions, that a strictly savings bank, in order to function properly, must have this type of account. These accounts are opened principally for personal convenience by savings depositors, who prefer to do all their banking in one place. They are not of a type that require commercial accommodation. The balances are moderate and the checking service has been found to be a benefit to the depositor as well as to the savings bank. Also, frequently, people obtain loans from a savings bank, open checking accounts, and some portion of the money remains with the bank for a long period.

The savings bank of which I am president has over 2,286 accounts of this type, aggregating over $780,000, of which only 21 are above $5,000, and 275 between $500 and $5,000; 1,990 accounts are below $500, which goes to show that these accounts are in no way commercial accounts, but are opened for the necessary personal accommodation of our savings depositors; and it also shows that, in our western country, the ability to allow a withdrawal by check is extremely important and necessary to any savings bank doing only a savings-bank business. This class of accounts has a provision for a 30 days' notice, if the bank should require it.

Our State banking department for years has classified these accounts as savings accounts. Where there is strong competition by departmental banks, savings deposits would be transferred from strictly savings banks that do not have checking privileges, to other banks, and would force savings banks to open commercial departments at additional expense, without really wanting to do a commercial business, simply to accommodate and give personal checking service to its savings depositors.

With over 40 years of experience in the savings-bank business, I have observed that strictly savings bank operated by men versed in savings-bank administration prosper and serve the public in a better way than those left to be administered by highly specialized commercial bankers, whose main thought is the advancement of commercial business.

I therefore urge that your committee amend the present acts at this session of the Congress as outlined in the four changes enumerated, so that savings banks may safely continue deposit insurance and at the same time have reasonable protection in operating under western conditions.

Mr. CAVICCHIA. May I remind you, Mr. Williams, that one question that you asked was not answered, and I hope you will have an answer as to what will happen to those 8,000 banks?

Mr. WILLIAMS. Yes; I am going to go back to that. It is very important.

Mr. GOLDSBOROUGH. The committee will adjourn until tomorrow morning at 10:30.

(Thereupon, at 12:45 p. m., an adjournment was taken until Wednesday morning, Feb. 27, 1935, at 10:30 o'clock.)

BANKING ACT OF 1935

WEDNESDAY, FEBRUARY 27, 1935

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

Hearings on the bill above referred to were resumed at 10:30 a. m., Hon. T. Alan Goldsborough presiding.

Mr. Goldsborough. The committee will be in order.

Mr. Williams, will you resume your questioning where you left off yesterday?

STATEMENTS OF LEO T. CROWLEY, CHAIRMAN, AND L. E. BIRDZELL, GENERAL COUNSEL, FEDERAL DEPOSIT INSURANCE CORPORATION—Resumed

Mr. Williams. I believe that we agreed that the amount of deposits in the commercial banks of the country was practically 36½ billion dollars. The last question was, what part of that is in time deposits.

Mr. Crowley. I am told about one-third. That would be about 12 billions.

Mr. Williams. What character of time deposits does that involve? There are different kinds of time deposits.

Mr. Crowley. That includes, for instance, savings accounts and certificates of deposit, where they are not subject to check.

Mr. Williams. That means all of the accounts, does it, in which notice is required before they can be withdrawn; or, in other words, they are for a definite, fixed period and not subject to check at all?

Mr. Crowley. That is correct, where you have to give definite notice of withdrawal.

That does not include postal savings.

Mr. Cavicchia. Do I understand that your answer to Mr. Williams' question includes deposits in savings institutions?

Mr. Crowley. No, sir; it does not.

Mr. Williams. They are not included?

Mr. Crowley. Would you like some detail on that, Mr. Williams? We have some figures here, if you would like to have us read them.

Mr. Williams. As far as I am concerned, no; unless someone else on the committee wants it more definitely than that.

Mr. Cavicchia. Does that figure of 36½ billions that you gave include sums deposited in savings banks and mutual banks?

Mr. Crowley. No; it does not; just commercial banks.

Mr. Williams. During the last year, or after the passage of the deposit insurance law and before the creation of this Corporation, as I understand it, there have been orders issued by the Federal Reserve bank and by the Corporation as well concerning the interest charges to be paid both on demand and time deposits in various banks that are insured.

Mr. CROWLEY. That is correct.

Mr. WILLIAMS. What have been the savings to the banks of the country by reason of those orders and their following out the instructions that were given to them with reference to paying no interest on demand deposits and limiting the amount that they would pay on time deposits?

Mr. CROWLEY. I do not know that we can give that to you. That is in our testimony, Mr. Congressman, and we will give it to you.

Mr. WILLIAMS. Perhaps I have your statement on that, but let me see if I understand it. Do I understand from your statement that by reason of that action on the part of the banks in not paying interest at all on demand deposits and cutting down the interest paid on time deposits there has been a saving to the extent of 26 cents per $100 during the year 1934?

Mr. CROWLEY. As the banks became more liquid, and as the demand for money became less, the banks themselves declined to pay interest on daily balances. That was prior to the Banking Act of 1933 Then, Mr. Congressman, in the Banking Act of 1933 it was provided they could not pay interest on demand deposits, and we then showed a saving that had been brought about by not paying interest on demand deposits. A percentage of that saving was brought about by the legislation in 1933.

Mr. WILLIAMS. The fact remains that that was done, regardless of the cause of it, and that the banks during the last year have saved about one-fourth of 1 percent on their entire deposits by having cut down the rate of interest paid to the depositors?

Mr. CROWLEY. That is correct.

Mr. FOX. Our figures are based on national banks, and the data is available for the last half of 1933, the 6 months subsequent to the passage of the act.

That shows that the savings to all national banks because of the passage of the Banking Act of 1933, which reduced the interest on time deposits and eliminated the interest on demand deposits, was 28 cents per $100 on deposits, 2 cents of which was due to a reduction in the rate of interest on time deposits and 26 cents due to the elimination of interest on demand deposits.

Mr. WILLIAMS. Then, instead of 26 cents, it is 28 cents per $100?

Mr. FOX. That is correct.

Mr. WILLIAMS. Which would be between a third and a fourth of 1 percent on all of the deposits in the banks, which in figures would amount to how much?

(At this point Mr. Crowley handed a paper to Mr. Williams.)

Mr. WILLIAMS. I would like to have that in the record, to show how much the banks of the country have served by reason of reductions in the rates of interest paid during the last year.

Mr. REILLY. Have the banks been reporting how much money they saved as interest on time and demand deposits?

Mr. CROWLEY. The banking law of 1933 forbids that.

Mr. REILLY. I know, but before that did not they make a specific report of the amounts of money that they paid on demand deposits?

Mr. CROWLEY. Yes.

Mr. FOX. The national banks filed reports of earnings and dividends every 6 months, and in that report is the section which details their expenses, and there are three items in that section.

Mr. GOLDSBOROUGH. Will you proceed, Mr. Williams?

Mr. WILLIAMS. It would be a simple matter of calculation.

Mr. FOX. It is about $43,000,000 per year for national banks.

Mr. WILLIAMS. $43,000,000 for national banks alone.

Have you any data showing the amount that has been saved by the Federal Reserve members and the nonmember banks?

Mr. FOX. We could put the information in the record for the Federal Reserve member banks. We did not until this year have information on the nonmember State banks. Therefore, we could not give you that information.

Mr. WILLIAMS. Your statement of a saving of 28 cents per $100 is based on the record of the national banks alone?

Mr. FOX. That is correct.

Mr. WILLIAMS. How does that compare with the State member banks that you know of?

Mr. FOX. I will have to put that in the record later on.

Mr. WILLIAMS. You will put that in the record for us?

Mr. FOX. Yes, sir.

Total savings in interest paid on deposits by State member banks were at the rate of $30,000,000 per year. Expressed another way, the savings in interest expense to State member banks amounted to 29 cents per year for each $100 of total deposits.

Mr. WILLIAMS. And you have no information at all with reference to the amount that the State member banks have saved on that item?

Mr. FOX. No, sir. That is not available at all.

Mr. WILLIAMS. And it is a fact, is it not, that the State nonmember banks have followed the same policy as the member banks and the national banks in that respect throughout the country?

Mr. FOX. I think so.

Mr. CROWLEY. I think that is generally true, Mr. Congressman. In some States they have not.

Mr. WILLIAMS. Now, it is also true, is it not, that you issued an order—and I refer to your Corporation—limiting the interest on time deposits to 3 percent, and then later on formulated, at least, another order bringing it down to 2½ percent?

Mr. CROWLEY. That is correct.

Mr. WILLIAMS. But that was never put into effect, was it? Some controversy arose over the legality of it?

Mr. CROWLEY. That is correct. A year ago last December the Federal Deposit Insurance Corporation and the Federal Reserve Board fixed a 3-percent maximum. Then last December the Federal Reserve Board fixed a rate of 2½ percent, and we did likewise; and then the controversy arose, and we withdrew our regulation.

Mr. WILLIAMS. Then the practice that has heretofore prevailed throughout the country of paying in certain cases interest on demand deposits is a thing of the past, is it not?

Mr. GOLDSBOROUGH. May I suggest to you, Mr. Williams, that in my section, in the First Congressional District of Maryland, they are still paying 2½ percent?

Mr. WILLIAMS. But that is not a fact so far as the order of the Board is concerned?

Mr. CROWLEY. The order of the Board was drawn, but a great many of the banks, as the chairman says, have followed along on the 2½ percent.

Mr. WILLIAMS. And they are following that not by your order or direction but because of their own inclination and perhaps a desire to be uniform with the order of the Federal Reserve System?

Mr. FORD. One big banking group on the coast did not do that. They offered 3 percent; and all of the other banks came to me and asked me to come down to see you to change it, which I could not do.

Mr. CROWLEY. May I say this, on that matter of time deposits, first, that I think that history will show that prior to the Federal Reserve Board and prior to the Federal Deposit Insurance Corporation issuing their regulations, in years gone by banks paid as high as 4, 5, and 6 percent for what we would term "time deposits." They offered all kinds of premiums, like blankets and clocks and savings banks, and the banks which perhaps should not have paid those high interest rates were the ones that were the most apt to offer to the depositor an interest rate that was not sound.

Now, the same thing was true of demand deposits. For instance, a great many of your national corporations would have $25,000 or $50,000 balances, and the banks would bid for that business; and in reality in a great many instances it was not of any particular benefit, and that was considered as an unsound practice. That is the reason why in the Banking Act of 1933 you eliminated that abuse, because it was an unwise and unsafe practice.

Now, the same thing goes for interest on time deposits. What the supervisory agencies wanted to bring about was that a bank not only paid to these people a reasonable rate of interest but also gave them back their principal, because in a great many instances where the bank paid 4, 5, and 6 percent, the depositors lost a very large percentage of their principal.

Mr. WILLIAMS. Is it your idea now that your Corporation should have the power to direct the members of your Corporation not to pay interest on demand deposits and to limit their payments on time deposits to 2½ percent?

Mr. CROWLEY. I think it would be a great contribution to your banking system if we had that power. There might be given sufficient authority, perhaps, that we might take into consideration the various districts of the United States in regulating that interest. In other words, we might find that in the East they were able to put in one rate of interest and in the West another, and under those conditions the thing to do would be not to make it all uniform, because in some parts of the country they get a little more money for their loans.

Mr. WILLIAMS. But that idea is not contained in this bill?

Mr. CROWLEY. No; it is not; but if you will read the entire Banking Act of 1935, it does give that power to the Federal Reserve Board.

Mr. WILLIAMS. Undoubtedly. I think there is no question but what the Federal Reserve Board has it.

Mr. CROWLEY. And it covers all insured banks in the new act that has been presented to you.

Mr. WILLIAMS. Do you mean by that that the provision with reference to the Federal Reserve Act will cover all insured banks?

Mr. CROWLEY. That is correct.

Mr. WILLIAMS. And that is on the theory that they will now have to come into the Federal Reserve System?

Mr. CROWLEY. That is correct.

Mr. WILLIAMS. But on the theory that we are going, perhaps, to have a lot of them insured that are not in the Federal Reserve System, what will we do about them?

Mr. CROWLEY. I think that it would be very helpful to the banking system if that were made a part of the permanent insurance act.

Mr. BIRDZELL. If you will turn to page 65 of your printed bill, H. R. 5357, you will find a provision there relating to interest. Shall I read it to you?

Mr. WILLIAMS. I think from what you have stated about it, it is not necessary to read it.

The point that I am asking about it is that there are some 8,500 banks of this country that are not in the System; and it is at least my view that they will not be in it, unless they want to be, and what will we do with them with reference to this interest charge?

Mr. BIRDZELL. Do you understand, Mr. Congressman, that this provision of the bill on page 65 that I have directed your attention to will enable the Federal Reserve Board to regulate the interest rate for that portion of those 8,500 banks that is insured?

Mr. WILLIAMS. I did not so understand it.

Mr. BIRDZELL. That is the provision of the bill.

Mr. WILLIAMS. Regardless of whether they are in the Federal Reserve System or not?

Mr. BIRDZELL. Yes, sir.

Mr. CROWLEY. As long as they are insured banks.

Mr. WILLIAMS. The point that naturally arises in my mind is, why should the Federal Reserve Board have that authority rather than the Insurance Corporation, if they are not members of the Federal Reserve System?

Mr. CROWLEY. It is only just a matter of uniformity; that is all.

You might have a situation where the Federal Reserve System would have one rate for national banks, and the Federal Deposit Insurance Corporation would have another one for State banks. That was the reason, I believe, for putting it all under the Federal Reserve Board.

However, our Corporation would welcome an opportunity to regulate the interest rates of the nonmember State banks.

Mr. WILLIAMS. Now, during the period of time since the banking holiday, there have been a great many concerted efforts on the part of your Corporation, the R. F. C., and others to recapitalize and rebuild the capital structure of the various banks throughout the country. I believe that we went into that to some extent the other day.

Mr. CROWLEY. Yes, Mr. Congressman.

Mr. WILLIAMS. And we reached the conclusion that perhaps half of them had been helped in that way.

Mr. CROWLEY. There have been pretty close to 6,000, and there are some to be done yet, so you won't be far out of the way in saying that close to 40 percent have been helped.

Mr. WILLIAMS. I would like to have in the record the figures showing the capital structure of those banks, say, as of March 1, 1933, about the beginning of the bank holiday, and as it exists at the present time.

Mr. FOX. It will not be possible to give it for March 1, 1933, for State nonmember banks. It will be possible to give the book capital for State nonmember banks as of the 1st of January 1934, virtually before most of the aid had been put into the banks. However, the book capital will not necessarily reveal what has been accomplished.

Mr. WILLIAMS. Unless we had the capital structure existing at the time these processes were begun, you could not tell what had been done in that connection.

Mr. CROWLEY. That is very difficult for this reason: Suppose that you had a million dollars in deposits or in assets; you could not determine the position that your capital structure was in just from the books of your bank, because perhaps you had not taken out your losses, and perhaps you had not set up any reserve for bonds or for depreciation, and you really cannot tell that without an examination, don't you see? In other words, we could not tell what condition the banks were in in March 1933 until first an examination was made of them.

Mr. WILLIAMS. I understand that, except that you could get it from the books themselves; the capital is there stated, by the books.

Mr. CROWLEY. Yes; but that would be misleading.

Mr. WILLIAMS. I understand that it may be, but I just wanted to know what that was as shown by the books; in other words, what was the capital of the banks of this country.

Mr. CROWLEY. I think the capital was about $6,000,000,000.

We could get that for June 30, and that would be satisfactory.

Mr. WILLIAMS. Yes. What is it now?

Mr. CROWLEY. About 6 billion dollars.

Mr. WILLIAMS. Do you mean by that that the capital structure of the banks of the country has not improved any during the last year and a half?

Mr. CROWLEY. Here is what happened: We might have had 6 billion dollars in March or June 1933, as far as their books were concerned. Now, then, they may have had a billion and a half of losses there that had not been deducted. When we came along with our rebuilding program, we eliminated the undesirable assets, and put capital back in.

Mr. WILLIAMS. But did you not also, in the case of a great many of the smaller banks, increase that capital?

Mr. CROWLEY. Yes; but we increased——

Mr. WILLIAMS. I mean not only increased the physical assets, but that you increased the book value? In other words, you raised the capital in many cases from $50,000 to $100,000?

Mr. BIRDZELL. Just word with respect to that.

It has been quite a general practice where preferred stock has been issued and sold to the Reconstruction Finance Corporation for a bank that issued and sold that prefererd stock to make a correponding reduction of its common stock, so that while the new capital has gone into the banks, the book capital remains substantially the same as it was before. That is the reason why the present book capital does not show much change from the book capital as it might have been shown before the rehabilitation took place.

Mr. WILLIAMS. Now, let us get at it from this angle. How much in public funds from the Reconstruction Finance Corporation, and how much in private funds have been put into the banks to rebuild and strengthen the capital structure during the last 18 months, or since the bank holiday?

Mr. FOX. Approximately 1 billion dollars has been put in by the Reconstruction Finance Corporation for recapitalizing the banks, and we are now estimating what the extent of the local funds that have been raised was, and while we have only gotten replies from 30 States, it already amounts to about $300,000,000 additional.

Mr. WILLIAMS. It will, perhaps, then amount to a billion and a half?

Mr. FOX. At least.

Mr. CROWLEY. I would say much in excess of that, Mr. Congressman. When you take into account your local contributions, reorganizations, and things like that, it will run far in excess of a billion and a half dollars.

Mr. WILLIAMS. In other words, the capital structure of the banking system of the entire country has been very materially and very substantially strengthened during the last 18 months?

Mr. CROWLEY. Pretty close to 50 percent of the banks, before we get through, will be practically rebuilt.

You asked whether we aided in the increasing of capital. Where we have rebuilt the capital structures of a great many of these banks, we have tried through the Reconstruction Finance Corporation and local contributions to build their capital so that they would have a ratio between deposits and capital which was larger than the ratio that they had before.

Mr. WILLIAMS. I was just going to ask you what has been your policy with reference to trying to create capital and establish a definite relationship between capital and deposits. I understood you to say that you had been making an effort to establish some kind of a ratio between the capital and the deposits of an institution. That has been your policy, has it?

Mr. CROWLEY. That has been our policy.

Mr. WILLIAMS. What is the ratio?

Mr. CROWLEY. Where a bank has been able to go all the way through, even though its ratio of capital to deposits might be less than 10 to 1, we have not disturbed it. Those were banks that had been able to carry themselves through, keep their capital intact, had a good earning capacity, and could build reserves and surplus. Where we rebuilt a bank we tried to rebuild on a 10-to-1 basis.

Mr. WILLIAMS. What I am trying to get is a general picture of the bank situation in this country now as compared with what it was during the 10 or 12 years preceding the bank holiday. When did we reach the highest peak in the number of banks in this country? I want to get what happened during that period.

Mr. CROWLEY. We reached it in 1920 or 1921.

Mr. WILLIAMS. What was it in numbers?

Mr. CROWLEY. About 30,000 banks.

Mr. WILLIAMS. At the present time there are how many?

Mr. CROWLEY. 15,000.

Mr. WILLIAMS. In other words, we have half as many banks now as we had in 1920—later than that, was it not?

Mr. Crowley. About 1920 when your failures started.

Mr. Fox. 1921, exactly.

Mr. Williams. Yes; 1921 and 1922. And at that time the bank deposits were about 50 billions?

Mr. Fox. Thirty-eight and a half billions in 1921.

Mr. Williams. When they were at their peak?

Mr. Fox. When the number of banks was at the peak the deposits were not at their peak.

Mr. Williams. The bank deposits were at their peak about 1928 and 1929?

Mr. Fox. 1930; 59.6 billions.

Mr. Williams. Now, during that period from 1922 to 1932 there was the failure of some 11,000 or 12,000 banks, was there not?

Mr. Crowley. That is right.

Mr. Williams. Of all kinds and characters, in all sections of the country, I take it?

Mr. Crowley. More of them, Mr. Congressman, in the Northwest. Your early failures first came, I think, in South Dakota, and then in northern Iowa—the whole Middle Western country.

Mr. Williams. There were, of course, a number of causes for that. Is it your opinion that we were overbanked; that we had entirely too many of them?

Mr. Crowley. Yes; we had too many banks, Mr. Congressman, that could not make a sufficient return on their investments or could not set up reserves to take care of their losses. In other words, a bank that has a $6,000 gross income, from which it must pay its overhead and set up its reserves for losses, it remains very difficult for it, if it has a $2,000 or $3,000 loss in any particular year, to take it currently.

Mr. Williams. That was one thing; that there were too many banks.

Mr. Crowley. And also later, from 1930 on, our banks suffered terribly by bond depreciation and defaults.

Mr. Williams. It was due to another reason, to the fact that they had invested their money in securities of different kinds at inflated values?

Mr. Crowley. That was a contributing factor to the banking trouble, and, of course, your economic situation.

Mr. Williams. Was it not due to the fact that there had been rather loose supervisions on the part of the authorities of the State and Government?

Mr. Crowley. You have in this country, under the State system, 48 different types of supervision. It is very difficult to have State supervision that will be as efficient as where it is a long way removed from local pressure.

Mr. Williams. And there were other contributing causes to the enormous number of failures that we had during that time?

Mr. Crowley. I think that the large contributing cause, Mr. Congressman, was your economic collapse. For instance, in the Middle West, when your banking trouble started in 1921, that was the beginning of your agricultural trouble. You can say that as your agricultural trouble became more severe, your bank failures increased very materially. Furthermore, they were frozen up in farm and chattel mortgages and also in bonds that had depreciated to a point where they could not sell them without taking a severe loss, and they had nothing to charge their losses to.

Mr. WILLIAMS. It is the hope and the intention now to eliminate a great deal of that, is it not? This very act itself tries to furnish a market for long-term rediscount paper?

Mr. CROWLEY. That is correct.

Mr. WILLIAMS. And to avoid that situation in the future, and also by having supervisory control, regulatory control over these various institutions by your examinations and your reports, it is the hope to eliminate many of the bad practices that have existed before, is it not?

Mr. CROWLEY. That is right.

Mr. WILLIAMS. And, of course, it is also the intention further to prevent the establishment of any more banks where they are not needed?

Mr. CROWLEY. That is correct.

Mr. WILLIAMS. And by means of all of those things, you hope to avoid the recurrence of this condition which has come upon us and caused so many failures among these banks in the past?

Mr. CROWLEY. That is correct.

Mr. WILLIAMS. Now, I want to get back to this question: What are you going to do, if this act is passed as written, with the 8,500 banks that are not members of the Federal Reserve System?

Mr. CROWLEY. You mean as to what we are going to do with them in 1937?

Mr. WILLIAMS. Yes.

Mr. CROWLEY. I hardly think that that is a fair question to ask me.

Mr. WILLIAMS. You do not think that that is fair?

Mr. CROWLEY. I do not mean that personally.

Mr. WILLIAMS. The fact is that this law would provide for that, would it not?

Mr. CROWLEY. This law provides for them to join the Federal Reserve System in 1937.

Mr. WILLIAMS. We have had a Federal Reserve System in effect for 20 years, have we not?

Mr. CROWLEY. Yes.

Mr. WILLIAMS. And we have now 8,500 banks in the country that have not seen fit to join it so far?

Mr. CROWLEY. That is correct.

Mr. WILLIAMS. I notice that the expression is used throughout this act, "insured banks", and I understand that you have a definition of an insured bank in your bill, but there is not any such thing as an insured bank now, is there?

Mr. CROWLEY. I assumed that all banks that are insured are insured banks.

Mr. WILLIAMS. They are simply members of a temporary fund.

Mr. CROWLEY. That is correct.

Mr. WILLIAMS. And there has not been a bank that has come in and bought stock?

Mr. CROWLEY. No, sir.

Mr. WILLIAMS. And insured under the permanent policy?

Mr. CROWLEY. No, sir.

Mr. WILLIAMS. Now, when July 1, 1937, comes and this law is enacted, all of these nonmember State institutions that are now in the temporary fund will have to come into the Federal Reserve System or get out of the insurance corporation?

Mr. CROWLEY. That is the law.

Mr. WILLIAMS. I am very much concerned myself about the 8,500 banks, because they are scattered from one end of the country to the other, especially in the southern part of the country, and the rural sections and small communities, and I, for one, have not reached the conclusion yet that there is not a place in our system for a local independent, unit bank. I do not believe that they ought to be required, if they do not see fit to do so, to come into the Federal Reserve System. You have means provided in this very act by which you could supervise them rather strictly, by which you can examine them, and you have a provision by which you can put them out of the System if they engage in any unfair or unsound banking practices of any kind or character, but it does seem to me that we ought not to place in this bill a provision requiring them against their wishes to come into the Federal Reserve System in order to get the benefit of the insurance feature.

Mr. GOLDSBOROUGH. Mr. Cavicchia.

Mr. CAVICCHIA. Pursuing the line of thought that Mr. Williams has been following, I would like to ask this: Why force these 8,500 banks into the Federal Reserve System if they do not wish to join? Is it not protection enough to the stockholders and to the depositors that they are members of the insurance funds?

Mr. CROWLEY. I think the thought is, Mr. Congressman, that it brings about a greater unification of banking, and perhaps better control of your monetary system, if you have them all in the Federal Reserve System.

Mr. CAVICCHIA. Will it cost these banks any more to become members of the Federal Reserve System than if they had stayed out?

Mr. CROWLEY. They will have to pay for their stock, but it will not be a great burden.

Mr. CAVICCHIA. To get back to the elimination of interest on demand deposits, many insurance companies, as well as municipal authorities, used to have large deposits on which they received throughout the East something like 2 percent on demand deposits. Has not the fact that this interest has been terminated forced these people to go into the bonding field raher than to have the money on deposit on which they receive no interest?

Mr. CROWLEY. Well, of course, that is purely a matter of their own judgment. If an insurance company has a million dollars of excess reserves and it can find a place to employ it, I presume that it is good business for them to do it.

On the other hand, you cannot expect a bank to pay 1 or 2 percent on daily balances when the money is only lying there idle.

Mr. CAVICCHIA. Has there not been a great deal of complaint on the part of municipal authorities because they have lost this 2 percent on demand deposits?

Mr. CROWLEY. I think that that is correct, that there has been complaint, but I do not think it is justifiable. I mean by that that they might just as well wish for 4 percent as to wish for 2 percent when the banks cannot pay out the 2 percent. There is no rime or reason why I should, if I were in the banking business, take a $100,000 account from you and pay you 2 percent for it, and then leave it in the vaults or in the Federal Reserve banks and not employ it.

Mr. CAVICCHIA. That is true, because of the conditions existing now, but if a time should come when the banks can employ money to advantage and get good returns for it, if you pass this law they will not be able to pay any interest, because the law forbids it.

Mr. CROWLEY. Mr. Congressman, that is not in this law. That law was passed in 1933.

Mr. CAVICCHIA. But the fact is that we have that law.

Mr. CROWLEY. That is right.

Mr. BIRDZELL. One further suggestion there, Mr. Congressman.

In the Banking Act of 1933, which forbids the payment of interest on demand deposits, exception is made where, under local law, State laws, interest is required to be paid on public deposits.

Mr. CAVICCHIA. Now, to go back to that 29 cents per $100 that has been saved through the law of 1933, does this 29 cents per $100 that the banks have saved in interest cover their costs of going into the temporary insurance fund?

Mr. CROWLEY. It would more than cover their costs on one-twelfth of 1 percent.

Mr. CAVICCHIA. In other words, the banks do not have to meet an unreasonable demand to join in your fund, inasmuch as they have saved 26 or 27 cents on every $100?

Mr. CROWLEY. I do not think that we have presented anything in which offers any great obstacle to the banking system of the country.

Mr. CAVICCHIA. You mean, so far as the extra cost is involved?

Mr. CROWLEY. That is correct.

Mr. CAVICCHIA. That is all.

Mr. GOLDSBOROUGH. Mr. Reilly, you were not here yesterday.

Mr. REILLY. I do not have any questions.

Mr. GOLDSBOROUGH. Mr. Cross.

Mr. CROSS. Now, Mr. Crowley, going back to the questions put to you by Mr. Williams, you said that the bank crash was started in the Western States. That was caused by falling prices of the commodities of the people who did business with those banks, was it not, and that caused falling prices in lands, did it not, and that reflected finally on the eastern sections and caused a decline in the prices of stocks, and that destroyed the purchasing power of the country and brought on your bank crash?

Mr. CROWLEY. I think that is correct.

Mr. CROSS. Now, under title II you say that you can get a sound banking situation, that tile II seems to be the key to the situation. The question is to keep up your prices, and in order to control prices that you should have a unified banking system. In other words, if you have a whole bunch of banks that are uncontrolled in the credits that they handle, if there are too many of them, they affect the whole structure, and if they do not come into the system where they can be regulated as to their credits, it directly affects price levels. Do you see the point?

Mr. CROWLEY. I agree with you that your bank failures were largely due to your economic collapse starting back in 1921.

Mr. CROSS. Surely.

Mr. Crowley. However, there were other factors such as overbanking conditions, poor judgment, or not being able to foresee that land values were too high, and things like that.

Mr. Cross. Was not the overbanking situation brought about by inflated credit, by abnormally high prices at that time of lands and the things that securities were braced on, and the banks figured that they could all make money, and everybody was taken into the banking business?

Mr Crowley. I think that is right.

Mr. Cross. And, of course, when the crash came, prices went down, securities went down, and they were all blown up.

In reference to the question of paying interest on checking or cash deposits, you remember that we had that question up, as you say, in 1933.

Mr. Crowley. Yes.

Mr. Cross. And the fellows that had big checking deposits the banks got competing for, and they were paying too much interest on them, and the mass of the little fellows knew nothing about that, and, in addition, the big fellows also knew what condition the banks were in, and they pulled their money out, but the little fellow got caught.

In other words, there was a vicious system brought about by the banks bidding on the checking deposits of the big fellows.

Mr. Crowley. That is correct.

Let me say one thing here, so that you will understand my viewpoint on the banking system. I think that the Federal Deposit Insurance Corporation must have these powers that we are talking about, but I do not want to go on record as saying that the entire State system should be eliminated. I think that your State system can be a very major factor in your banking system.

There are two types of banks in this country. You have your larger banks, which by the very nature of their type of business cannot afford to make the type of loans that are made in the small community, because it costs them too much money.

Your community bank does contribute to your local community a type of credit that I think is very essential in your whole financial picture, and I do not believe that it is necessary for us to eliminate in a wholesale way that type of bank. I think the think that we should be very careful about is that we do not get back to that overbanked condition, but we should do everything we possibly can to try to preserve the banks that we have now, as long as they have an opportunity of serving the people of those communities.

In other words, let us take a bank of $250,000 or $500,000 in deposits. To my mind, they can be a large factor in the local community and lend a larger percentage of their money locally in the future than they have in the past if they will only profit by their experience in the past in making those loans so that on maturity they will be reduced from time to time and not be permitted to become frozen.

Mr. Cross. Of course, those banks would not belong to the Federal Reserve System, and the danger of that seems to be that the Federal Reserve Board, not being able to control their credits or the landings of those banks, could not bring about the situation which you say is desirable.

Could this deposit insurance feature here be so administered so that at least your Corporation would have something to say about their credit activities?

Mr. CROWLEY. I think that as long as you have the State system, Mr. Cross, that the State authorities must have the primary responsibility for the supervision. Now, the only place where I see that we are entitled to supervise is where that supervision is necessary for the protection of our Corporation.

I do not like to get into the matter of the Federal Reserve, because I think that is a matter for Mr. Eccles, and I much prefer not to go into anything that would interfere with his end of this bill, if you have no objection to it.

Mr. CROSS. Yes; I understand.

That is all.

Mr. GOLDSBOROUGH. Mr. Gifford.

Mr. GIFFORD. I want to pursue the line of inquiry with reference to the part of this bill that deals with the examination of banks.

I wish I had with me letters that I have received, with respect to the fact that the Comptroller was out making speeches all over the country, calling on the banks to loosen up on their credit, whereas before that we found that the examining department of the Comptroller's office had put a great deal of fear into the bankers, so that they did not dare to loan.

The whole tenor of this bill is to get a pretty good grip on these banks by examination, and this assessment of one-twelfth of 1 percent would be sufficient so that you could control the conduct of the banks, and you want to force them to carry burglary insurance and other insurances, and, if they do not carry them, you order them and charge them up to the bank.

Now, as I read this bill, and after having heard your statement, you base a great deal of your possible success on your opportunity to make examinations just as often as you like, so that you may make the banks conform to anything that you may want them to do, and that sort of thing. Is not that asking a good deal?

Mr. CROWLEY. No; I do not think that there is a single thing in our bill that goes too far.

Let me say this to you, that, in the first place, the law that was passed said that we may take these banks in on a test of solvency. Now, we all know that a bank that only has sufficient assets to meet its deposit liability on any kind of a forced liquidation could not pay out its deposits. Furthermore, our whole trend of banking in this country is based on the theory that first the stockholder shall have an equity in this bank, because it is a capitalistic system. So that when we started in January 1934 after taking these 7,800 banks in, we were faced with the problem of going out to determine their position.

Now, our job, first, was to find out really what the condition was, and in order to find out what the condition was, we had to try to determine the value of their assets, and we were trying to do that, of course, at a time when values were at perhaps a very low ebb, and perhaps it was necessary sometimes to be pretty severe, but my own judgment is that when we classify an asset, a good asset in the bad column, that we perhaps classified as many bad assets in the good column.

Mr. GIFFORD. Do you understand that recently there has been a tremendous change in attitude on the part of bank examiners in the whole country, and instructions must have been given to them to have a different viewpoint?

Mr. CROWLEY. As far as Federal Deposit Insurance is concerned, there has been no change in the attitude of our examiners, because our whole program has been based upon, first, putting the banks in a sound position as far as capital is concerned. After you once get the banks in a sound capital position, then you may not have to use as severe a yardstick in a wholesale way as you had to at first.

Mr. GIFFORD. I am not criticizing your method of examination, but national bank examinations in the last 2 or 3 years. Do you not know that there has been a very great change in the method of making bank examinations lately, where slow loans in a bank have not been persecuted as formerly?

Mr. CROWLEY. I do not know what the policy of the Comptroller's Office is.

Mr. GIFFORD. Did you not see an article in the newspapers, to the effect that the President himself had severely criticized the strictness of bank examinations?

Mr. CROWLEY. Let me say this to you on the matter of the criticism of slow loans. You may criticize a slow loan if the bank has too large a percentage of them, or if the bank is badly frozen. The easing up of the criticism of slow loans has been due largely to the fact——

Mr. GIFFORD. That is all I asked, and you agree.

Mr. CROWLEY. Wait a minute—if it has been done.

Mr. GIFFORD. Has it been done?

Mr. CROWLEY. I presume it has, at least in places where the banks have such extreme liquidity that there is no necessity of forcing liquidation.

Mr. GIFFORD. Do you think that you could still hold these banks as members of your corporation if they are subjected to all of these things?

Mr. CROWLEY. We have had in here 22 State commissioners for conferences on the matter of examinations and related topics.

Let me say that in the matter of rebuilding capital, in the matter of local contributions, time after time we have had a State commissioner come to us and ask us to exert our influence, because on account of local conditions he could not do it, and he has asked the Federal Deposit Insurance Corporation to exert pressure in order to put that bank back in shape.

So far as that examining program is concerned, every State commissioner who wants a good State banking system will agree that if we are going to carry such a high percentage of liability we have to have ways and means of protecting ourselves.

Let me say this to you: That in the large percentage of the State banks we are insuring them better than 70 percent. I think that there are some 9,600 that we are insuring up to 80 percent. That is a tremendous responsibility.

Now, on the matter of burglary insurance, the reason we asked for that is that a good many of the States have no legislation at all that gives the Commissioner the power to force a bank to carry a reasonable amount of insurance on its officers or employees. Already, out of the 11 banks where we have paid out, we have had a very unfortunate experience. If they had had some adequate insurance, it would have helped the stockholders very materially.

We do not propose, you understand, to do that in the case of a wholesale majority and put an unnecessary burden on those banks. We must be reasonable in all of our demands.

Mr. GIFFORD. I am wondering what the cost of those things will be to the bank and what you insure them against?

Mr. CROWLEY. We certainly do not want to pay for all of their mistakes without having any right to try to get them to correct them.

Mr. GIFFORD. Do you want them to insure themselves against every conceivable thing, so that your corporation will not have any liability?

Mr. CROWLEY. No; but where they have not sufficient burglary insurance and protection and sufficient surety coverage on their employees, I see no reason why they should not carry it as a matter of protection to themselves and their own stockholders.

Mr. GIFFORD. Do you think that it is a fair treatment, and do you think that it is a safe treatment of a bank to demand of it a certain kind of report, and if it does not publish it in 5 days, to fine them $100 a day?

Mr. CROWLEY. I think that you are exaggerating that a little bit. The purpose of the authority to publish reports is this, that a great many of your bank statements in the past did not really show the true conditions of the banks.

Mr. GIFFORD. Whose fault was that?

Mr. CROWLEY. I think it was the fault of the entire system.

Mr. GIFFORD. Do you mean to say that our present national bank system is not sufficient to show the true condition of the banks?

Mr. CROWLEY. You take the old condensed statements gotten out by national banks and State banks for years; they did not show the market value of their bonds or the reasonable value of their loans.

Mr. GIFFORD. Did not they show the last demand of the bank examiner in connection with the market value of those things?

Mr. CROWLEY. Oh, no; that has never been in a statement.

Let me say this to you. I think that you are starting out on a different basis now. We are starting out anew, with the banking system practically rebuilt and values way down.

Mr. GIFFORD. Do you not see that you are adding considerably to the present burden of the banks by way of these examinations, and, secondly, that these examinations may be so irritating that many banks would rather not belong?

Mr. CROWLEY. No. The great majority of the banks give to our examiners every kind of cooperation, and do not seem to be irritable because we are trying to get a true picture of their institutions.

Mr. GIFFORD. Then your answer would be that they would not object to these things?

Mr. CROWLEY. A certain percentage, yes, would object, but I do not believe that that is the answer. Our corporation was set up for the protection of depositors, not for the protection of the bankers. We are trying to cut the losses to the depositors and of this corporation down to a minimum, and that is what our job it.

Mr. GIFFORD. And, in order to protect the depositors, you want to get control of the banks?

Mr. CROWLEY. You can call it control or what you please, but we are insuring 80 percent of the deposits in 9,600 banks in this country, and we have to do whatever is necessary to cut down their losses, within reason, of course.

Mr. GIFFORD. My question is really friendly. I am simply asking you if these irritating things that you are asking for are not lessening the number of banks that might belong.

Mr. CROWLEY. I do not think so.

Mr. GIFFORD. Are your examiners under civil service?

Mr. CROWLEY. No; they are not.

Mr. GIFFORD. Are the national-bank examiners under civil service?

Mr. CROWLEY. There are no bank examiners under civil service.

Mr. GIFFORD. Do you train them so that they all use about the same methods, or do you tell them that they must not follow any fixed rule but use their own judgment in the case of, say, a bank that has too many slow loans in proportion to the assets?

Mr. CROWLEY. Let me say this to you, that bank examiners are like any other human beings. Some are good, and some are bad; and, as far as their classification is concerned, you understand that after they make their classification, it is reviewed again in supervising office by a reviewing committee, and even the reviewing committee may make a mistake.

Like any other persons who get some authority, there is always a certain percentage of them that become autocratic, but we try to be as sympathetic as we can.

Mr. GIFFORD. The Comptroller wrote me a letter stating that he had had but one or two cases where a bank had been dissatisfied with the examinations, and where it had asked for a reexamination. I wonder if that is because the officials of that bank wanted so badly to get rid of the examiner that they did not want to see him again?

Mr. CROWLEY. I do not know about that.

Mr. GIFFORD. Do you not think that when an examiner walks into a bank, it is a very irritating thing to the officials of that bank?

Mr. CROWLEY. No; I do not agree with you there. I think that the average examiner during this entire depression has certainly been very helpful to the bankers. However, as I say, there are exceptions to all rules.

Mr. BIRDZELL. May I add one word in reference to examinations? The Corporation is working on a program in which it has solicited the cooperation of the banking departments in all of the States on the matter of examinations for the very purpose of making the examinations a matter of as little burden to the banks as possible.

The program that we are working on contemplates that where a State law might require two examinations of a bank a year, that the banking commissioner would be authorized to accept the report our examination in lieu of one he might make himself, and also that provision be made so that the Corporation might receive the reports of examinations made by examiners of the State administration.

Mr. GIFFORD. You think that any more than two examinations a year would be irritating?

Mr. Birdzell. We would have two wherever the State law requires two.

Mr. Gifford. But you think that any more than two would really be an irritation?

Mr. Birdzell. I would think so.

Mr. Crowley. I think it would be unnecessary except in some unusual conditions.

Mr. Birdzell. I might say that that suggestion is being very favorably received in the various States.

Mr. Gifford. But you are asking us here for permission to make examinations just as often as you want to.

Mr. Crowley. If you restrict us as to how many times we can go in, there might be a condition where, in order to protect ourselves, we might have to go in at some other time. We might find a bank in a bad condition this morning that we were in last week, and we want to be able to go back and correct that. That is the reason why we cannot limit it.

Mr. Kopplemann. In the light of what Mr. Gifford has been questioning you about, perhaps it would be in order to ask Mr. Crowley——

Mr. Goldsborough. Mr. Koppelmann, we are attempting to take the Members in regular order.

Mr. Kopplemann. I beg your pardon.

Mr. Goldsborough. Mr. Spence.

Mr. Spence. When the banks joined the temporary fund, you levied an assessment of one-fourth of 1 percent on the insured deposits, did you not?

Mr. Crowley. That is corect.

Mr. Spence. And now the one-twelfth of 1 percent will be levied on the entire deposit liability?

Mr. Crowley. That is correct.

Mr. Spence. What will be the difference in the amount realized from the one-fourth of 1 percent on the insured deposits and one-twelfth of 1 percent on the entire deposit liability?

Mr. Crowley. We received about 38 or 39 million dollars under the one-fourth of 1 percent, and we will receive about 30 million dollars under the one-twelfth of 1 percent; but you understand, Mr Spence, that we could only call, during the temporary period, for an additional one-fourth, whereas one-twelfth is an annual premium payable each year, which must be charged to the bank's overhead.

Mr. Spence. You did levy the full assessment?

Mr. Crowley. No; only one-half of it. We never levied the other one-half.

Mr. Spence. What percent of the amount of deposits is now insured?

Mr. Crowley. Forty-four percent in all, but I think that we ought to read to you the insurance figures by size groupings, because that is very necessary for you to get the picture.

Mr. Fox. According to the total liability size groupings, banks with $100,000 or less in total deposits, of which there are 1,500 now insured, are insured up to 92 percent of their total deposits.

Banks in the next size grouping, from $100,000 to $250,000, of which there are approximately 3,600, are insured up to 87 percent of their total deposits.

Banks in the next size group, $250,000 to $500,000, of which there are approximately 3,100, are insured up to 83 percent of their total deposits.

In the next size grouping, $500,000 to $750,000, of which there are approximately 1,500 banks, they are insured up to 80 percent.

From $750,000 to $1,000,000, of which there are 950, they are insured up to 78 percent.

From $1,000,000 to $2,000,000, of which there are 1,600, they are insured up to 75 percent.

From $2,000,000 to $5,000,000, of which there are about 1,100, they are insured up to 70 percent of their total deposits.

From $5,000,000 to $15,000,000, of which there are only 630, they are insured up to 50 percent of their total deposits.

$50,000,000 or over, there are about 100, and all of those banks are insured about 26 percent.

Mr. BIRDZELL. For the record, where Mr. Fox said up to a certain percentage, the average is meant.

Mr. SPENCE. Since 1921, according to this statement, including 1934, there have been 2,548 national banks suspended and 11,004 State banks suspended.

What percentage of the national banks were suspended, and what percentage of the State banks?

Mr. CROWLEY. Of course, as you go down your ratio, your percentage always changes.

Mr. SPENCE. Was a great number of the State bank failures caused by insufficient supervision or because of the inherent weakness of the bank?

Mr. CROWLEY. I would say it was undoubtedly both.

Mr. SPENCE. In other words, there are a good many small communities where they have two or three banks and where they only need one. Is not that true of the State banks?

Mr. CROWLEY. That is right.

Mr. SPENCE. Did that not to a large extent cause the failure of those banks more than insufficient supervision?

Mr. CROWLEY. In a great many of your States, Mr. Spence, the State supervisors did not examine their banks with any great regularity. I have known of some States that did not examine some banks for 2 years, and possibly sometimes a little longer, and then a great many of the State laws did not give the supervisors perhaps sufficient authority over their banks, and in a great many instances, on the matter of licensing new banks, the Commissioner would decline a charter and perhaps then they would go to some board and the board would override the Commissioner and grant the charter in a community such as you are talking about.

Mr. SPENCE. I have received some letters from some of the smaller bankers, in State banks, and they say that they now see no advantage in becoming members of the Federal Reserve System.

What is your opinion about that, outside of belonging to the insurance fund?

Mr. CROWLEY. I think this, that if your Federal Reserve System is liberalized to the point that farm mortgages may be discountable, certainly there is going to be an advantage to bank in availing itself of that opportunity. In other words, in the matter of seasonal borrowings, or where they perhaps have a temporary sloughing off of deposits, there is an advantage to a bank in having some place where they may rediscount their long-term loans.

Mr. SPENCE. Do you think that that will overcome any of the other disadvantages that might accrue to them by reason of being a member?

Mr. CROWLEY. Mr. Spence, I do not like to get into a discussion on the Federal Reserve provisions at this time. Mr. Eccles is coming and he will present his information, and I am sure that we will all be together on it.

Mr. SPENCE. Did you give us the percentage of deposits in the insured banks?

Mr. CROWLEY. We just read it to you.

Mr. SPENCE. In numbers?

Mr. CROWLEY. On your bank closings? Do you mean the depositors?

Mr. SPENCE. Yes.

Mr. CROWLEY. It is over 98 percent. Almost 99 percent of all of the depositors in the country, including all the banks, are insured up to $5,000. In other words, their balances are under $5,000.

If you were to take all public funds out of your smaller banks where they are insured 95 percent, I think you would find perhaps only one account in such a bank that was more than $5,000.

Mr. SPENCE. You think there is a justification for including all of the deposit liability of the bank within the scope of this program?

Mr. CROWLEY. Yes; for this reason, that I think that the responsibility of the Federal Deposit Insurance Corporation and their contribution, as I said many times here, cannot be the paying out of that loss. People generally have lost confidence in the banking system on account of the severe losses that they have had during the last 12 years, and while the Federal Deposit Insurance Corporation has had a psychological effect in the way of restoring confidence, we must not do anything that is going to destroy that confidence in the Corporation. Otherwise you are again going to have losses and withdrawals from your financial institutions.

I think that Federal Deposit Insurance is the only vehicle in the banking system that can help to correct this, and I think that it is a long-term proposition over a period of a great many years, and that the banks generally can well afford to make their contribution to it for the benefit of the entire banking system. I do not think that it is unreasonable in any degree.

Mr. SPENCE. It not only insures the $5,000 liability, but it has an effect upon all of the depositors in the banks?

Mr. CROWLEY. That is right.

Mr. SPENCE. Just one other question. On page 12 of your bill, in reference to new banks, it says:

> Notwithstanding any other provision of law, its franchise, property, and income shall be exempt from all taxation now and hereafter imposed by the United tSates, or by any Territory, dependency, or possession thereof—

and so forth.

That would exempt a bank building.

Mr. CROWLEY. No. That is where you set up a Federal deposit bank during the time that the local stockholders are raising money in your own community. Just as soon as the local stockholders come in and take things over, then it becomes regular, taxable money.

Mr. BIRDZELL. The term "new bank" is defined in the first section of the act, and it is confined only to a new national bank set-up.

Mr. SPENCE. You do not contemplate that that bank will lend money on real estate? Is that your idea?

Mr. CROWLEY. It should not during our term of office. We would not buy any real estate. Ours is really a bank that carries on during the interim in a community where they need banking facilities until the local people can take its place.

Mr. BIRDZELL. It can make no investments except in Government bonds.

Mr. SPENCE. That is all.

Mr. GOLDSBOROUGH. Mr. Wolcott.

Mr. WOLCOTT. I notice that the proportion of the losses of banks other than national banks seems to be materially less than the proportion of losses of national banks. Could that be due to the fact that there are so many small units in State banks?

Mr. CROWLEY. You mean in the State system?

Mr. WOLCOTT. Yes.

Mr. CROWLEY. Yes. You take your number of failures, they are largely in your small State system.

We have an analysis of that, if you would like to see it.

Mr. WOLCOTT. As I understood you, the trust deposits were divided so that the trust company having deposits in a bank could have insured up to $5,000 each of their accounts as they carried them on their books.

Mr. BIRDZELL. If the trust company were a member of the Insurance Corporation?

Mr. WOLCOTT. Yes.

Mr. BIRDZELL. Yes.

Mr. WOLCOTT. With respect to public money, where a county or municipality determines on a particular bank as a depositary for its funds, that is usually kept in a lump-sum deposit?

Mr. BIRDZELL. Yes.

Mr. WOLCOTT. However, on their own books, they carry it as grades, highways, sewers, contingent, and so forth.

Would the municipality have this fund guaranteed as a lump sum, or would it be guaranteed according to the manner in which it was carried on the books?

Mr. BIRDZELL. According to the manner they are owned.

For instance, if a city carries its deposit in a bank, and it places its funds divided, we will say, for general fund purposes or for some specific purpose for which funds may be appropriated, so that it keeps its books separately, so that it can keep account of deposits withdrawn or deposited for particular purposes, nevertheless those are city funds and they must be combined for the purpose of insurance; but, on the other hand, school funds may be deposited by the same treasurer as deposits of city funds, and yet the schools, being a separate corporate entity, would separately own whatever funds were deposited and the school corporation could make a separate claim.

Mr. WOLCOTT. Let us take, as an example, a county where they have a general fund, and then they have a drainage fund, and they have a highway fund and a school fund, and then a fund into which go the collections made by the county treasury for the benefit of the townships, where the county treasurer acts on the matter of delinquent taxes as the agent of the township, your criterion is as to whether these funds are held to the credit of the distinct political subdivision and political entities of that county?

Mr. BIRDZELL. Yes. It may be different in the case of your drainage funds that you speak of, or your——

Mr. WOLCOTT. Irrigation district?

Mr. BIRDZELL. Irrigation district, or something of that sort, where that is a special-assessment district and as such would be the proceeds of special assessments levied. The same may be true of your highways. In that case the drainage district or the highway district would be considered a separate political entity.

Mr. WOLCOTT. Then, in order to get the full advantage of this insurance, the municipal corporation or the State legislature should provide that the school district and the drainage district or irrigation district, sidewalk district, or highway district should be considered to all intents and purposes a political entity of the county?

Mr. BIRDZELL. It would depend on whether or not they are in fact so. If they are, they are getting the benefit of insurance now.

Mr. WOLCOTT. The average county or municipality makes a separate levy for school purposes. They make a separate levy for highway purposes and for all of these different purposes, and carry them separately on their tax rolls.

Do you think that under that system they should be entities to the extent that each of these funds would be insured up to $5,000?

Mr. BIRDZELL. It depends upon whether the proceeds of the city tax for school purposes belongs to the city, or whether they have a separate corporate organization. If it be a separate organization, and the tax was intended for that corporation, then that corporation would own the deposits.

Mr. WOLCOTT. Of course, there is a great deal of overlapping there in their prerogatives, and the municipality or city or county always exercises a certain supervisory duty with respect to all of these other entities, and while perhaps specifically these funds belong to the district, at the same time they belong to the county and the county is made responsible for them.

Mr. BIRDZELL. The county might be merely the agent for collecting the funds. That is true in many instances, and it might be that they would employ one common treasurer who would have the control of the deposits, but nevertheless the funds, when they go on deposit, are certainly going on deposit to the credit of the particular municipality that is authorized to expend them. That being the case, they would belong to that municipality, and that municipality would be getting the benefit of the insurance.

Mr. WOLCOTT. The criterion seems to be whether any part of this fund which is deposited by the county or city treasurer is intended to have been deposited in connection with the credit which he gives that entity on his own books?

Mr. BIRDZELL. Yes; that is correct. We have even gone to the extent in some cases of giving assurance that sinking funds actually belong under the peculiar law that they be rated under to the holders of the bonds rather than to the municipality. There is one instance that we have come across where the ownership of the sinking funds is so definitely fixed by the State law under which they are collected that it can be said definitely that they belong to the owners of the bonds rather than to the municipality. It is a question of ownership in the last analysis.

Mr. WOLCOTT. Carrying out that same thought a little further, when the banks in Michigan closed an endeavor was made to interpret the law in such a manner that the funds of correspondent banks would be preferred. We found that under certain rulings of the State courts and of the United States Supreme Court, as I recall, they had no preferred status.

Mr. BIRDZELL. That is right.

Mr. WOLCOTT. Under the present law, or under these changes as contemplated, a small bank having deposits with a larger bank would only have $5,000 of its deposits insured?

Mr. BIRDZELL. Yes; that is correct.

Mr. CROWLEY. Do you mean $5,000 of public funds?

Mr. WOLCOTT. No. I mean a small bank in a city, we will say, of 30,000 or 35,000 in close proximity to a large city where there are large banks, and frequently, to safeguard their funds, they have amounts deposited with the larger banks. In my own case, if I may use it, we are located about 60 miles from Detroit. When the crash came, we found that our banks in Port Huron had deposited their reserves and the money that they were not using daily in the large banks in Detroit, so when the large banks in Detroit closed, all of the ready cash that our banks had to do business was what they needed to carry on their daily business, and their reserves were tied up. We found instances where some of our banks had their reserves in the Chicago banks, and I know of one instance where the cashier of the bank went to Chicago and drew out $80,000 of reserves and came back with them in his inside pocket.

Of course, that precipitated the national bank closing; no question about it, and I wonder if it would be feasible to provide for the isolation of those funds in some manner so that it would prevent the recurrence of a situation such as we had in Michigan, where one or two large banks are closed by arbitrary authority, and where it would not necessarily compel the closing of 500 other banks.

Mr. CROWLEY. We went into the matter of the entire bank deposits, and it is my honest judgment that that should not be touched until we have had an opportunity to study that thing a little further. There is a lot to what you have said, but we have only had 1 year's experience here, and perhaps next year from our experience we can make a recommendation to you that may correct that difficulty. It does increase our liabilities, as you know, tremendously, if we take on the entire bank deposits.

Now, on the question of public funds, Mr. Wolcott, there has been perhaps more damage done by banks taking on too large a percentage of public funds. In your average size bank your large account can give us more trouble than where you have a diversification of deposits, where your withdrawals are more or less uniform. If you had, for instance, a bank of $250,000, and you have one account of $750,000, you have really got to carry excessive reserves to take care of that large account, because you do not know when it will go out on you.

So there is a lot of danger in banks taking too large a percentage of their deposits in large accounts, which accounts will always cause you trouble unless you have your investment in conformity with the size of your accounts.

Mr. WOLCOTT. I brought that out merely because I wanted to know whether, in the future, we could work out some plan so that these fellows would not be isolated by the closing of a bank in one case, which is always the case in connection with a branch-bank system, but should not be the case with our present system, where it affects 40 or 50 others in that locality.

Mr. CROWLEY. That is a matter that we have already given quite a lot of thought to, and it should be studied for another year, I think.

Mr. WOLCOTT. When a corporation terminates its connection with the Federal Deposit Insurance Corporation, there is a provision in section 1 (5) on page 13 of your print that provides that the corporation may publish notice of such termination and the bank, meaning the assured institution, I assume, shall give notice of termination to its depositors in such manner and at such time as the board of directors may find necessary.

Of course, it is my thought in that particular that whenever a bank withdraws from the fund, they are not going to rush out and advertise the fact, and I wonder if we should not make this notice mandatory, or specifically provide in this act the manner of the notice and the time for giving notice by the bank which was withdrawing, rather than to leave it to the board of directors of these banks as to whether or not they will give any effective notice.

Mr. BIRDZELL. You understand that the " board of directors " there means our own Corporation, not the board of directors of the bank?

Mr. WOLCOTT. Possibly that clarifies that whole situation.

Mr. CROWLEY. Here is the reason why. On the matter of notifying depositors, we might have a bank, Mr. Wolcott, that we were having considerable trouble with, and that we were going to expel from the fund. We would notify the State supervisor, who would notify the bank of the particular difficulty. What we want to do is to stop the bank from doing anything that may affect an innocent depositor, because there are banks that are perfectly willing to stay in here during this recovery program and which, after confidence has been restored and we get on a normal condition again, will perhaps want to get out because they do not want to have any part in the whole banking system.

Mr. WOLCOTT. I think that perhaps my objection to that language is answered by section 10 of your definition, which says:

> The term "board of directors" means the board of directors of the Corporation.

One more question, please. In the Federal Reserve Act, there is a provision that national banks may loan on real estate up to 75 percent of the value. I wonder whether that does not affect some of the effectiveness of the Federal Deposit Insurance Corporation?

Mr. CROWLEY. In the Federal Reserve provision, Mr. Wolcott, there is a provision that those mortgages shall be eligible for rediscount, which, of course, puts a little different complexion on it.

Mr. WOLCOTT. You think that that clause is adequate protection so far as your fund is concerned? I know that that is out of your scope.

Mr. CROWLEY. It is out of my scope a little bit, and I think that the Comptroller should talk on his national banks. There is no question but what in the past, in your State systems, where they were permitted to take mortgages, and where you had your shrinkage of values, it affected their conditions materially.

Mr. Wolcott. I understand that back in 1923 they amended the National Banking Act to increase the amount that a national bank could hold on real estate from 25 percent to 50 percent. Now there is a school of thought which lays all of our industrial ills on the doorstep of that policy which allowed the banks to invest so heavily in real estate that they created a condition of insolvency on the real-estate market, and I wonder if we are not just contributing to the recurrence of a bank crash by increasing this still further from 50 percent to 75 percent, and, if so, of course we all are vitally interested in whether or not the Federal Deposit Insurance Corporation would be in a position to meet such prices brought on by a slump in the real-estate market.

Mr. Crowley. I think there is a lot to what you say, and it all depends, in my mind, as to what provisions you make in the Federal Reserve Act for it. If they cannot rediscount those, there is a great danger of a bank being frozen.

Mr. Brown of Michigan. Even if they did rediscount those mortgages, the primary loaning bank would still be responsible to the Federal Reserve bank.

Mr. Crowley. Oh, yes; it would be bills payable.

Mr. Brown of Michigan. I do not see that that would clear up the situation that he is discussing.

Mr. Crowley. Here is what it would do: It would just place a long-term loan in a position that they might borrow on it the same as on their eligible paper. It does not place the same stigma against a long-term loan if it is eligible for rediscount that it would have if it were not eligible.

Mr. Wolcott. Here is another point in respect to that same question. There is no restriction made upon the funds which might be used for investment in real estate at 75 percent of its value, and they might take long-term real-estate paper and invest commercial funds in it, and your commercial deposits are guaranteed under the fund.

Mr. Crowley. I think it does this: It means that they have to pay off each year, reducing the principal, and that is the limit to the amount of funds that they may employ in the mortgage field.

Mr. Wolcott. Yes; but we allow them to take 20-year commercial paper up to 75 percent of the value of the real estate.

Mr. Crowley. Yes; but it must be amortized.

Mr. Wolcott. Nevertheless, it is a long-term investment.

Mr. Crowley. There is no question that it puts it in the same position as a bond.

Mr. Brown of Michigan. I am a little bit disturbed about what might be a duplication, or even a triplication, of the duties performed by your corporation, the Comptroller's office, and the Federal Reserve Board.

Now, in your very clear statement which you gave to us on the first day, and of which we all have copies, you said on page 26—

> In the future the Corporation should devote a large part of its efforts to the maintenance of sound conditions among the insured institutions.

Now, it seems to me that that clearly defines just what the duty of the Comptroller of the Currency now is. Am I right about that, or wrong?

Mr. CROWLEY. Do you mean in the case of a national bank?

Mr. BROWN of Michigan. Yes.

Mr. CROWLEY. The only authority that we have, Mr. Brown, over a national bank or a State member bank is that we have the power to put them out of the fund just the same as a State bank, after notifying the Comptroller and the Federal Reserve Board, just as we notify the State supervisor.

Mr. BROWN of Michigan. I think that your power is greater than that. You not only have the power to put them out of the fund, but upon your determination that they should be out of the fund, the statute is mandatory that both a member of the Federal Reserve System and a national bank shall then be suspended. Is not that true?

Mr. BIRDZELL. That would be correct.

Mr. BROWN of Michigan. If you once determined that a bank cannot remain a member of your fund, then the Federal Reserve Board must suspend that bank and the Comptroller must appoint you as receiver.

Mr. BIRDZELL. No; the Federal Reserve Board must see that the bank is no longer in the Federal Reserve System, and in the case of a national bank, of course it would result in liquidation.

Mr. CROWLEY. You understand, the Federal Reserve Board has no authority to appoint a receiver for a State member bank.

Mr. BROWN of Michigan. I understand that. It will appoint your Corporation, or, if you do not care to take it, some other suitable person as receiver.

In other words, in the power that you have asked, you will have absolute authority in your board of directors to suspend any bank in the United States if it is a member of your Corporation.

Mr. CROWLEY. I do not think that there is any duplication there. I think that we are the only ones that have that power.

Mr. BROWN of Michigan. Of course, the national bank department has that power with respect to national banks.

Mr. CROWLEY. There is no particular reason why we should not have the same control of putting a bank out of the fund, be it a Federal Reserve member bank or a State bank, if they are not conducting themselves in a manner that is going to give to this Corporation the usual safeguards.

Mr. BROWN of Michigan. Well, I think that is true, but I am saying that that gives you the same power that the Comptroller now has over national banks and that the Federal Reserve Board now has over Federal Reserve banks.

Mr. CROWLEY. No; the only power that the Federal Reserve Board has over a State bank is that if they do not conduct themselves properly, they may put them out of the Federal Reserve System, but there they stay.

Mr. BROWN of Michigan. That is right.

Mr. CROWLEY. Now, then, the power that we have over the State banks is just the same as the Federal Reserve Board has over the

State banks, but we carry ours further, and we ask for the power also over a national bank, that we may put them out of the fund.

Mr. Brown of Michigan. But it does seem to me that we certainly have a duplication there of power. In the temporary plan or the permanent plan as it now exists, for instance, in the matter of examinations of banks, you have to accept the examinations of the Office of the Comptroller.

Mr. Crowley. That is right.

Mr. Brown of Michigan. And the only examinations which you are empowered to make now under existing law are examinations of nonmember banks.

Mr. Crowley. That is correct.

Mr. Brown of Michigan. Now, on page 18 of the bill, I think it is, you ask for the power to examine all banks——

Mr. Crowley. No.

Mr. Brown of Michigan (continuing). With the consent of the Comptroller.

Mr. Crowley. May I explain that to you, Mr. Brown?

Mr. Brown of Michigan. Yes.

Mr. Crowley. The reason for that is this. Supposing that the Comptroller or the Federal Reserve Board has a bank which is in difficulty; under our law, we have asked you for the authority to buy assets for the purpose of mergers. We may wish to go in with the Comptroller or the Reserve Board and make an examination to know the position of the bank, in order to try to determine upon a program that will prevent us from taking too great a loss. In other words, we will go into a bank with a million dollars in deposits and buy $250,000 of undesirable assets, and the Comptroller would merge that with $750,000 in another bank, and that would save us the liquidation of a million-dollar liability where we would be getting off with $250,000.

Do you get my point?

Mr. Brown of Michigan. I get your point, but——

Mr. Crowley. In order to do that, we have to have the authority to go into a national bank, and we are only asking for that where the Comptroller is agreeable that we should go in with him on that proposition.

Mr. Brown of Michigan. But it seems to me that even at the present time, under existing law, where we have a group of national-bank examiners under jurisdiction of the Federal Reserve Board, and a group of national-bank examiners under the jurisdiction of the Comptroller, each having different duties, we must bear in mind that we are here establishing a third group of national-bank examiners under your control, with power, I grant you, only upon the consent of the Comptroller, to examine national and member banks of the Federal Reserve System.

Now, my point is this, that it seems to me that the three departments ought to get together to see if we cannot consolidate you all into what seems to me to be a logical organization governing all the national banks of the United States. If we cannot do that, we at least ought to consolidate these three boards or bureaus into one examining division, that would have authority to examine for all three of these governmental bureaus, and it just strikes me that the legislation is ill-conceived in that respect. We have that provision now with respect to the Federal Reserve Board and the Comptroller's office.

Perhaps I ought to say that I think that your Corporation is an illogical Government organization or bureau to undertake that work, but it does seem to me that you are placing an unnecessary burden upon national banks and member banks and forcing them to pay the expenses of examinations which certainly will be more numerous than they have been in the past. It seems to me that you are by this act diversifying the power and authority that the Comptroller's office has over bank examiners.

Now, if this office is not the right office to handle the matter of the examination of national banks, let us turn it over to you or to the Federal Reserve Board, but let us not have three different groups of national-bank examiners.

Mr. CROWLEY. Mr. Brown——

Mr. BROWN of Michigan. I believe that it is illogical.

Mr. CROWLEY. I do not think that you would have any three groups of national-bank examiners, to this extent, that we have examined only State banks. Now, there is no way under the present law that anyone else can examine a State bank except the Federal Deposit Insurance Corporation and the State supervisor.

Mr. BROWN of Michigan. That is true; but let me interrupt you to say that if the law is enacted as you and your Corporation want it to be enacted, that is, with the elimination of nonmember State banks from the Federal Reserve Corporation, then the argument that you are just making would not apply?

Mr. CROWLEY. That is correct.

Let me say to you that there is no duplication of Federal examination at this time. I mean by that that the Comptroller examines the national banks, the Federal Reserve Board examines only the Federal Reserve member banks, and we examine only the State banks.

Let me add, on this matter of examination, that the Federal Deposit Insurance Corporation cannot be put off here all by itself and not be permitted to use the usual precautions that will be necessary in order to keep this fund sound.

Mr. BROWN of Michigan. You have all of that authority under the existing law.

Mr. CROWLEY. We have not the authority to do this. All of the help that we have had so far has been in going into the banks and working with the State commissioner and, by moral persuasion, getting the banks to build their capital, make their application to the Reconstruction Finance Corporation, and things like that.

Mr. BROWN of Michigan. When you made that statement I was inclined to disagree with you. You made it in your opening statement. On page 13 of the original act it provides " that such certification to the Corporation by the State banking commissioner that the bank is in a solvent condition shall, after examination by and with the Corporation, be entitled " and so forth. I grant you that great pressure was brought upon you to be liberal about that, but you had no legal right under the law to admit any bank that was not solvent, and, of course, that means solvent not only as to its deposit liability, but solvent as to its capital.

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Mr. BIRDZELL. The definition of solvency is given in the act, and it says " whose assets are sufficient to meet its liability to depositors and other creditors."

If you will look further, that is the definition that we are revising in this new draft.

Mr. BROWN of Michigan. You feel that until this serious question of what is going to become of several thousand nonmember State banks is solved, that we cannot very well set up a national bank examining department?

Mr. CROWLEY. I think this, Mr. Brown, that you have seen the opposition to your State banks in joining the Federal Reserve System——

Mr. BROWN of Michigan. Yes.

Mr. CROWLEY (continuing). And over a period of 20 years 960 have joined. Now, if you put the 7,800 State banks virtually under a national examining supervision, I think that you would have the same objection that was expressed to their joining the Federal Reserve System.

I think that this whole matter must be taken step by step and corrected each year until you finally get the system that you wish.

Mr. BROWN of Michigan. I may want to pursue that a little bit further, but, before we close I would just like to call your attention to one item on page 27 of the comparative print.

You will remember, Judge Birdzell, when the section of the law which was called the Steagall amendment was attached to the Federal Deposit Insurance law last spring, and that provided that loans to closed banks were to be made through the Federal Deposit Insurance Corporation.

Mr. BIRDZELL. Yes, sir; that is the way the House passed it.

Mr. BROWN of Michigan. And when it got to the Senate and came back, our conferees agreed that it would go to the R. F. C.

Mr. BIRDZELL. Yes.

Mr. BROWN of Michigan. You will remember that either your department or Judge Reed's department in the R. F. C. held that under the wording of the statute, loans to closed banks or the assets of closed banks could only be made on sale of all the assets. I do not remember whether that was your ruling or the ruling of the R. F. C.

Mr. BIRDZELL. That ruling was not our ruling.

Mr. BROWN of Michigan. There was such a ruling, and I am sure that the gentlemen on the committee remember that ruling.

Why not clarify this language here, which is identical, so that you can make loans upon the assets in whole or in part? Do you not think that that amendment would be desirable?

Mr. BIRDZELL. There could not be any objection to that amendment at all.

Mr. BROWN of Michigan. Because that ruling was made, so that you could loan on a part of the assets.

Mr. BIRDZELL. There would not be any objection to that kind of an amendment at all.

May I say, while we are on that subject, that that ruling was not made during the pendency of that bill in Congress last year. It was made subsequently, and it was not our ruling.

Mr. BROWN of Michigan. I think that you are a little bit unfair to the depositors when you require them to file a claim within 1 year. It is readily conceivable that a great many people may be away on trips, or something of that kind.

Mr. BIRDZELL. We have no objection at all to a longer period. The reason 1 year was suggested is because that is a sort of a prevailing contract limitation in insurance contracts, generally.

Mr. BROWN of Michigan. I understand it is.

Mr. BIRDZELL. And it was generally thought to be reasonable, but if the committee should think that a longer period should be provided for, 18 months or 2 years, all right.

Mr. BROWN of Michigan. I thought that perhaps we could clear it up by some language to this effect, that when the claim is clearly meritorious and not contested by the bank itself, the amount should be paid, but if it is a case where there is any contest about it, I would not object to a limitation.

Mr. CROWLEY. You understand that in a great many banks they accumulate a lot of very small balances, maybe of 38 cents or $1, or $2, or $5, and sometime or other we ought to be able to eliminate ourselves from that liability.

Mr. BROWN of Michigan. On page 27, in the matter of loans to banks concerning which you spoke a short time ago, Mr. Crowley, where you are going to bring about a consolidation in order to avert disaster, why do you limit that to July 1, 1936?

Mr. CROWLEY. For this reason——

Mr. BROWN of Michigan. Why should it not be permanent?

Mr. CROWLEY. What we would like to do is to operate it for a year, and then we will come back and give you the benefit of our experience and then have you extend it if you believe that it has been entirely successful. There is grave danger in paying the losses of these banks too easily. It might cause the banks to become careless; that is the reason we limit it so we can have a little experience to guide us in the future.

Mr. BROWN of Michigan. A little trial legislation?

Mr. CROWLEY. That is right.

Mr. BROWN of Michigan. I would very much like to see you give consideration to that matter of seeing that we do not have too many different groups of Federal examiners investigating these banks. I think that that is a serious question.

The CHAIRMAN. I want to ask if anyone else desires to interrogate Mr. Birdzell or Mr. Crowley?

Mr. DIRKSEN. Yes; I do.

The CHAIRMAN. Then we will meet tomorrow morning and resume this questioning at 10:30.

(Thereupon, at 12:45 p. m., an adjournment was taken until Thursday morning, Feb. 28, 1935, at 10:30.)

BANKING ACT OF 1935

THURSDAY, FEBRUARY 28, 1935

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

Hearings on title I of the bill above referred to were resumed at 10:30 a. m., Hon. Henry B. Steagall (chairman) presiding.

The Chairman. The committee will be in order.

I do not have before me the list of those who have already questioned the witnesses, but I believe that Mr. Dirksen indicated at the close of yesterday's session that he wanted to ask some questions.

STATEMENTS OF LEO T. CROWLEY, CHAIRMAN, AND L. E. BIRDZELL, GENERAL COUNSEL, FEDERAL DEPOSIT INSURANCE CORPORATION—Resumed

Mr. Dirksen. Mr. Crowley and Mr. Birdzell, in the comparative print, on page 33, I want to direct your attention for a little bit to the new language there, which states that no State nonmember bank, other than a mutual savings bank, or a Morris Plan bank, or a bank located in the Territories of Hawaii or Alaska, shall become or continue an insured bank after July 1, 1937.

Now, a State nonmember bank, of course, is not a member of the Federal Reserve System.

Mr. Birdzell. That is correct.

Mr. Dirksen. It means that these banks are going to be compelled to become members of the Federal Reserve System, or else the so-called "State nonmember banks" can have no insurance after July 1, 1937.

Mr. Birdzell. That is correct.

Mr. Dirksen. That is the proper inference from that paragraph?

Mr. Birdzell. That is correct.

Mr. Dirksen. First of all, the question arises in my mind as to why, if a State bank is solvent, and if it is sound, and it is so disclosed to be upon your own examination, such a bank should not be insured without having to become a member of the Federal Reserve System.

Mr. Birdzell. Mr. Congressman, that provision is in here in the form that it is because section 12 (b) as passed originally, in June of 1933, contained a similar requirement, except that the date was July 1, 1936; that is, nonmember banks were permitted to obtain the benefits of the insurance until July 1, 1936, without joining the Federal Reserve System. Then, when the temporary fund was extended for a year, that date was also set ahead a year, so as to give the nonmember banks the benefits of the insurance until July 1, 1937, instead of 1936.

Whatever the policy may be with respect to that question Congress apparently considered at the time the Banking Act of 1933 was under consideration here, and the Corporation has not suggested any change in that respect, because it does not particularly affect its operations. That is a matter of policy primarily for the consideration of Congress. There is an exception——

The CHAIRMAN. Let me interrupt you for just a moment.

Mr. BIRDZELL. The exception relates to the mutual savings banks and the Morris Plan banks. Our experience with regard to them shows that there is no likelihood of those banks finding a place in the Federal Reserve System, and we have suggested the amendment which would enable those banks to continue insurance without joining the System.

Anything that Congress may do with respect to other banks is something that we have no particular feeling about one way or the other.

The CHAIRMAN. Let me say this in that connection, that the provision in the Banking Act of 1933 requiring State nonmember banks, in order to avail themselves of the benefits of participation in the deposit insurance, to become members of the Federal Reserve System after July 1, 1936, was stubbornly contested. The House bill had no such provision, but provided for the admission of member banks and State nonmember banks without discrimination, but the Senate bill limited the insurance to member banks. The older members of the committee are familiar with the differences of opinion that obtained among the members of the conference committee, and I presume that you are, on that bill. This is the simple fact of the matter, that we found ourselves with the adjournment of Congress approaching, and the conferees deadlocked over two propositions, one of which was the provision providing that national banks should be permitted to have branches in all States where State laws permitted such branches. That provision, and the provision requiring membership in the Federal Reserve System after July 1, 1936, in order to participate in deposit insurance, were the two controversial points, and we fought those out down to almost the hour of adjournment.

Rather than see the legislation embodied in the so-called "Glass bill", which had been developed as a result of long hearings and labor on the part of Senator Glass and his committee in the Senate, defeated, and rather than to see the defeat of the insurance plan which in a former session of Congress passed the House, and which was embodied in the bill then under consideration, and which the conferees for the House were exceedingly desirous of adopting, we finally agreed to an amendment which would permit branch banking and we yielded on the provision requiring membership in the Federal Reserve System as a condition precedent to participation in the benefits of deposit insurance by nonmember banks.

Last year when the act was passed extending the temporary insurance, another compromise was reached respecting the privilege of nonmember banks of participating in deposit insurance by postponing until July 1, 1937, the date upon which they should be required to become members of the Federal Reserve System in order to participate in the insurance benefits of the Corporation.

Now, of course, all of those questions will arise again in this committee and in the House, and probably in the conference when this bill is to be passed upon later.

Mr. DIRKSEN. Mr. Chairman and Mr. Birdzell, let me point out what is bound to happen under this provision, which you have to read in connection with section 202 of this bill, in title II. Your paramount interest for the moment is in title I, but I suppose that every member of this committee has had the same experience that I have had in the last 2 years, where I helped or sat in on the reorganization of 12 or 15 small banks out in the central part of Illinois. We had to go to the depositors and take waivers of anywhere from 15 to 50 percent, and when these banks were finally reorganized, they had to issue in lieu of the amount of money that was waived by the depositors, so-called " deferred certificates ", which are payable out of earnings, and there is not any other way to pay them.

Now, the Federal Reserve bank in Chicago maintains that those deferred certificates are a contingent liability, and they will not accept them, and they will not accept any bank which has those deferred or contingent liabilities outstanding.

You take a bank in a small town, say of 1,000 people, where they had to waive 50 percent of the deposits and in lieu thereof issue these certificates, which became a charge upon the earnings of the bank if and when earned; certainly a great many of these banks cannot even earn enough money between now and the 1st of July 1937 to get those certificates out of the bank. They are there as a definite charge upon earnings.

If then the Federal Reserve System does not accept those banks because these contingent liabilities exist, and if you do not give insurance to those banks because they are not members of the Federal Reserve System, then there is only one thing for them to do, and that is either to go out of business or otherwise try to get along without the benefits of insurance.

I might elaborate on that a little bit. You may remember that 41 percent of all of the banks in this country are in towns of under 1,000 people, and in section 202 of this bill you will notice——

Mr. BIRDZELL. What page is that?

Mr. DIRKSEN. That is on page 41, that particular section—you will notice that that section says that the Federal Reserve Board, in order to facilitate the admission of these banks, has authority to waive in whole or in part the requirements of this section relating only to the capital requirements of a bank.

Now, we have 2,900 banks in this country that have a capital of $25,000, and in those cases the Federal Reserve Board, under this section, has a right to waive those requirements if it desires, but it has no right to waive any requirement with respect to a contingent liability, and you are going to put those banks out of business under that section. Either they will have to become members of the Federal Reserve System, or not get insurance, and it constitutes a club which is going to have two effects, to put some banks in the Federal Reserve System that do not want to go in, and, secondly, there are some banks that will not be able to go in, and, if insurance is material to the stability, the soundness, and the continued operations of banks, they will have to go out of business.

Mr. BIRDZELL. I think that there is merit in the Congressman's suggestion, particularly with reference to the effect of the waivers that he spoke of. We have come across a number of instances where the depositors had waived a certain amount of their deposits and released the bank from any obligations so far as that liability was concerned, and that enabled the bank to reorganize.

The CHAIRMAN. Let me say a word right here in connection with what Mr. Dirksen just said, in order to bring the history of this transaction down to date.

It is not unfair to say that the conferees on the part of the House, when this bill was under consideration, would never have yielded in connection with this provision and permitted this provision to be enacted requiring State nonmember banks after the 1st of July 1936, to become members of the Federal Reserve System if they were to participate in the benefits of deposit insurance, if we had not felt that the Congress could be trusted before that time to enact proper legislation to extend the benefits of the Deposit Insurance Corporation to the nonmember banks.

Mr. REILLY. There will be two sessions of Congress after this one before that will become effective.

Mr. DIRKSEN. Before what?

Mr. REILLY. Before the 1st of July 1937 will be here, and I think that this discussion at this time is beside the issue, because Congress will later be in a better position to determine what should be done with State banks that do not come into the Federal Reserve System. We might pass a law today, and it might be changed in 2 years.

Mr. DIRKSEN. But, on the other hand, we are writing a permanent bill here now.

Mr. REILLY. It is permanent only until the next Congress sees fit to change it.

Mr. DIRKSEN. But it easier to try to get it right in the first place than to have to come along later and change it.

Mr. WILLIAMS. That is especially true when it should never have been in there in the first place.

Mr. DIRKSEN. Precisely.

Mr. BIRDZELL. If I may complete the statement that I started to make a moment ago, I think that I can shed a little light on this matter from the standpoint of its actual operation.

As the Congressman said in the case of those reorganized banks where there are deposit waivers and the depositors have some kind of a deferment certificate, but no claim against the bank, only against its earnings, we have reviewed in the legal department of the Deposit Insurance Corporation many hundreds of reorganizations where that element entered, and you will appreciate that such banks were not eligible for membership in the Deposit Insurance Corporation unless they were solvent. Whether deferment certificates of this type constitute liabilities of the bank, has much to do with whether that bank is solvent and, consequently, eligible. Wherever we became satisfied that the bank would not be liable for the amount of those deferment certificates, we held that the bank was solvent, and insured it.

Now, what attitude the Federal Reserve Board may take with respect to that same question I cannot tell you. I do know that there have been instances where banks have been reorganized on a deposit-waiver basis, where the Federal Reserve Board has questioned whether the banks had the unimpaired capital required under section 9 of the Federal Reserve Act; so that that is one of the things that is going to confront Congress in dealing with this question.

The Reconstruction Finance Corporation has taken very much the same view of that matter that we have taken in the Federal Deposit Insurance Corporation.

So the Congressman does raise a question that should be considered whenever this matter of Federal Reserve membership requirement is under consideration, and particularly where the capital requirements of section 9 are under consideration.

Mr. DIRKSEN. Then, Mr. Birdzell, as a general thing, is there any reason why a sound and solvent bank should not have insurance and continue to have it?

Mr. BIRDZELL. I do not want to suggest any reason why it is not entitled to insurance.

Mr. DIRKSEN. We have about 3,000 banks in this country that have been operated continuously for 50 years, a great many of them being State banks, and when a bank has a record like that, is there any reason why you should either force them into a system or not give them insurance?

Mr. FORD. If we are going to have a unified banking system, why not have one?

Mr. DIRKSEN. Why compel State banks to surrender all of the rights that they have, and crowd them into a system when probably they will not derive any benefit from it?

There are two or three banks in Missouri that have not missed a dividend for 20 years, and one of them a few years ago declared a dividend of 50 percent, and they never had occasion to use the Federal Reserve System. They do the banking business of their community, and they have never rediscounted paper, and their services have been adequate in their community.

Why force banks like that into the Federal Reserve System, when they do not want to go in, and it carries with it the additional burden of further examinations?

Mr. FORD. There are a good many things that a great many institutions do not want to do, and they have been allowed to run along in their own way, and as a result others have been the victims of their action.

Mr. DIRKSEN. That is beside the point, because those banks that you refer to cannot qualify for the benefits of the F. D. I. C. But now you bring in this alternative proposal, of either shoving them into the Federal Reserve System, or else they cannot get insurance.

Mr. FORD. Of course, my view at the present time is——

Mr. DIRKSEN. And no case has been made out to show why they cannot get it, if they can qualify.

Mr. FORD. I would like to have this put into the record, on the statement of somebody else, that there are supposed to be 8,500 State banks outside of the Federal Reserve System. Is that about right?

Mr. Dirksen. I think so.

Mr. Ford. I would like to have a study made to see what percentage of those banks and to what extent they were strengthened by the R. F. C. in proportion to the banks that were in the Federal Reserve System.

Do you get my point?

Mr. Fox. That is in the testimony.

Mr. Birdzell. That study has been made.

The Chairman. That is something that I have been wanting.

Mr. Ford. I want that study made in a way so that we can make an independent study of that situation.

The Chairman. Let us have it as it is; let us not let those figures be played up in a way so that they do not depict the real situation.

Mr. Fox. They are on page 30 of Mr. Crowley's first statement.

Mr. Dirksen. I have one other question, and I think that I raised this question a year or two ago, with respect to the provision starting at the bottom on page 12 of the comparative print, subsection (i).

I understand from the full text of that section that banks whose insurance has been terminated will be compelled to pay assessments for an additional 2-year period, and that that coverage for an additional 2 years will be imposed upon them whether they will or not.

I think that that is quite long to require that period of 2 years, because in that same section the Corporation is given the power to require any kind of notice to be given, can give the notice itself or compel the bank to give the notice. You can send the notices by mail, or compel circulation of the notices in a newspaper for a month or two, and I should say that 6 months would be an ample time and that thereafter no further assessment should be required.

Mr. Birdzell. Two years may be too long, but I believe that 6 months would be too short.

Mr. Dirksen. Possibly so.

Mr. Birdzell. We do not want to be open to the charge of not dealing in good faith with depositors of banks, and we would rather err on the side of having that period too long than on the side of having it too short. It is a matter of judgment.

Mr. Dirksen. Of course, in the metropolitan centers a little longer time might be required, but in a community of 1,000 people, and almost half of our banks are in towns of that sort, for all practical purposes a week would be ample notice.

Mr. Crowley. I do not object to cutting it down from 2 years to some extent, but it should be a long enough time so that there can be no doubt in our minds but that the depositor has had plenty of time in which to make up his mind as to whether or not he wants to keep his money in that bank. Furthermore, if the bank is an institution that has been doing things which caused us to put it out of the fund, there is a question as to whether we should not give them ample protection for a long period of time, to enable them to correct their practices and again quality for insurance.

I do not think that the judge or any of us has any objection to any compromise in that particular, but the time should be long enough. I do not see that it is any great hardship to the bank to have a period of 2 years, and it is a great benefit to the depositor.

It is also of great benefit to the Corporation. These banks that are badly managed, these banks that should be put out of the fund, should have some string on them until you know that the depositors have had that opportunity to which I have referred.

The CHAIRMAN. Let me say this, please, in this connection, and I do not want to prolong this discussion unnecessarily, that the Deposit Insurance Corporation was never established, nor was the plan of insurance deposits designed, nor in my judgment should it be used, for the purpose of settling any quarrel between the nonmember bands and the member banks. Some believe that we should have a unified banking system, and if that view has enough support to express itself in legislation, let those who believe in a unified banking system in this country devote their efforts to that purpose, but let it be fought out on its own merits; and if we are not to go the whole way and adopt a unified system, let us leave the matter of membership in the Federal Reserve System for State nonmember banks to be determined by the nonmember banks themselves, as provided in the Federal Reserve Act. If a State bank wants to join the Federal Reserve System and finds it desirable, if the inducements are such that the State bank wants to come in, let it come, but with all of its rights under its charter issued by the State in which it does business.

This question of insurance on bank deposits ought not to become involved in any way with the permanent policy respecting a unified or dual banking system. I have my views about that, but I do not think that they have any proper place in legislation affecting bank deposits.

What we are trying to do here is to protect the public against bank failures and against the horrors that have attended bank failures heretofore, and let that legislation be dealt with on its own merits, and leave this question of membership and nonmembership in the Federal Reserve System to be fought out in a normal way, on its own merits.

I believe in membership in the Federal Reserve System, but undoubtedly there are banks that do not want to join the Federal Reserve System, and certainly, as I see it, it is not necessary, and surely not indispensable, that every bank in the country should belong to it or be members on a definite date.

Mr. REILLY. Do you not think that the Congress of the United States will be in a better position 2 years from this time to decide the question whether we want a unified banking system, after we have had 2 years more experience, than it is today? That matter can well be deferred until 2 years from this time, when we can make a better final decision on it.

Mr. DIRKSEN. I think you are right, but this section would have to come out of the bill, because that is an instrument of compulsion to force them in.

Mr. WILLIAMS. And you ought not to wait until the last day to do that. I think that you ought to take it up right now, and give them at least 2 years' notice that we mean to make this a permanent policy, and not compel these State nonmember banks to wait until 2 years from now to see what they are going to be up against.

Mr. CLARK. I just want briefly to supplement what you said, if I may.

As I said the other day, regardless of politics I think that the Federal Deposit Insurance Corporation has the confidence of the people of this country. I know that it saved our West.

There has been some question as to whether or not the Federal Reserve System, at least as it existed in 1929, did not break down. There is a grave question in the minds of a lot of people in this country as to the soundness at all of the Federal Reserve System. Many of the small banks disapprove of it.

I do not believe that we should, under any circumstances, use a well-respected institution like this institution is, which has the confidence of the country, to club nonmember banks into a system which may not have the confidence of the country.

I just wanted to make that one observation.

Mr. FARLEY. In the figures that you have submitted, is there anything that might be a guide as to how many of these banks could not qualify, if this bill went through?

Mr. CROWLEY. I think that 72 percent of the nonmember State banks which are insured could qualify on their capital position now. In other words, in the rebuilding program that has been taking place, we have tried to base it so that they would have sufficient capital to be eligible under the capital requirement.

Mr. FARLEY. I do not know that this question is germane to the bill that we are considering here, but does your Corporation feel that there are still too many banks?

Mr. CROWLEY. No; I do not think that that is generally true now, Mr. Congressman. I think that the banks that have survived this depression certainly showed themselves pretty well able to take care of their situation. There may be certain isolated places where we are overbanked, but I think that as a general proposition the country can support the number of banks that we have now, if properly located.

The big trouble is that you may go much further than the banks that we have now, in extending new licenses.

Mr. FARLEY. Did this elimination of daily balances do the banking business any good?

Mr. CROWLEY. Do you mean the elimination of the interest on daily balances?

Mr. FARLEY. Yes; the elimination of the interest on daily balances.

Mr. CROWLEY. Yes; Mr. Congressman, it did.

The banks were faced with the problem of reducing expenses in proportion not only to their volume of business but also to the reduced rate of earnings on the business that they had. As I explained the other day, the elimination of interest on daily balances subject to withdrawal on demand was an important factor in reducing expenses.

Mr. FARLEY. Is there any demand that you know of on the part of the large, central banks that that provision be restored, so that they may pay interest on daily balances?

Mr. CROWLEY. I know of no demand from any source, either large or small.

Mr. FARLEY. When we put that into the law, there was a great deal of talk then along this line, that if we could hold this money in the smaller banks and eliminate that 2 percent on the daily balances, or any other percent, they would use the money at home instead of using it in the larger centers.

Has that worked out that way?

Mr. CROWLEY. Of course, that is a very hard question to answer, because there has been a very limited demand for new credit on account of your business depression. I do not know how that would work in normal times. I think that under the theory of the insurance of deposits, as I said yesterday, the banks might employ a larger percentage of their deposits in local loans, because I do not think they have to have that extreme liquidity through fear of runs that they might have had before.

Mr. FARLEY. I think that the intent of this bill—and I do not refer to you gentlemen personally—is further to eliminate banks, to get rid of a lot of banks that we now have. I am just wondering how many would have to go if we did it. Today we would lose 28 percent of them.

Mr. CROWLEY. In what way? Do you mean that we would eliminate 28 percent on account of joining the Federal Reserve System?

Mr. FARLEY. I mean that they could not get through.

Mr. CROWLEY. I do not like to get into the controversy on Federal Reserve membership, because that is another part of this bill; but I might say that I have always had enough confidence in legislative bodies, and I have enough confidence in you men to feel that when the time comes, if there are 2,000 or 3,000 banks in this country that cannot join the Federal Reserve System, certainly you are not going to put those banks out of our insurance system. I do not believe that you are going to put into liquidation 2,000 or 3,000 banks. From our own standpoint, all that we have to do is to be reasonable. If you were going to put 2,000 or 3,000 banks into our laps for liquidation, we would be the first ones to tell you how impracticable that was, because of the cost to ourselves. So I have a lot of confiedence that somewhere along the line that will be adjusted, so that the great majority of the State banks are going to be cared for.

Mr. WILLIAMS. There is one thing that I do not yet understand, and I want to get the record straight on it. You say that there are only 72 percent of these nonmember banks that can qualify?

Mr. CROWLEY. I mean by that, Mr. Congressman, that under the present Federal Reserve Law, they must have a minimum capital, and 72 percent of these banks already have sufficient capital to meet that requirement.

Now, under part 2 of this bill, the Federal Reserve Board is asking for authority so that they may waive that minimum requirement of capital.

Mr. WILLIAMS. Let me ask you this, then: Have you not already qualified more than 72 percent of them for admission into the temporary fund?

Mr. CROWLEY. Do you mean by the temporary fund, the Federal Deposit Insurance Corporation?

Mr. WILLIAMS. Yes.

Mr. CROWLEY. Of course, there are 7,800 State nonmember banks. You and I are talking about two different things. I say that there are 72 percent, Mr. Congressman, that are members of our fund now whose capital position is sufficient to joint the Federal Reserve System with the old provision governing capital requirements for Federal Reserve members.

Mr. WILLIAMS. I am not talking about the Federal Reserve. I do not know whether Mr. Farley was or not.

Mr. FARLEY. Your answer was just what I wanted.

Mr. WILLIAMS. I am talking about the number of nonmember banks that can qualify under the law as it is now and come into the temporary insurance fund, and automatically pass into the insured.

Mr. CROWLEY. There are only 1,100 banks, Mr. Williams, State banks, that are outside of our fund today, and our law calls for the 7,800 banks now members of our fund to automatically become members of the permanent fund.

Mr. WILLIAMS. They automatically pass in on the effective date of this law?

Mr. CROWLEY. That is right.

Mr. WILLIAMS. And that is more that 72 percent.

Mr. CROWLEY. Yes; but we are talking about two different things. That is 90 percent.

Mr. WILLIAMS. Now, you have already qualified that number of banks for the temporary fund, and qualified them for the permanent fund; that is, until July 1, 1937.

Mr. CROWLEY. That is correct.

Mr. WILLIAMS. Is there any reason why they should not pass right on into the permanent system after July 1, 1937?

Mr. CROWLEY. You mean, in our permanent system?

Mr. WILLIAMS. Yes.

Mr. CROWLEY. They would go into our permanent system just as soon as you pass this bill.

Mr. WILLIAMS. But they go out on July 1, 1937.

Mr. CROWLEY. My answer to that is this, Mr. Williams: As I said, I have enough confidence in Congress to feel that they are not going to force out of our insurance system 2,000 or 3,000 banks.

Mr. WILLIAMS. You see what my point is, that you have already qualified them, and they automatically pass into the system on the effective date of this law and will be members of the system at least until July 1, 1937, and my inquiry is why they cannot remain in the system after that date.

Mr. REILLY. I might suggest that that will depend entirely upon the judgment of Congress as to whether or not we shall have a unified banking system.

Mr. WILLIAMS. I am asking if there is any reason on the part of this Corporation why that cannot be done. If there is, we would like to have it, because that question will confront us from now on.

Mr. CROWLEY. I think this, that in dealing with that provision, you have to take into consideration your capital requirements and the advantages to your smaller banks of membership in the Federal Reserve System. That, to my mind, is entirely a matter for Congress to determine. As I said, unless you change the Federal Reserve law and liberalize it so that these banks can qualify, there will be at least 2,000 of them that cannot come in unless we build their capital structure up for them.

To put 2,000 banks out of the insurance fund would be a very serious matter.

Mr. REILLY. You said that about 1,500 nonmember banks are out of the insurance system.

Mr. CROWLEY. About 1,100.

Mr. REILLY. Why are they unable to come in and qualify?

Mr. CROWLEY. A very small percentage of these banks felt that they did not need it.

Mr. REILLY. What percentage of those banks that could come in did not come in?

Mr. CROWLEY. We do not know, exactly.

The CHAIRMAN. Of course, there is no way on this earth by which you can know how many banks failed to apply for participation in the deposit fund because they felt that they do not need it, or for other reasons. You do not know anything about those who did not apply.

Mr. CROWLEY. We made the best analysis that we could, but, of course, we cannot say that that is the reason.

The CHAIRMAN. You cannot analyze a bank that you never had anything to do with.

Mr. CROWLEY. Taking the 1,100 banks outside of the fund, their deposit liability only amounts to a little over $500,000,000, so, as a whole, they are very small banks. But there are two or three real large ones.

Mr. WILLIAMS. But that does not mean that they do not serve a useful purpose in their communities, and that they are not sound?

Mr. CROWLEY. That is correct.

I think this: That really the ambition of the Federal Deposit Insurance Corporation should be to get every bank in the Federal Deposit Insurance system, for the protection of depositors, even though they had to make some adjustments in order to get them in.

Mr. WILLIAMS. What percentage of the banks that applied for insurance have not been admitted?

Mr. CROWLEY. We admitted to the temporary fund all except 200 banks that made application, but what we did was this; we took them in, and then we rebuilt them afterward.

Mr. WILLIAMS. Then there have been about 200 out of all of these applications that have been definitely and finally rejected?

Mr. CROWLEY. Yes.

The CHAIRMAN. I want to ask something about that, Mr. Williams.

How many State banks that are nonmember banks belong to the Deposit Insurance Corporation and participate in the insurance?

Mr. CROWLEY. Seven thousand eight hundred, Mr. Chairman.

The CHAIRMAN. How many member banks, both national and State member banks, participate in the deposit insurance fund?

Mr. CROWLEY. Six thousand three hundred; that is, State and national member banks.

The CHAIRMAN. Now, you have 7,800 nonmember banks that participate in the Deposit Corporation?

Mr. CROWLEY. That is right.

The CHAIRMAN. Now, the Reconstruction Finance Corporation has supplied to those 7,800 banks $184,000,000 to replenish their capital, has it not?

Mr. CROWLEY. $256,000,000 up to February 1, Mr. Chairman.

The CHAIRMAN. And you supplied to national banks $465,000,000 through the R. F. C.?

Mr. CROWLEY. That is right.

The CHAIRMAN. And to your nonmember State banks, numbering 7,800, you have supplied $256,000,000?

Mr. CROWLEY. That is correct.

The CHAIRMAN. And, to your State member banks, numbering about 900, you supplied $238,000,000?

Mr. CROWLEY. That is correct—960 such banks, instead of 900.

The CHAIRMAN. So that to your 7,800 nonmember banks that are insured, the R. F. C. has extended $256,000,000, and to the member banks $703,000,000. That does not seem to indicate that your State banks involve any greater hazards or present any worse difficulties than your national banks or member banks.

Mr. CROWLEY. Just let me answer that off of the record.

* * * * * * *

The CHAIRMAN. What is the amount of the deposits of your national banks?

Mr. FOX. About 20 billions.

The CHAIRMAN. Is that for the national banks or for the members?

Mr. FOX. Just the nationals.

The CHAIRMAN. What is the amount of the deposits in your member banks?

Mr. CROWLEY. You mean your State member banks.

Mr. FOX. Twelve billions.

The CHAIRMAN. So that you have 32 billions of dollars of deposits in the banks that are members of the Federal Reserve System.

Mr. CROWLEY. That is correct.

The CHAIRMAN. What is the amount of the deposits in your nonmember State banks?

Mr. FOX. About $4,800,000,000.

The CHAIRMAN. Those figures are not what I thought they would be.

Mr. CROWLEY. Where you become confused a little bit is that we are talking only about State banks that are commercial banks. If you add the savings banks, that increases your total tremendously.

Mr. WILLIAMS. Let me ask one other question, and then I think I will be through.

In all of these figures respecting insured banks that we have before us, I think your latest report is as of last June. If we could get those figures right up-to-date, I would appreciate it, and I think that we ought to get them into the record.

What is the number of the national banks that are insured now, and I would like to have your figures the same as they are in your report, by classes.

Mr. FISH. May I ask a question?

The CHAIRMAN. I suggest that you supplement your statement by the figures that Mr. Williams asked for, and if you do not have them you can get them from the Comptroller's Office.

Mr. FOX. This is for January 31, 1935.

Mr. WILLIAMS. January 31 is all right.

Mr. FOX. Five thousand four hundred and sixty national banks.

Mr. WILLIAMS. Now, your State banks that are members of the Federal Reserve System?

Mr. Fox. Nine hundred and seventy-five.
Mr. Williams. And your State banks that are not members of the Federal Reserve System?
Mr. Fox. Seven thousand seven hundred and thirty-five.
Mr. Williams. And your Morris Plan banks?
Mr. Fox. That is included in that.
Mr. Birdzell. They are in the State nonmember bank figures.
Mr. Williams. The total, if you have it? Of course, that is just a matter of figuring it up.
Mr. Fox. Fourteen thousand one hundred and seventy.
Mr. Williams. Now, have you at this time the exact number of State member banks, commercial banks, that are not in the system at all?
Mr. Fox. One thousand and sixty-six.
Mr. Fish. This may already be in the record, but I have not attended the hearings regularly. If it is not in the record, I think it should be.
I would like to know the total amount of deposits that have been insured, and the percentage of the deposits that have been insured.
Mr. Crowley. In the entire banking system, or of the members of our fund?
Mr. Fish. I should think both. Can you tell that percentage?
Mr. Crowley. 43.49. In other words, of the 38½ billion dollars in deposits in the entire system, they are insured 43.49 percent.
Mr. Fish. Therefore, when you provide for an assessment of one-twelfth of 1 percent, it is one-twelfth of 1 percent of the total deposits, and not of the insured deposits?
Mr. Crowley. That is correct.
Mr. Fish. So it really amounts to about one-sixth of 1 percent of the deposits that are insured?
Mr. Crowley. That is correct.
Mr. Fish. I really wanted to clear that up in my own mind. I figured that on the basis of one-twelfth of 1 percent on the insured deposits, the assessment might be too low to take care of the situation except during normal times, but as long as it covers all of the deposits, it really amounts to one-sixth of 1 percent of the total deposits.
Mr. Crowley. Of the insured deposits.
Mr. Fish. I would like to ask you this—and I hope that it is not an embarrassing question—whether you could tell the committee who sponsored or wrote or originated title I?
Mr. Crowley. Well, I think that we can very safely say that it was our legal department and our statistical division.
Mr. Fish. And when you say " our legal department ", you mean of the F. D. I. C.?
Mr. Crowley. Of the F. D. I. C., and the board of directors, and we did have some help from Mr. Ekern, who gave us some ideas on this thing. He is an insurance man, an insurance lawyer. Mr. Awalt and Mr. McGrath of the Comptroller's staff also gave substantial assistance.
Mr. Fish. Those are the facts that the committee ought to know. So far as I am concerned, I want to congratulate you. You did a very fine job.

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Of course, I want to make it clear that I am referring to title I, and to title I only, in my commendation.

Mr. Crowley. I think that what I said about that was correct?

Mr. Birdzell. That is correct.

Mr. Crowley. May I put into the record here a statement as to losses of insured banks and losses in uninsured banks during the last year?

The Chairman. Let that come in in connection with your statement touching the same matter, at the proper place.

(The statement referred to is as follows:)

Licensed commercial banks suspending operations during the calendar year 1934

Item	Amounts per $100 of total deposits in active banks	Percent of item to total deposits in active banks
	Cents	
Deposits in suspended banks:		
All banks	10	1/10
Insured banks	.5	1/200
Estimated losses in licensed banks suspending:		
Total losses	3.6	36/1,000
Losses to depositors:		
In banks not insured	3.5	35/1,000
In banks insured	[1] .007	7/100,000
Losses to Corporation	.1	1/1,000

[1] More than ⅓ of this loss represented losses to depositors with restricted deposits in 1 institution

Mr. Birdzell. During the hearing questions have been asked concerning paragraph 5 of subsection (h) of the proposed draft relating to trust funds. That provision is new, and I am not surprised that the members have shown some curiosity about it, and, furthermore, it does deal with quite a technical matter.

Recently I had occasion to discuss the general subject of that subsection with the trust section of the American Bankers Association at their meeting in New York. The discussion is too lengthy, of course, to be reproduced here for the purpose of listening to it, but if the members would like to have the benefit of that discussion I would be glad to leave a copy of what I had to say with your reporter so that it may be put into the hearings.

The Chairman. Let me suggest, Judge Birdzell, that you incorporate so much of your statement on that occasion as you regard as helpful to the committee.

Mr. Birdzell. I think that it would be helpful. I could boil it down some——

The Chairman. You be the judge of that.

Mr. Birdzell. I will leave it with the reporter.

(The remarks of Mr. Birdzell referred to are as follows:)

Address of Hon. L. E. Birdzell, General Counsel Federal Deposit Insurance Corporation, on Federal Insurance of Trust Deposits, at the Midwinter Trust Conference of the American Bankers' Association, New York City, February 13, 1935

I am indeed grateful for the opportunity to participate in this conference of the trust division of the American Bankers' Association.

It is always a privilege for one who is daily concerned with problems that affect any group of his fellow citizens to be permitted to present the difficulties with which he is confronted and to gain from the group the viewpoint of those affected by the same problems and whose experiences are gained from a somewhat different angle.

One of the finest characteristics of our basic system of jurisprudence—the common law—has always seemed to me to be that it was founded upon custom, and that it has been sufficiently elastic to yield to the changing customs of society. If this be a virtue in our legal system, as I believe it to be, the virtue is emphasized with respect to that branch of our law which is broadly embraced within the term "law merchant." Much of that law, particularly that dealing with the rights, duties, and obligations of parties to negotiable instruments, was incorporated directly into our legal precedents by the definition and determination of established customs in the market places by those whose contacts and experiences were most immediate and reliable.

If in the formative stages of the law merchant Lord Mansfield was lead to right conclusions by empaneling juries made up of merchants and tradesmen, perhaps it is not too much to expect that even in this day we may proceed with greater assurance in dealing with questions peculiarly affecting a highly specialized branch of business if we seek the counsel and guidance of those who are most familiar with its processes. It is with this hope in mind that I venture to lay before you some of the problems that arise in the administration of the insurance provisions of the Banking Act of 1933 as they relate to the insurance of trust funds.

By way of introducing the discussion, it may be well to refer briefly to some purely elementary matters because of their bearing upon the main questions of interest and because of the principles that rest upon fundamental practices.

In this presence it is not necessary, of course, to speak of the history and development of trust business, nor to trace in detail its connection with commercial banking business. It is sufficient to observe that the banking functions and the trust functions of modern trust companies are and should be kept separate and distinct and to keep in mind at all times that there are certain advantages in combining the two functions under one corporate organization. The clients of a trust company find it convenient to avail themselves of services which can only be furnished by the banking department and, conversely, banking clients find it convenient to avail themselves of the trust facilities of their bank. These advantages have been recognized by the provisions of section 11 of the Federal Reserve Act, which authorize national banks to operate trust departments under the permission of the Federal Reserve Board.

The proper observance of the relations between the bank and its clients and the trust department and its clients requires, however, that the bank shall at all times function as a bank with respect to all funds coming to it in that capacity, while the trust department shall equally observe the fiduciary relation with respect to all funds coming to its trusts.

Under the Reserve Act and under laws existing in many of the States, a national bank or fiduciary company, by complying with stated requirements, may in effect become a debtor to its own trust department without entirely losing its character as a fiduciary. We have, then, one corporate entity sustaining a dual legal relationship with respect to a single account with a single client.

But the act and the Federal Reserve Board in administering it have due regard for the different relationships. The Reserve Board in fixing reserve requirements has provided in regulation D that a bank exercising trust powers need not maintain reserves against trust funds which it keeps segregated and apart from its general assets or which it places on deposit in another institution to its credit as trustee or as fiduciary. But if such funds are mingled with the general assets of the bank, under the authority of the Federal Reserve Act, it is provided that deposit liability thereby arises against which reserves must be maintained. This liability is classified as individual deposit liability rather than as bank deposits.

Assuming, in the language of the Federal Reserve regulation D, that the fiduciary keeps its trust funds segregated and apart from its general assets or that it deposits them in another institution, some might question whether the trust status is strictly maintained. Unless in addition to segregating them the funds of each trust be kept separate and be not mingled with the funds of any other trust, it could be plausibly contended in light of ample trust precedent, that a breach of trust had been committed for which the trustee could be charged. But any such requirement is so foreign to accepted methods for the proper handling of uninvested funds that it would be highly artificial to exact it. A story is told, however, of a trust officer in recent years exhibiting to an examiner his uninvested balances in cash, filed away in the vault, the funds of each trust being kept separate and apart in an effort to comply with the law. It may as well be expected that a warehouseman, in the case of grain or other fungible goods, would provide separate bins for the accommodation of each of his storage customers. It is to the credit, I believe, of the courts of New York that this latter artificiality was abolished many years ago.

Let us look now to some of the specific problems which arise out of the trust and banking relation as we seek to apply the insurance provisions of the Banking Act. Surely in the light of the provisions of the Reserve Act which facilitates the flow of trust funds into ordinary banking channels, there can be no serious question that funds thus legally entering the channels of commerce are deposits within the terms of the law! They are called deposits under the regulations of the Federal Reserve Board and under the existing law which provides for permanent insurance such regulations are controlling. These funds have been regarded as deposits during the temporary period. With this as a premise, how shall we answer the question as to the extent of the liability of the Federal Deposit Insurance Corporation for trust funds which are deposited in the commercial side of the same institution? Shall we regard the company as one depositor and say that the insurance protection extends only to $5,000 or, using the records of the insured institution as a guide, shall we say that each beneficiary is an owner within the terms of the law, and consequently, insured to the extent of $5,000?

Let us look to the law. After prescribing the percentages of insurance coverage based upon the net amount due an owner from a closed bank (and the same language applies to the limited amount insured under the temporary fund), the act says, "*Provided*, That in determining the amount due to such owner for the purpose of fixing such percentage, there shall be added together all net amounts due to such owner in the same capacity or the same right, on account of deposits, regardless of whether such deposits be maintained in his name or in the names of others for his benefit." From this it would seem that if the account be maintained in the banking department in the name of the institution or of its trust department as trustee that it is maintained for the benefit of those who appear upon the books and records of the insured institution to be the ultimate owners, and it is believed that the Insurance Corporation is so liable to each of such owners. The command seems to be clear that we shall determine the amount due, regardless of whether the deposit be maintained in the name of the owner or in the name of another for his benefit and where the records of the institution show for whose benefit the account is maintained the legal measure of insurance protection for each cannot be withheld.

Let us take a second hypothesis: Suppose an insured trust company should deposit uninvested trust funds in another insured institution, the records of the latter will not reflect the beneficial ownership of the funds deposited as in the instance above noted. This would seem to be a single deposit account to be insured as such in the depositee bank. The realization of this situation has led to a great many interested inquiries concerning the extent of the insurance coverage on such a deposit, and it has led further to specific requests that the coverage be extended to meet the practical requirements of the situation. Trust companies making such deposits and desiring to be insured to the same extent as where a similar deposit would be made in its own banking department have made a variety of suggestions. They have offered to pay the assessment upon the additional amount of insurance coverage which would result from a break-down of the deposit according to the interests as they appear upon their own books. (Bear in mind that the assessment is on the insured amount only and not on total deposit liability.) They have demanded, in some instances, that the bank open separate accounts for each trust or each beneficiary. They have offered to file schedules identifying the beneficiaries and showing the extent of their interests, if only they may be assured of corresponding protection. I think we can all agree that there are all but insuperable objections, either from a legal or a practical standpoint, to each of these proposals. Yet, it would seem that if both the initial trust company and the depositee bank be members of the fund, protection should be accorded in this case in the same measure as is given where the deposit be made by the trust company in its own banking department.

Recognizing the reasonableness of such oft repeated requests, the Insurance Corporation offers a solution during the period of the temporary fund based upon this principle: that where a fund member trust company made such a deposit in another insured institution, it would be recognized that the deposit was maintained by it for the benefit of those appearing upon its books and records to be the owners. This gives substantially the same protection to the initial trust company and its patrons as where a deposit is made in the banking department of the same institution. Concerning the assessment, in such case, it was recognized that while two insured institutions were interested there was in fact but one risk; consequently, provision was made for substantially one assessment. Some additional reasons for this will be mentioned later.

Time does not permit a discussion here of the minor details of this arrangement—details which are concerned with the manner of apportioning the interests of the various beneficiaries where deposits are made in several institutions and of the difference which results from exclusive allocation of the funds of each particular trust to one of several general trust accounts as distinguished from depositing uninvested trust funds in general trust accounts without such exclusive allocation—but an effort was made which has been attended with considerable degree of success to make appropriate provision for accommodation to the different methods of handling such transactions. It was necessary to recognize two fundamentally different methods of handling such trust deposits. Where it was the practice of trust companies to group uninvested funds or unexpended balances belonging to certain trust estates, and to deposit each group balance in one of several banks in which the trust company maintains general trust accounts the records of the company would be a sufficient guide in determining the beneficial interests represented in such deposits; but where deposits of trust funds might be made by the trust company without exclusive allocation according to groups of trust estates the interest of a beneficiary in any such deposits in a particular bank would be subject to determination only by applying a formula designed to allocate on a proportional basis. This explains why, in carrying out the general plan for the insurance of trust deposits, under the temporary fund it has been necessary to provide optional plans in order to determine the extent of the insurance coverage on such deposits.

If I may tax your patience sufficiently to enumerate some of the minor factors involved in our consideration of the general problem presented, let me suggest the following:

Filing a schedule of beneficiaries with the depositee bank would involve disclosure of confidential information. This, in some instances, would involve violation of law and it would be objectionable also from a purely business viewpoint. Owing to the constant shifting of interests, the account will be maintained actually for the benefit of persons not named in the schedule and the records of the depositee bank would not identify the owners nor the extent of their interests in the deposit. Where limited insurance is provided, with the depositor as the insured unit, the coverage should not be increased by introducing undisclosed beneficiaries.

Opening separate accounts for separate beneficiaries or trusts involves prohibitory service charges. The depositee bank many properly decline to accept the schedule or to open numerous small accounts.

The furnishing of schedules and certified statements of insured amounts involves examination of numerous trust instruments and a determination of difficult questions concerning vested and contingent interests and the like.

It would seem that any solution of the problem of protection of trust deposits made in the general circumstances outlined above should have regard to these factors to the end that the whole matter may be simplified and be brought into accord with rational practice.

It is believed that the proposed act which is now pending in Congress will acceptably meet this situation. It is there provided that "trust funds held by an insured bank in a fiduciary capacity whether held in its trust or deposited in any other department or in another bank shall be insured subject to a $5,000 limit for each trust estate and when deposited by the fiduciary bank in another insured bank, shall be similarly insured to the fiduciary bank according to the trust estates represented. Nothwithstanding any other provision of this section, such insurance shall be separate from and additional to that covering other deposits of the owners of such trust funds or beneficiaries of such trust estates: *Provided*, That where the fiduciary bank deposits any of such trust funds in other insured banks, the amount so held by other insured banks on deposit on the last day of the month preceding the filing of the certified statement required by paragraph two of subsection (h) of this Section 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. The board of directors shall have power by regulation to prescribe the manner of reporting and of depositing such funds."

Let us briefly note the salient features of this provision:

First, the doubt in the existing law as to whether trust funds while held by an insured fiduciary in its trust department should be considered as deposits is removed. It so considers them. To this extent it is open to the criticism that it is somewhat artificial. But there is no hardship in this because trust companies do not as a rule hold any substantial amount of trust funds for any length of time in a fiduciary capacity. They are either invested or properly utilized as bank funds. Besides, in the event of the closing of an insured trust company the Insurance Corporation could not otherwise give satisfactory answer to the demands of patrons who would have had no means of knowing whether their funds were in one department or another of the institution or deposited elsewhere.

Second, it treats each trust estate as a unit and obviates the necessity for any further break-down.

Third, it preserves the fiduciary status of the depositing trust company by expressly permitting it to be the claimant against the insured bank.

Fourth, it further preserves and recognizes the fiduciary relation and the rightful control of the trust company over the account by treating the insurance of such a deposit as separate from all other insurance for the trust company or for any beneficiary of the trust estates. The amount of the insurance is not affected by the circumstance that beneficiaries may likewise have accounts in the insured bank.

Fifth, in the event of a deposit by an insured fiduciary bank in another insured bank, it recognizes the singleness of the risk. The fiduciary bank is not required to report the amount of such deposit for assessment purposes, this being reported only by the depositee bank.

Sixth, further provision is made to enable the Insurance Corporation to know the extent of its liability.

I am not presenting to you statistics which will show what we all know to be the fact, that a very high percentage of trust funds consisting of uninvested cash and unexpended trust balances and fiduciary accounts generally go into the banking departments of trust companies and into commercial banks to be utilized in the channels of commerce to the same extent as other deposits. These funds, therefore, are properly to be regarded as deposits in any plan which has for its aim deposit protection. They have some characteristics, however, which are not shared by other deposits generally.

In certain circumstances security of one kind or another may be required at the point where they cease to be trust funds and become deposits, but not in all circumstances. Furthermore, they are deposited, as indicated by regulation D of the Federal Reserve Board, not as bank deposits but as individual deposits. By this it is meant to say that a trust company in its trust capacity does not deposit in a bank primarily to promote its trust business or perform its trust function. It does not establish a correspondent relation to facilitate its trust business in the sense that a commercial bank utilizes correspondents to facilitate the transaction of its banking business. Yet such deposits, except to the extent that they may be otherwise secured, are, in common with all other deposits, subject to the hazard which insurance is designed to cover.

It is believed that the characteristics just referred to as peculiar to this class of business warrants the special provisions in the law which have been set out above—provisions which are consistent with existing law and regulations concerning such deposits.

It has been suggested that in view of the security requirements such as are contained in section 11 of the Federal Reserve Act and which are designed to protect transfers of funds from the trust to the commercial side of a banking institution, such deposits might well be excepted from deposit insurance. Similar suggestions have been made from time to time with respect to deposits that are required to be otherwise secured—public funds and the like. The insurance provisions of the Banking Act are clearly intended to apply to all deposits, regardless of whether they be otherwise secured. But from the beginning Congress recognized that other security requirements might properly be relaxed to the extent insurance coverage was effected in the Federal Deposit Insurance Corporation, for it provided that deposits of Postal Savings funds in the banks need not be protected by collateral to the extent they were so insured. In following out the policy thus expressed in the Banking Act of 1933 some of the States are likewise relaxing the requirement for other security for public deposits and bills are pending in Congress to this effect with respect to funds other than Postal Savings funds.

It may well be questioned whether it accords with sound policy for banks to be permitted or required to give collateral security for particular types of deposits. The Supreme Court of the United States last year decided that the power to thus secure deposits generally was not an implied charter power of a national bank, and there are like decisions in a number of States applicable to State banks. Such arrangements, in the event of the closing of a bank, operate to create a privileged class of depositors and in the case of an insured bank they necessarily have an adverse effect upon the Insurance Corporation in that they cut down the amount to be recovered through subrogation to the claims of the insured depositors. Wholly aside from these considerations, however, it must be borne in mind that under the prevailing practice trust companies and trust departments find it advantageous to establish deposit relations with other banks which do not and perhaps which cannot offer security for the deposits, and it would seem to be preferable to establish a uniform rule for insurance coverage rather than engraft a more or less artificial exception. It is believed that such deposits should not be excepted from the insurance provisions of the law.

Trust companies which are not members of the temporary fund of the Federal Deposit Insurance Corporation, which are not members of the Federal Reserve System, and which confine their activities to trust business have likewise exhibited an interest in insurance coverage for such of their funds as are deposited in commercial banks. The problem with respect to these institutions is substantially the same as with respect to institutions which are members of the fund. They desire like coverage, but since they are not members of the fund the powers of the Corporation with respect to examination do not extend to them, and for this reason they are, with regard to their deposits, in the same position as any other depositor. Hence, the Corporation is not able to say to such a trust company that it is maintaining its deposit in a particular bank for the benefit of any specified beneficiary or beneficiaries, and to recognize such undisclosed beneficiaries would involve the introduction of undisclosed owners for the purpose of increasing the insurance coverage.

These companies are all, it is believed, eligible for membership in the fund, and eligible for membership in the Federal Reserve System, and as they may become members they will, of course, share in the benefits of the insurance
These companies are all, it is believed, eligible for membership in the fund,
the existing law. Until such time, however, the only arrangement for insurance protection with regard to them, which the Corporation has been able to suggest, has been that they are insured as one depositor within the limit fixed for one depositor, or if they should find it feasible to so arrange their deposit transactions that they may open separate accounts as trustee for a named beneficiary or for a group of beneficiaries, each separate account would be insured up to the limit of $5,000.

May I leave with you one final word with respect to the Federal Deposit Insurance? I think we can all agree that insurance of bank deposits came into the Federal law at a time when there was the greatest need for restoration of public confidence in the banking structure of our country. I think, too, that we can agree that the general acceptance of the principle has operated to restore and maintain that confidence. We are engaged in an effort to work constructively toward the end that there may never be in our country a repetition of the financial catastrophe that has accompanied the late persistent depression. We can work toward this end and succeed only, in my judgment, with the cooperation of all who are immediately concerned with the major problems presented.

I am glad to be able to express to you this morning the appreciation of the officers of the Federal Deposit Insurance Corporation for the attitude of helpfulness and for the constructive criticism which we have always had from the members of your group. I am personally and particularly grateful for the patience and fine spirit which was manifested by your president, Leon M. Little, on an occasion some months ago when he was good enough to respond to a request for a conference in Washington. If we go forward in this spirit it is our hope that we may all have a part in a great constructive enterprise.

I thank you.

Mr. Crowley. Are there any other questions?

Mr. Sisson. How are we proceeding, in order or out of order, if you will pardon this inquiry?

The Chairman. You are in order right now.

Mr. Sisson. We started out 3 or 4 days ago with the idea that we would make the rounds and give each member of the committee an opportunity to question the witnesses, but the way we are proceeding now, the younger member of the committee will be gotten to on the next Fourth of July.

The Chairman. As you know, I have been away, and when I came in yesterday morning, I thought that the hearings had been pretty well concluded. But let me say to you that everybody on the committee will be glad to hear you right now.

Mr. Sisson. I am not speaking for myself alone, nor in criticism of you.

One of the questions that has been raised here and discussed at considerable length this morning is the question whether the State banks should be required to come into the Federal Reserve System in order to be eligible to membership in the insurance fund, and whether the present provision of law as to when they shall come in, which is, I believe, July 1, 1937, should be changed in this particular bill at this time.

I want it understood, Mr. Chairman, that in anything I say I am not taking any position; I mean by that that I feel that it is not necessary from my point of view to take a position at this time. I do not know whether I have any definite opinion on the matter now or not, but it occurs to me, and I merely make this as a suggestion, that the statement made by Mr. Reilly has considerable merit. There will be two more sessions of Congress before that question becomes imminent, and perhaps we would be in a better position to pass on that after having had a greater fund of experience either at the next session of Congress or the second session of Congress from now, and for the reason stated by Mr. Reilly, I think that my position would be that at the present time we leave that as it is.

However, I appreciate that there are others who have different views and who probably have very sound reasons for them. However, it seems to me that possibly there is an additional reason, one in addition to the reason stated by Mr. Reilly, why that is perhaps academic now, that is, that it is academic for us to decide now whether they shall or they shall not be required to come into the Federal Reserve System in order to get into the insurance fund, and that is that if the Congress should decide that that requirement applies, that they should come in, there is pretty good reason, is there not, why that should be in the law at the present time? In other words, that gives them 2 years' notice or more, and by "them" I refer to the nonmember banks.

Now, I want to ask either Mr. Crowley or Judge Birdzell a question with reference to the provision regarding the limiting of insurance on a single deposit of a trust fund, which I believe appears in subsection (h) of paragraph 5. You fix that limit at $5,000. Is that because of your assumption that the limit of insurance on a single trust-fund deposit is in the permanent writing of this law to be $5,000?

Mr. Birdzell. Yes.

Mr. Sisson. I was wondering if there was any confusion in your answers. When you answered Mr. Williams in regard to the qualification of banks to go into the permanent fund, were you assuming that the permanent fund would contain that limitation of $5,000?

Mr. Birdzell. Yes.

Mr. Sisson. Of course, under the present law, if we do not change it, there will be a $10,000 limit up to 100 percent, and then——

Mr. Birdzell. Up to $50,000 it is 75 percent, and beyond $50,000 it is 50 percent insured.

Mr. Sisson. Now, regarding another question that was raised yesterday, about the examinations and whether they were irritating and irksome, do you have a practice at the present time of combining in certain circumstances your examination with the examination made by the Comptroller of the Currency?

Mr. Birdzell. Not with the Comptroller, but we do with some of the States.

Mr. Crowley. You understand, we make no examinations of national banks.

Mr. Sisson. I just want to make this further comment with regard to some questions raised yesterday by Mr. Gifford about the examination of banks and the suggestion—and this is not a question addressed to you; I presume it is not in your province—that the exactions of the Comptroller of the Currency are so great as made through his examiners with respect to liquidity that it is slowing up and retarding our credit.

I presume, Mr. Chairman, that Mr. O'Connor is going to be here before the committee some time.

I would like to call the attention of the committee to this, that perhaps 2 or 3 months ago the Comptroller of the Currency made a speech at an association of bankers, I think in Nebraska, in which he, in my opinion, gave facts which pretty conclusively disproved the statement or the suggestion made by Mr. Gifford, and he gave the figures which were secured by his examinations and a classification of loans, as to whether they are in the slow column, or doubtful, and so forth, and that address of the Comptroller is incorporated in an appendix to the Record some time in January, I believe. If it is not, I make the suggestion, Mr. Chairman, or perhaps the request, with the approval of Mr. O'Conner, of course, that that be incorporated in these hearings. I think it pretty conclusively establishes—at least it does to my mind—that the oft-repeated statement that the Comptroller's examination of banks is the reason why the banks are not lending money as they ought to is merely an alibi on the part of the banks.

The Chairman. I am sure that the statement of the Comptroller would be valuable in connection with these hearings; I will be glad to have that incorporated in the hearings.

Mr. Sisson. I have one further suggestion, and then I am through. I think that everything else has been covered in which I am interested.

Now, I assume that there will not be any foreclosure on the question as to whether the amount of deposit insurance is going to remain permanently at $5,000, or whether it will be increased to $10,000, and I want to say that the statement of the chairman as to the history of this legislation, on whether State banks should be required to come into the Federal Reserve System in order to participate in this fund, to my recollection is an absolutely correct and accurate statement of it.

But going back to this other question for just a moment, the chairman and those of us who were on the committee when the Banking Act of 1933 was passed containing the provision for deposit insurance will recall that many of the big banks took a very decided and positive position against deposit insurance in general and deposit insurance in any amount, and, in fact, the American Bankers Association—and, of course, the chairman is more familiar with this than, I think, anybody else, because he probably had more to do with deposit insurance than any of the rest of us—met in convention very shortly after the adjournment of Congress, and very solemnly passed a resolution calling upon the President not to put this act into effect.

The CHAIRMAN. That is quite true, and they predicted dire consequences to the economic structure of the country, and then last year they were insisting that the amount of insurance on individual deposits should remain at $2,500 in the permanent law. This year I am not sure, but I think they are now insisting that we make it $5,000 in the permanent law.

In that connection, and not to be critical, but merely because we are dealing with a little history, the American Bankers' Association met here last fall, and that was 1 year from the date of the Chicago meeting to which Mr. Sisson referred, in which they passed a resolution condemning the bank-deposit-insurance law as dangerous to banking institutions and to the general condition of the country; and the first meeting after that was held here last fall.

The first 6 months of operation under the temporary-insurance fund had shown not a single bank failure among the banks that were participating in the fund, and down to the time of the meeting last fall, I think six or seven banks represented the total number of failures, and it showed that the Federal Deposit Insurance Corporation, instead of having encountered an insurmountable loss, was operating at a profit, and the country for the first time in the history of any man at that meeting had had a year of experience practically free from bank failures.

But no mention whatever was made of those developments by any man at the meeting of the American Bankers' Association last fall. They forgot it.

Mr. MEEKS. I want to ask Mr. Sisson this question: The address of the Comptroller of the Currency to which he made reference was delivered in Iowa, was it not?

Mr. SISSON. I think it was in Nebraska.

Mr. MEEKS. There was one delivered in Iowa, and he sent copies of the address to the Members of Congress and invited comment. That is the address that I have reference to. Was that delivered in Iowa?

Mr. BIRDZELL. In Nebraska.

Mr. MEEKS. Thank you; I just wanted to get clear on that.

Mr. FORD. Now, in connection with these examinations, there have been repeated charges made that there were three classes of examinations made of banks. First they said that the F. D. I. C. made them, and then that the Comptroller made them, and then that the R. F. C. made them, and that each one of the examinations called for a different standard as to the classification of assets, and that they never knew where they were.

I would just like to ask, is there any basis for that charge?

Mr. Crowley. Let me say to you that we have never examined a national bank and have no authority to do so. The law specifically says that we shall accept the Comptroller's examination.

I believe that we have attempted, in the entire Federal Service, to try to classify assets as nearly uniformly as possible. The R. F. C., on the matter of State banks, has always taken the examination of the Federal Deposit Insurance Corporation. The only time that they have ever sent a man in was where there had been some difficulty arising, where perhaps they already had an investment, or where, when we made our examination and found that perhaps the bank needed additional aid, or something like that, they have gone in with us and tried to work out that situation. There has been no harassing by duplicate examinations of the Federal Deposit Insurance Corporation and the R. F. C. The R. F. C., except in those unusual cases, has taken the examination of the Federal Deposit Insurance Corporation.

Mr. Ford. I was very certain that that was the case, but I wanted to get that in the record.

Mr. Birdzell. May I just add to that one thing that is just an impression with me, but I am quite certain that I am correct in asserting it.

I think that about 2 months ago the Reconstruction Finance Corporation announced that it would no longer examine banks, but would take the examinations of our Corporation, of the Federal Reserve Board, and of the Comptroller.

Is not that true?

Mr. Crowley. They have been doing it.

Mr. Birdzell. I think that they made a formal announcement of that. That is an impression that I have, and we can all check it.

Mr. Crowley. Except this, that they do reserve the right to protect their investments.

Mr. Sisson. You mean that they have taken the Comptroller's examination?

Mr. Birdzell. If they go into a national bank, they take the Comptroller's examination, and if they go into a State bank that we are interested in, they take ours. They did that with the idea that it would remove the criticism with respect to examinations so far as they were concerned.

Mr. Williams. Has that been the policy all the time?

Mr. Birdzell. It has been the policy quite largely.

Mr. Williams. I mean, in a case where the R. F. C. was advancing money for capital structure purposes, have they not gone in and made an examination of the bank to determine whether or not they would make that advance?

Mr. Crowley. No; except perhaps where there was a condition there where they did not agree with our examinations, or in connection with something that they wanted particularly to verify. In the capital rebuilding program, in better than 90 percent of the cases, they have always taken our examination.

Mr. BIRDZELL. A year and a half ago, they were then engaged in the work of capital rehabilitation, and they might have had to consider banks before we had gotten around to examining them at all, and in that case they would have had to make examinations on their own account.

Mr. WILLIAMS. I have heard that complaint.

Mr. BIRDZELL. A great deal is being done to eliminate the basis for it.

The CHAIRMAN. I am not complaining, exactly, but we should remember in this connection that the R. F. C. act as originally passed contained a provision for loans to banks, and also for loans upon the assets of closed banks, and at that time the F. D. I. C. was not even in existence.

Mr. BIRDZELL. That is correct.

The CHAIRMAN. And the country was in an unprecedented economic upheaval.

Mr. BIRDZELL. That is right.

The CHAIRMAN. And the R. F. C. was acting under a law that required them to take full and adequate security, so that when they began their operations they, of course, were more particular in looking over the assets of banks upon which they were to make loans than they were later on, in the light of later developments.

Mr. CROWLEY. There has been a lot of criticism of the examination of banks. A great deal of that criticism is very unwarranted. You understand that bankers have been under a great strain. They have seen the sloughing away of a lot of values. They have seen a lot of men who under normal times could take care of their obligations promptly unable any longer to do so.

Now, you go in and try to determine the position of a bank, in order that you may try to rebuild its capital position and put it on a sound basis. By the very nature of the trials and tribulations that they have had, if they have not sufficient reserves to absorb their losses and have to write down their capital, naturally there is a feeling of resentment.

But, after the job is all done, it is like the person who has an operation; they feel very good about it.

I know that there are a great many banks that take the examination of the Comptroller's office and of our office and use them as a sort of a club for collections, which is a very unfair thing. They take out the report and say to the borrower. " Don't you see, we have to call this, because the examiner classified it as slow."

Now, there is no criticism on the part of the examining body of a slow asset. The classification of a slow asset only means that the asset is good, but that it cannot be paid at maturity, that it must be spread over a period of time to give the borrower an opportunity to pay it gradually. As long as your banks are sufficiently liquid, it does not particularly mean that they are in hazardous position if a percentage of their loans is in a slow classification; but, as you went into the depression, with your depositors demanding money day by day, it was necessary that the banks, to protect themselves, force this liquidation, and that is the reason why you got your criticism of your slow loans. The depositors were demanding their money more rapidly than the banks could liquidate the loans to furnish it to them. When we have completed our capital rebuilding program, the recovery from the assets that perhaps have been charged off as doubtful and loss may mean considerable in the taking of losses that we have not yet found in our institutions. As we come out of this depression, our banks are again going to have some losses that they will have to face which do not show up on the surface today. A great many borrowers who are struggling today, hoping against hope that they may be able to pay their debts and maintain their businesses, will become discouraged and have to throw it up.

I think that a lot of this criticism is unfair. We will all grant that certain examiners become too officious, and when they get an assignment, they become autocratic; but, as a whole, I think that the examiners have tried to be sympathetic in taking into consideration the mental state of a great many of these bankers.

The CHAIRMAN. Now, if there is anybody else who desires to propound further inquiries to these gentlemen, I will be glad for you to proceed.

Mr. CROWLEY. Before we close, I would like to express our thanks for your kind consideration. Your questions have been most constructive, and if there is any additional information that we may furnish, we shall be very happy to do so.

The CHAIRMAN. If no one else has any more inquiries to make, I will say that we have finished with Mr. Crowley and Mr. Birdzell, and we will meet again tomorrow morning at 10:30, and I will try to advise the members of the committee this afternoon just what the program will be tomorrow. Before doing that, I want to talk to the comptroller, to Mr. Eccles, and to the members of the committee.

(Ordered inserted in hearing)

SPECIAL REPORT OF PUBLIC OPINION AS GATHERED BY THE NATIONAL EMERGENCY COUNCIL ON THE ACTIVITIES OF THE FEDERAL DEPOSIT INSURANCE CORPORATION

ALABAMA

March 26, 1935.—Never any criticism of this activity.

April 9, 1935.—Stands highest in public opinion of all emergency measures; has restored confidence in banks and resulted in greatly increased deposits.

ARIZONA

April 9, 1935.—Apparently public very favorable to Federal Deposit Insurance Corporation. This agency has restored confidence in all banks and undoubtedly exerted considerable influence in abolishing hoarding on the part of the people who had previously felt that banks were unsafe and that they should keep their money in cash at home. Every bank in this State except one is a member. Information at hand indicates that the citizens of the district where this bank is located are very dissatisfied and are not depositing their funds in this bank due to the fact that it does not have deposit insurance. Considerable interest expressed by public in the announcement that deposits in building and loan associations might be insured. General summary would be that the public is very much interested in continuation of deposit insurance and that it is a very determining factor in restoring and maintaining confidence in the banking institutions.

ARKANSAS

April 9, 1935.—Representative bankers advise that public reaction to Federal Deposit Insurance Corporation is 100 percent favorable. Great majority of bankers also favorable, but believe present limit might wisely be reduced to $2,500. Two bankers state they are strongly opposed to plan in principle. None interviewed has ever heard criticism of insured deposits by customers.

CALIFORNIA

April 9, 1935.—Public opinion strongly back of Federal Deposit Insurance Corporation, despite objections of some larger banks to paying premiums.

COLORADO

April 9, 1935.—Public opinion here practically unanimous in favor of Federal Deposit Insurance Corporation.

CONNECTICUT

April 9, 1935.—Public seems entirely indifferent to present Federal Deposit Insurance law. Some 12 or 13 banks in Connecticut have not subscribed to plan and their deposits have not been affected. Some depositors inquired of their banks about this insurance when it became effective, but none has mentioned it to the Hartford banks in months. There is no demand here for increasing amount of insurance above $5,000, as 95 percent of all accounts are fully protected under present law. No Connecticut savings banks subscribed to plan because of adverse opinion of State attorney general. I can find no objection by savings bank depositors. State director personally feels that the present $5,000 limit is sufficient in Connecticut. This State has been particularly fortunate in having very few bank failures.

DELAWARE

April 9, 1935.—Due to fact that no bank failures occurred in Delaware, the public has shown little interest in Federal Deposit Insurance Corporation. Contacts made are all favorable.

FLORIDA

April 9, 1935.—Have contacted 20 various business houses. Everyone heartily endorses the Federal Deposit Insurance Corporation. Believe this sentiment universal in Florida.

GEORGIA

April 9, 1935.—Federal Deposit Insurance Corporation was welcomed by great mass of people. Has been important factor in restoring confidence in banks, particularly smaller institutions. Regarded by many as one of the most constructive steps in present national administration. Increased savings deposits in many banks believed traceable to insurance plan. While activities not subject to general discussion now, individuals and business, especially smaller business, finding satisfaction in safety provided by its operation.

IDAHO

February 19, 1935.—Deposit insurance remains the cornerstone of public confidence in our banks.

March 26, 1935.—Remains cornerstone of public confidence in banks. Bankers admit Federal Deposit Insurance Corporation has produced solid public confidence in banks.

April 9, 1935.—Public opinion overwhelmingly favorable and confidence in banks remains solid with deposits increasing.

INDIANA

April 9, 1935.—Has restored confidence in banks, but has not resulted—for some reason—in a relaxation of bank credit.

IOWA

April 9, 1935.—Public reaction to Federal Deposit Insurance Corporation on bank deposits definitely favorable. Small depositor, which includes savings depositor, is very favorable to insurance of deposits. Best evidence of this is literally hundreds of cases reported to us of money taken from Postal Savings, from hoardings, and from larger banks in border States and deposited in Iowa banks after inception of Federal Deposit Insurance Corporation. There is some disposition to the belief that insurance is so satisfactory to the depositor that he does not seek other investments. Large commercial accounts do not emphasize insurance on their deposits, except as it tends to restore confidence in the bank and thereby stabilizes banking conditions and satisfies small depositor, who as a rule is a cause of runs on banks. Public is grateful and happy for benefits of Federal Deposit Insurance Corporation.

KANSAS

March 5, 1935.—Banks now beginning to fully appreciate the value of this activity with the result that an increasing number are subscribing, however, many banks still remain without insurance.

April 9, 1935.—Although many banks remain without insurance, it has greatly increased confidence in financial institutions.

KENTUCKY

April 9, 1935.—Much appreciated by public generally. Resulted in growing increase of deposits in all banks. Smaller banks quite enthusiastic. Some larger institutions feel their independence, objecting to expense of operation. Some suggest annual assessments of service; others suggest limitation of amount of insurance to $5,000. These objections made some months ago but little protest at present time. Unquestionable demand for retention of act.

MAINE

April 9, 1935.—Public sentiment favorable to Federal Deposit Insurance Corporation. Maine commercial banks favor this. State savings banks have centrally managed liquidity fund.

MARYLAND

March 26, 1935.—Activities progressing quietly.

MICHIGAN

April 9, 1935.—From every source I get only favorable public reaction to Federal Deposit Insurance Corporation. Belief quite general that this agency is reestablishing faith in banks. Increased deposits in Michigan banks best proof of renewed confidence.

MINNESOTA

March 5, 1935.—Agency has done outstanding work and 95 percent of banks in this State are insured. Public well informed and very favorable toward this activity.

March 26, 1935.—Agency 100 percent efficient and popular with both public and banks.

April 9, 1935.—Exceedingly popular and has produced great public confidence in banks.

MISSISSIPPI

April 9, 1935.—Public opinion appears entirely favorable because of Federal protection.

MISSOURI

April 9, 1935.—Reaction of public and State banking department to Federal Deposit Insurance Corporation is universally favorable. Deposits substantially increased. More than 500 State banks have voluntarily come under Federal Deposit Insurance Corporation and only 40 have not. Most of these 40 are small or family banks and expense is deterring factor. The favorable public reaction is general over entire State and also the four-State area. It is recognized as an essential part of the banking system.

MONTANA

March 26, 1935.—Has greatly restored confidence and receives almost unanimous acclaim.

NEBRASKA

February 19, 1935.—Agency has made a fine record in this State with a high percentage of deposits now insured.

NEVADA

April 9, 1935.—After experience of last 3 years when banks were blowing up like firecrackers in Nevada, depositors unequivocally approve deposit-insurance plan. They are not interested in howl of big banks, who may have to carry premiums for some of their weaker brethren. They feel this latter will be an incentive to insist on good banking practices and will insure national supervision and inspection.

NEW HAMPSHIRE

April 9, 1935.—About 1 out of 50 know anything about it. New Hampshire Bankers Association report public neither informed nor interested. Reaction nil.

NEW JERSEY

March 5, 1935.—There is little comment concerning this agency, but it is believed that this activity has full public support.

March 26, 1935.—There is little said about this agency, its activities being accepted as a matter of course.

NEW MEXICO

April 9, 1935.—Have heard of no comments either pro or con in New Mexico.

NEW YORK

April 9, 1935.—Public reaction to Federal Deposit Insurance Corporation not wide-spread, but generally favorable. Larger banks in Manhattan protest method of assessment, claiming only insurable amounts of deposits should be taxed. Otherwise not opposed, although unenthusiastic.

NORTH CAROLINA

April 9, 1935.—General public reaction most favorable. Find in contacting number of bankers, who will eventually help mold public opinion, in vast majority think $5,000 coverage sufficient and favor definite premium sufficient to cover, but to be lowered if justified later. Majority same parties favor premium on insured deposits only. Five thousand limit covers 95 percent depositors banks this State.

NORTH DAKOTA

February 19, 1935.—Public attitude and editorial comment uniformly favorable.

March 26, 1935.—Has restored public confidence in banks and is now accepted as a matter of course.

April 9, 1935.—Agency has restored confidence in banks and public opinion remains wholly favorable.

OHIO

March 26, 1935.—Program has been exceptionally beneficial and remains least criticized of all emergency activities.

April 9, 1935.—Is least criticized of all emergency agencies.

OKLAHOMA

April 9, 1935.—Public reaction reveals this is one Government program with which general public will go all the way. No derogatory comment to Federal Deposit Insurance Corporation was made in interviews with large number of Oklahoma business men and individual depositors. Editors and newspaper clipping bureaus report Statewide approval of program as reflected in press.

Increased deposits indicative of restored confidence. Group 4 of Oklahoma bankers' association in convention at Ardmore yesterday passed resolution recommending titles 1 and 3 of Congressional Banking Act of 1935 and commending work of Federal Deposit Insurance Corporation. Group 5 in Tulsa today expected to pass similar resolution according to secretary of association. These group meetings represent approximately 450 eastern Oklahoma bankers. State banking commission reports only two failures in State banks since inception of Federal Deposit Insurance Corporation. Continuance of Federal Deposit Insurance Corporation under competent management felt essential to continued faith in banking system.

OREGON

February 19, 1935.—Has produced desirable feeling of security of average citizen in his bank account.

PENNSYLVANIA

March 26, 1935.—Has functioned very successfully and restored confidence.

April 9, 1935.—Has greatly strengthened banking system, although many small banks, due to limited capital, criticize the provision compelling them to join the Federal Reserve System by July 1, 1937, in order to maintain their insured status.

RHODE ISLAND

April 8, 1935.—Banking situation here unusually strong, therefore, except for added confidence due to Federal Deposit Insurance Corporation, difficult to determine public reaction.

SOUTH CAROLINA

February 19, 1935.—Has restored confidence in banks. Comment is frequently expressed that this program is one of the most important in "new deal."

March 26, 1935.—Public has great faith in this activity.

April 9, 1935.—Most beneficial.

SOUTH DAKOTA

February 19, 1935.—Comment wholly favorable, with the exception of a very few bankers who are opposed to the principle of this activity.

March 5, 1935.—There is little comment concerning this agency, but it is believed that this activity has full public support.

TENNESSEE

March 5, 1935.—It is suggested that means be provided to inform the public of a bank's insured status by means other than the notices on tellers' windows.

March. 26, 1935.—Has restored public confidence in banks.

TEXAS

March 26, 1935.—Well-staffed and functioning effectively.

April 9, 1935.—Continues to function effectively.

UTAH

February 19, 1935.—Public opinion generally favorable.

March 26, 1935.—Public unanimously for Federal Deposit Insurance Corporation, although some bankers and financial interests remain skeptical.

VERMONT

April 9, 1935.—Public reaction to Federal Deposit Insurance Corporation quiet but favorable. About half the banks use their participation in their advertising. Bank public apparently take it as an accomplished fact and rely upon it, although not particularly outspoken in their comment.

WASHINGTON

March 26, 1935.—Has resulted in vastly improved banking conditions and a general increase in deposits.

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April 8, 1935.—Has resulted in improved banking conditions, although need is seen for means to enforce provisions of Federal Deposit Insurance Corporation.

WEST VIRGINIA

April 9, 1935.—Public reaction to Federal Deposit Insurance Corporation quite sympathetic and guaranteeing of deposits has stimulated confidence in banking institutions. Deposits have materially increased. Bankers, however, are opposed to proposed amendments to existing law now pending in Congress.

WISCONSIN

April 9, 1935.—Don't hear about it. Deposits on increase. Only through restatement of fact that money is in circulation, do we know about its works. Banks favorable.

WYOMING

April 9, 1935.—Banks noncooperative toward this activity.

(Thereupon, at 12:45 p. m., an adjournment was taken until Friday morning, Mar. 1, 1935, at 10:30 o'clock.)

BANKING ACT OF 1935

FRIDAY, MARCH 1, 1935

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

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

The Chairman. All right, gentlemen, we have with us this morning Mr. O'Connor, Comptroller of the Currency, and he will discuss the bill. I am going to suggest that Mr. O'Connor be permitted to proceed in his own way, without interruption, until he shall have finished his preliminary statement, if that is agreeable with the committee.

We will be glad to have you proceed without interruption, until such time as you desire to be interrogated, Mr. O'Connor.

STATEMENT OF J. F. T. O'CONNOR, COMPTROLLER OF THE CURRENCY

Mr. O'Connor. Mr. Chairman and gentlemen, I assume that, from the inquires I have received from the members of this committee and others in Congress, that they have a very especial interest in the national-banking situation, inasmuch as Congress is more directly and largely responsible for the national banks, and I, of course, have most to do with that possibly as Comptroller, and also as a member of the board of the Federal Deposit Insurance Corporation, and I would like to discuss the general situation as well as the bill.

The Chairman. Mr. O'Connor, if you permit me, I am going to suggest that you address yourself, first, to title I of the bill, as we have had that solely under discussion down to this time. After you shall have finished with that, we will then decide as to when we will take up the other parts of the bill, if that is agreeable to you.

Mr. O'Connor. Yes; thank you. Unless the committee desires it, or unless they do not desire it, I would like to bring you up to date with a brief picture of the national banking situation as it is today, from the office of the Comptroller, with reference to these closed banks and unlicensed banks that we started with after the termination of the banking holiday of 1933.

At the close of the banking holiday in March, we had 1,417 national unlicensed banks, and these banks had in deposits $1,971,960,000. The question naturally arises before us this morning as to what has been done with those banks and those deposits, and I am giving you the figures of my office up to the first of February, as we release a monthly report at the end of every month.

We have reorganized 1,091 of these banks with deposits of $1,805,622,000. Thirty-one of these banks decided to go out of business, and they paid their depositors in full, $11,513,000.

There was placed in receivership 292, with deposits of $151,540,000.

Now, that accounts for 1,414, leaving 3 unlicensed national banks at the beginning of the present month, or the beginning of February, rather, and those 3 had $3,280,000 in deposits.

Let us now take up the problem of these banks in receivership. We have paid to depositors in those particular banks, $51,084,265; and we have plans approved for reopening four of these receivership banks, which will release an additional sum of $1,427,000.

That is the complete picture, gentlemen, from March 1933 to the first of February of the present year, and you will notice that all that remains of approximately $2,000,000,000 in the receivership banks is approximately 5 percent of that amount.

That is, briefly, the story of the unlicensed national banks after the holiday.

During the same period, from March 16, 1933, there has been distributed to depositors in all banks, those closed before the bank holiday and since the holiday, $621,920,917; and, roughly, I believe that represents, gentlemen, about 54 percent of the total in the national banks; and please bear in mind that I am only referring to the national banks in this statement.

The total number of receiverships accumulated over the years up to the present time, including those that I mentioned of unlicensed banks, was 1,547, and they had deposits, at the time of the closing, of $1,880,710,184, and there has been paid to depositors to date of February 1, 1935, $1,016,836,666.

In addition to that work, the Comptroller's office has been very much interested in the sale of preferred stock in the national banks, to do two things: First, to strengthen the capital of the national banks; and, secondly, to make more money available for credit, and also to relieve the banks from compelling debtors to pay who are not able to pay at present, but had good, going businesses, and if permitted to go along, could, in time, pay. That was the object of purchasing preferred stock in national banks.

I have received this morning from the Reconstruction Finance Corporation the purchases of preferred stock and capital notes and debentured outstanding, and also loans on preferred stock outstanding, divided, first, national banks and, secondly, State member banks, and third, nonmember banks.

In national banks the loans on preferred stock outstanding were $9,624,716.30; purchases of preferred stock $437,577,064.65, a total of $448,444,001.09.

In State member banks the loans on preferred stock outstanding—and that probably would be also debentures or notes where they were not permitted by State law to issue preferred stock—$1,064,618.44; and purchases of preferred stock, capital notes, and debentures outstanding, $174,943,610.25, or a total of $176,008.228.69.

With reference to nonmember banks and other State banks that are not members of the Federal Reserve System, loans on preferred stock outstanding, $8,797,658.20; purchases of preferred stock, capital notes, and debentures outstanding, $242,213,311, or a total of $249,768,749.06.

Now, that makes a total of the loans by the Reconstruction Finance Corporation on these three classes of banks of $19,486,992.94; and purchases in the capital structure of $854,733,985.90, and a grand total of $874,220,978.84.

I think you will be interested in knowing that there was purchased, locally, of the preferred stock in national banks, $73,366,655.

I think you will be interested in having pointed out, so we will have the record clear, what we mean by loans on preferred stock or capital debentures by the Reconstruction Finance Corporation and the figure I have just given you, the figures with reference to purchases locally; it is the policy of the Reconstruction Finance Corporation that when a bank, whether State or national, needs capital strengthening, first an effort is made to get the people in that community to buy the stock. That seems to be the agreed and very sound policy, that we all feel that we would much rather have the people in the community own these banks, of course, than the Government; the Government, as I take it, being only a temporary expedient in the emergency, and that the stock should be purchased by stockholders and others locally.

Now, another plan that has been worked out, which is also sound, is that when local interests are willing to make purchases of the capital stock to strengthen the bank, preferred stock or debentures of capital notes, who are not able to pay for them in cash, which, of course, must be done, the Reconstruction Finance Corporation will take that stock and other collateral and lend against it, so that it gives the purchasing party an opportunity to finally buy his stock and own the bank.

Just for the record, because you gentlemen, of course, thoroughly understand it, but so someone else reading the record will have it clear, when we speak in the same breath about preferred stock and capital notes and debentures, the reason for that is that Congress permitted national banks to sell preferred stock, Congress having exclusive jurisdiction over the national banks.

Most of the State laws, however, do not permit the sale of preferred stock in State banks; and, therefore, Congress worked out the problem for them of permitting them to sell debentures, or sell capital notes; and the interpretation of all of the banking departments of the Government is, that those notes and debentures are considered the same as preferred stock in the capital structure of the banks, some States permitting notes and some permitting debentures to be sold. I thought that ought to be cleared up, but it does not need to be cleared up for you gentlemen, but someone else who might read it.

I would like, with your permission, Mr. Chairman, to read my recommendations with reference to title I, which is the bill under consideration, which is found on pages 14 and 15 of the annual report of the Comptroller of the Currency, for the year ending October 31, 1934:

> Consideration should be given to strengthening the provisions of the law governing the Federal Deposit Insurance Corporation. In view of the protection afforded depositors, no doubt many of the States will follow the precedent established by Congress in eliminating the double liabilities on shares of stock.

Relieving shares of stock from the double liability, and the insurance of bank deposits offer added encouragement to the establishment of new banks. Great caution should be exercised in the future in the establishment of either State or national banks, or branches of either, in order to prevent a repetition of the failures of a few years ago. Under the present law, if a bank's assets are sufficient to pay its liabilities, the Federal Deposit Insurance Corporation must accept it as a member, although it may have no capital structure.

The Comptroller's Office, under existing law, is in a position to require national banks to maintain adequate sound capital, and also to prevent the organization of a new national bank unless it has adequate, sound capital, and unless there is need for additional banking facilities in the location chosen, and a reasonable prospect that the bank will operate successfully. The Comptroller's Office is thus able to protect the interests of the Federal Deposit Insurance Corporation in those respects with reference to national banks, particularly since the Comptroller is a member of the board of the Corporation. There is, however, no such safeguard as to State banks and it is believed that the law governing the Federal Deposit Insurance Corporation should be amended to make a State bank's admission to the fund conditional upon the approval of its capital structure by the Corporation; and in the case of a new State bank, the board should be required to pass upon the need for additional banking facilities in the place selected and upon the reasonable prospect of the bank's successful operation.

It would be well to consider whether the law should not be further amended to permit the Corporation, under proper limitations, to purchase assets of an insured bank for the purpose of assisting in merging such a bank with another, or of reorganizing when it becomes apparent that a loss to the Corporation is impending. In this manner, losses may be limited or minimized. Under the present law, the Corporation may do nothing until a bank is closed and after that its recovery is dependent upon liquidation. Recoveries through liquidation are certain to be less than the values which may be placed upon the same assets by a going institution.

The law should be amended to provide for examination by the Corporation of State nonmember banks which become members of the fund. An express provision should be made for reports of condition by all insured banks not now reporting to a Federal agency at intervals of not oftener than twice a year, such report to be as of the same date as a call report made by national banks to the Comptroller of the Currency.

The Banking Act of 1933 in section 11, subsection (d) makes specific provision that security for deposits of postal savings funds in banks shall not be required to the extent that such deposits are insured. A general statutory provision should be enacted so that no security shall be required under Federal statutes for any deposits in banks to the extent that deposits referred to in such statutes are insured under section 12 (b) of the Federal Reserve Act, as amended.

It is believed that Congress might well consider the advisability of levying an annual assessment under the permanent plan in lieu of an assessment merely to repair insurance losses, and that it might make provision for carrying a portion of the assessment in a reserve which could ultimately operate to decrease such annual assessment. In banking, as in other businesses, it is desirable when practicable to anticipate the fixed charges, and so far as possible, the cost of insurance should be made a fixed charge subject to reduction through economical and efficient operation.

Miscellaneous incidental matters affecting the Federal Deposit Insurance Corporation should be provided for as follows:

Extend criminal provisions applicable to officers of member banks to officers of all insured banks. Eliminate reference to par value of Federal Deposit Insurance Corporation stock in subsection E of section 13 (b) of the Federal Reserve Act by substituting therefor the amount paid for said stock; extend the prohibition in the present law against gratuities to Federal examiners to examiners of all insured banks and their officers and likewise extend to same the prohibition against disclosure of confidential information; give the Federal courts jurisdiction of actions against the Corporation; extend to the Corporation the protection now given to other Federal institutions against misleading use of their names; and extend to all insured banks the present law making robbery of member banks a Federal offense.

Mr. Chairman, I am ready now for questions.

The CHAIRMAN. I am going to suggest that we begin with Mr. Reilly.

Mr. REILLY. I have received quite a few letters recently, Mr. O'Connor, from old national banks, inquiring as to the possibility of relief from that double liability of assessment through an act of Congress, or some other method. What is your view as to the advisability or necessity or wisdom of any act by Congress at this time?

Mr. O'CONNOR. I covered that in my annual report, and if you will permit me, I will give you that. On page 12 of the annual report of the Comptroller of the Currency for 1934, in answer to Mr. Reilly's question, I make this statement:

> Section 22 of the Banking Act of 1933 relieves shareholders of national banks from the additional liability imposed by Revised Statutes 5151, as amended, and section 23 of the Federal Reserve Act, as amended, with respect to shares issued after the date of enactment of the act. Bills were presented in the last session of Congress to extend this relief to all outstanding shares of stock of national banking associations, regardless of date of issue.
>
> In the event it is determined to completely eliminate this assessment liability of shareholders, it is suggested that serious consideration be given to providing for increasing the surplus of national banking associations until same equals the amount of its common capital stock, thereby restoring to the bank's creditors the protection now given by the potential assessment liability of the shareholders and maintaining a sound banking structure.

Let me say, in that connection, that is a matter that our office, Mr. Congressman, has given very serious consideration to. We must at once appreciate the fact that, by eliminating the double liability on all national banks, we have tremendously weakened the banking structure of the nation. That must be clearly kept in mind. Therefore, I have suggested that, if the Congress decides to eliminate the double liability on all old national banks, the banks should be required to build up, out of their profits, some substantial amounts which shall go into a surplus fund of the banks.

Thereby, you will have in a bank and behind the capital structure, really, in time, the double liability and then relieve the stockholders of it. I appreciate that many people object to relieving the stockholders of this double liability in banks, but those, I think, ought to consider this: First, that banking investments are greatly discriminated against, because of that double liability, investors not wishing to put their money into a corporation upon which they may be called upon later to pay double the amount, or the same amount they have already contributed; and particularly those who make investments feeling that, not during their lifetime, but it might happen that, at their deaths, they have unloaded onto their widows and children liabilities that might wipe out the whole assets and whole savings of that man during his lifetime, which has happened in some instances, unfortunately.

And, again, I think it ought to be pointed out to those who criticize Congress for doing this, that you levy the assessment at the very time when either the holder of the stock or his family is less able to pay it, because in good times you do not need it, and it is only when we get into a period such as we have been going through that we put this extra burden and hazard upon people who are less able to bear it.

It has been the policy of our office to look into every case individually, because we have the duty imposed upon us by Congress to collect these assessments, and when people are perfectly able to pay we require them to pay; we have no option, we cannot give away money.

When people who have property and are not attempting to transfer it to defeat this assessment, or to sell it, come to us and tell us that they are attempting to secure it, but they need time, in every instance we have worked out a satisfactory arrangement with people in those circumstances, and we have not had any particular complaint that we have been unduly harsh in that respect.

Now, directly to the Congressmen, I have given you my view of that, and have tried to answer the criticism.

Mr. REILLY. Your view would be that any legislation by Congress waiving the double liability in the old national banks should be limited to those institutions that have built up a reserve equal to their capital stock?

Mr. O'CONNOR. That is not quite correct. I would abolish the double liability on all banks and provide for the building of the surplus to 100 percent of capital in the future.

Mr. REILLY. I wonder whether any of that kind of legislation would be constitutional. Has Congress any right to declare, by law, that the depositors in a bank, say of $500,000 capital stock, shall be denied the right to levy to the extent of that capital stock, in case the bank should go into insolvency?

Mr. O'CONNOR. Mr. Congressman, you have raised a very important question, and if I have retained any law since I got into the banking business, I do not believe that Congress could pass a law effectively today that would relieve the shareholders from double liability as to depositors and creditors who have entered into a contract with the bank at that time, when their rights were fixed; and their rights are fixed and their contractual relationship with the bank does exist, and I do not think Congress can destroy it.

The only thing Congress can do would be to throw the operating period into the future a sufficient length of time, so that the existing creditors would not be affected, and that would be a contract—because every depositor has a contract between the depositor and the bank—they would then come under the terms of the new law.

I think you have raised a ver yimportant question.

Mr. REILLY. Or give them time to take their money out of the bank and put into some other bank?

Mr. O'CONNOR. Yes.

Mr. REILLY. Right on that point, on that question, what difficulties do the banks encounter when they attempt to reorganize and come under a new law? Suppose you had a national bank of $500,000 capital stock and it wants to get away from its double liability, is there any difficulty in reorganizing and getting a new charter by changing some word in its title?

Mr. O'CONNOR. No; it can do that. Any corporation has that right, but there is a great many procedural difficulties in it.

In the first place, they have got to get the consent of all of their stockholders and explain to them why they are doing it, and bankers rather hesitate to take all of these issues and explain them and get consent from several hundreds or thousands of stockholders and, frankly, since the law has been in effect, we have not had that question presented. There are probably one or two cases that I am not familiar with, in no number that would affect the attention of anybody.

That is my best answer, and I believe bankers have the feeling that it is difficult to do it.

Now, under the present law, Mr. Congressman, you have this: We have in national banks some stock that is subject to double liability, and in the same bank we have stock that is not subject to the double liability.

Mr. REILLY. How does that happen?

Mr. O'CONNOR. Because all the new issued stock is not subject, as you provided in the act, to the double liability.

The CHAIRMAN. Right there, let me trace the history of this legislation. I might say I am responsible for the amendment to the law, the purpose of which was to remove the double liability of the stockholders. The bill as it passed the house, applied to the need to something constantly requiring—I mean the bill as reported by the committee to the House had that language, and the bill was amended in the House in language that I cannot just at the moment recall. I asked Mr. Awalt, a moment ago, if he remembered, but he does not recall the exact language, but in conference the provision was rewritten, and I suggested to Senator Bulkley—the fact was that the Senators in Congress were hesitant about agreeing to it and I suggested to Senator Bulkley, who is an able lawyer, that he rewrite the language so as to make sure of the accomplishment of the purpose in mind.

It was my thought that the language employed by the House in the passage of the bill was not adequate to accomplish the purpose, and Senator Bulkley suggested a new idea which made it apply to stock thereafter issued.

I, at least, and I cannot speak for the other members of the conference committee, but for myself, I proceeded upon the idea that all stock repurchased or resold had to be reissued and that, therefore, the language making the relief applicable to stock thereafter issued would cover all old stock, if transferred.

So that the Comptroller's office—and I am not questioning the soundness of the decision—conclude the act to apply to stock thereafter authorized to be issued; or in other words, applicable only to new issues of stock. The construction was not in line with my own idea. However, that is not important now.

I understood you to say that, in order to make such a provision applicable to the existing stock, or to old stock, it would be necessary to make the effective date at some future time as would remove all question of the contractural relationship between the stockholder and the depositor, or any other creditor of the bank.

I am wondering if you are not slightly in error about that, for this reason: That under the original law, any stockholder of capital in a national bank might transfer his stock and relieve himself of all further liability by meeting the requirements of the existing law, which fixes a definite time within which the statute of limitations would operate against a stockholder who had transferred his stock in good faith, and the period, as I remember it, was 60 days, as I remember, Mr. Awalt.

Mr. AWALT. That is correct.

The CHAIRMAN. So that, in any event, any stockholder could have relieved himself, under the original law, completely from any liability to assessment, if he transferred his stock in good faith 60 days before the failure of the bank, or the period of liquidation; is that true?

Mr. O'CONNOR. Then, Mr. Chairman, the man to whom he transferred it would be liable.

The CHAIRMAN. What was that?

Mr. O'CONNOR. The stock is still liable. The man to whom he transferred it would then be liable.

The CHAIRMAN. Yes, that is quite true.

Mr. O'CONNOR. You have not, you see, eliminated——

The CHAIRMAN. I am speaking now of the contractual relationship of the man in the first place. That man could relieve himself of the contractual relationship after a period of 60 days, if he transferred his stock in good faith?

Mr. O'CONNOR. To make it clear, we had better talk about the liability attached to the share of stock, rather than to the individual, and that you cannot abrogate by act of Congress.

The CHAIRMAN. Let me ask you this question: Do you know how many States have laws providing double liability on the capital of banks—State banks?

Mr. O'CONNOR. My recollection is, nearly all of them.

The CHAIRMAN. Nearly all of them?

Mr. O'CONNOR. Nearly all of them. That is my recollection.

The CHAIRMAN. I am a little surprised to hear that. Although I have never seen the figures.

Mr. O'CONNOR. I think we can get a very clear picture if we ask each member of the committee what his State holds, and you can then get a cross section of the whole country.

The CHAIRMAN. It was my impression that only a few States provided for the double liability.

Mr. O'CONNOR. The members of the committee could tell us quickly what State has not got it.

The CHAIRMAN. Let me ask you this question, in that connection: What would you think of a provision that would go the whole way in the limitation of contractual obligations and existing difficulties in relieving stockholders in national banks, in all States where no double liability attaches to the stockholder, or to stock issued by a State bank?

Mr. O'CONNOR. I can say, Mr. Chairman, and I am just giving my opinion from my experience as a lawyer, my answer would be that it would not avoid the constitutional objection that Congressman Reilly has mentioned.

The CHAIRMAN. I don't think you quite got my question. I mean aside from those difficulties, insofar as you might do so—I am speaking now of the policy of duplicating the same law as to the liability of stockholders.

Mr. O'CONNOR. That is a matter of policy entirely within the discretion of Congress, with the limitation that I previously stated to the committee with reference to the constitutional objection. It was placed, as I believe, in the future a sufficient length of time——

The CHAIRMAN. My question contemplated the removal of those difficulties.

Mr. O'CONNOR. Oh, I see.

Mr. CROSS. Let me ask a question right there, Mr. Chairman.

The CHAIRMAN. Certainly, Mr. Cross.

Mr. CROSS. See if this would not eliminate the situation: I understand, of course, about making a deposit in a bank, and that at the time I do it the stockholders are subject to double liability. I assume, of course, that I have a contract with them, or when I put it in the bank, they are liable, and that gives me better security to get my money back. But suppose you were to put a clause in the law that all deposits hereafter, the new deposits that go in a bank, shall not have the double liability, so that when I put in money in it, in that bank, after that—any money that I put in there before that, I can take it out, all right, but that money that I put in after that is no longer put in there under a contract that I can reap the double liability on the stockholders, so why not put in a clause like that relieving those stockholders of that double liability only in reference to all new deposits?

Mr. O'CONNOR. Mr. Congressman, I think you are absolutely correct, because whenever you do that, you establish a new contractual relationship. Could I suggest probably that some difficulty would be that of administration, of segregation of the amounts, the determination of the dates of the deposits, and then waive the assessment for depositors who are under the double liability and segregated from those that are not?

Mr. CROSS. Suppose I had $10,000 in a bank today in my checking account—of course, I am putting money in the bank and drawing money out, and my checking account will add up to $10,000. Now, when my checking account adds up to that, then the stockholders are not liable for the penalty, for the double liability?

Mr. O'CONNOR. You are absolutely correct. Mr. Congressman, may I call your attention to page 53 of H. R. 5357, section 304, which reads:

> Section 22 of the Banking Act of 1933, as amended, is amended by adding at the end thereof the following sentence: "Such additional liability shall be on July 1, 1937, with respect to shares issued prior to June 17, 1933, by any association which shall be transacting the business of banking on July 1, 1937."

I just call your attention to that because that is the section that you would operate on, if I might use that word, if you decide on what you are discussing.

Mr. HOLLISTER. Mr. O'Connor, your idea is that, even with respect to the deposits which have been incurred, or which have been made obligations of the bank, incurred prior to the enactment of this act, if enacted—if a certain length of time, 2 years or something more is given, that notwithstanding the obligation that exists at the time the deposit was made, which would give them ample opportunity and they would be charged with knowledge of the change in the act, no depositor could claim it after that time?

Mr. O'CONNOR. Now, you are probably a better lawyer than I am——

Mr. HOLLISTER. I doubt it.

Mr. O'CONNOR. This is very important, Mr. Congressman. Of course, as lawyers, we both agree that any individual charged with notice of the law, that he is bound by it, so far as it affects his rights.

You have raised the question that, if he continues during that period with the same contractual relation that he had with the bank as to those amounts, it is doubtful if the bank could abrogate that contract. There is no doubt about a new contract, as the Congressman has suggested. In view of the law, there would be no question about relieving them.

Mr. HOLLISTER. Would it not be a very simple matter with respect to that, because the bank coud really notify all of its depostors to that effect, or to the effect that, on such and such a date, the law would come into effect, and that any depositor will have a right to withdraw his deposit? It will be assumed that, if a depositor does not withdraw his deposits, that he will consent to making that new deposit on that date, and thus change the contractual reationship between the depositor and the bank.

Mr. O'CONNOR. I think, Mr. Hollister, you are absoutely correct.

Mr. HOLLISTER. It seems to me that woud be a perfectly easy way of obviating constitutional questions which might otherwise arise.

Mr. O'CONNOR. In other words, this contractual relationship you talk about can be terminated by either party, because the bank has the right to say to a depositor, "We don't want your money."

Mr. HOLLISTER. A depositor has no vested right in making a deposit, and if a bank cares to notify a depositor that, at a certain date, the relationship between them will be changed, giving him plenty of time to withdraw, it seems to me you are more than liberal in 2 years. You can make it 6 months, and if a bank wanted to notify all of its depositors and give them plenty of time to withdraw their savings as well as demand deposits, that constitutional difficulty will be obviated.

Mr. O'CONNOR. I am inclined to agree with you.

The CHAIRMAN. I was going to propound that very inquiry.

Mr. O'CONNOR. You are too late.

The CHAIRMAN. That is just what I was going to ask.

Mr. O'CONNOR. You are too late.

The CHAIRMAN. What would be the difference between terminating your liability at the end of 60 days, or at the end of 2 years or more? The principle would be the same, of course. Under the amendment, you are going to terminate those obligations arbitrarily, or by one party to the transaction, and if you are, you could do it just as well at the end of 60 days, if you met the same requirements.

Mr. O'CONNOR. Mr. Congressman, may I make this rather broad and rather challenging comment on why this should not be done at the present time, in my judgment? You may not follow it, at all, but looking at the picture now and not from a local angle but from a national angle, I have given to this committee the work of the Government in strengthening the capital structure of these banks. We have gotten them all in very good condition today. I am inclined to believe that we were able to do this job a good deal because of the double liability that was on the shareholders.

Now, let me make that very particular: Here is a bank that has an impairment of its capital, and the Comptroller says, "You have got to repair that capital and put up $100,000, or $1,000,000", and if there is no double liability, those directors and shareholders are not as interested in repairing that capital and working out the problems of that bank as if there was no double liability, because they are just apt to say, "Take it; it is yours", and walk out of the picture.

Now, while we are working out this problem, it is their problem as well as ours, and the Government has gone a long way with these banks in strengthening the capital structure of them, in getting local contributions, so that ultimately they will be owned in the communities; and when they realize the fact that, if we close them, they will pay one hundred cents on the dollar of the liabilities, they are going to hesitate a long time before they will permit that to be done.

Therefore, I believe that, until we get it worked out further, that that is the controlling influence in saving a great deal of the banking situation of this country, and that is why I would not like to see it interfered with.

The CHAIRMAN. Mr. Comptroller, there is a great deal of force in what you say, and I think I can appreciate it. The fact is, if I may take time to say so, that I am not so enthusiastic about the change in the law as I was at one time, because my attitude grew out of the deep sympathy that I felt for so many innocent stockholders, many of them citizens who, out of public spirit and for the promotion of the community, had purchased stock in banks that were under the control of others, with no part in the management, themselves, and who had suffered finally by the imposition of the double liability; and as you suggested a little while ago, many instances have occurred of widows and children who found themselves in the attitude of having inherited a serious liability, rather than an asset. Those conditions were accentuated a year or two ago.

But let me ask you this, in connection with your statement a few moments ago: Is is not true that great difficulty was encountered, in many instances, in reorganizing banks that had been temporarily closed, because of the dread of the investors putting their money in institutions where they incurred liability of reassessment equal to their original investment? Would that not, in many instances, interfere with the reorganization of banks?

Mr. O'CONNOR. No; because that was the reason for passing the law limiting double liability in new banks.

The CHAIRMAN. I am not talking about that; I am talking about old institutions, who had a chance to replenish their capital and go forward under the same ownership or organization and——

Mr. REILLY. The new stock issued has no double liability?

The CHAIRMAN. That is true.

Mr. O'CONNOR. It was all new stock, because it wiped out the other stock.

The CHAIRMAN. You had many cases of this kind, where stockholders would come to the rescue of a weakening institution, by putting in new investments, and all that sort of thing, did you not?

Mr. O'CONNOR. They took new stock, which was not subject to the liability.

The CHAIRMAN. They could take the existing stock, as well as the new stock——

Mr. O'CONNOR. You mean to issue new stock?

The CHAIRMAN. No; strengthen the existing stock was what I referred to.

Mr. O'CONNOR. Yes; they have done that, Mr. Chairman, but not in a great many cases.

The CHAIRMAN. Let me ask you one other question: I believe you suggested that stock in an existing institution is to be relieved of double liability—that when it is to be relieved of double liability, it shall be a requirement that a surplus should be built up equal to the amount of capital. Would you apply that to a newly organized institution?

Mr. O'CONNOR. Absolutely. There is no reason why they should be exempted from it. We would, under the terms of the bill, require 20 percent to start and gradually build up to 100 percent.

The CHAIRMAN. I was wondering, if they did not, why not. They would be, of course, better protected, and it may be better business—I would not say it would not—than the old plan of putting up one-half and being liable for the other.

Mr. O'CONNOR. That is better. Mr. Congressman, can I make one more comment?

The CHAIRMAN. Certainly, go ahead.

Mr. O'CONNOR. Do you not see how much it is going to also assist the Federal Deposit Insurance Corporation, of course, if we can keep that system strengthened and——

The CHAIRMAN. It would, of course, make for a sounder system. I think anybody can appreciate the contention that a bank should not be permitted to pay out dividends to the point of weakening its position.

Mr. REILLY. Mr. O'Connor, with the exception of the interest that the Federal Deposit Insurance Corporation would have in the subject, and the interest of the depositors above the insurance liability, is not that academic, as far as the great mass of depositors are concerned—that you are going to get this money, whether you get it from the stockholders or from the insurance corporation? So, relatively speaking, they are only a small fraction of the depositors in our banks today, and only about 2 or 3 percent of them having any financial interest in the question of whether or not that double liability will be wiped out or left in, they are going to be paid just the same, are they not?

Mr. O'CONNOR. You are absolutely right, Mr. Congressman, keeping in mind the distinction between depositors and deposits in a national bank, and that 42 percent of the deposits are insured under $5,000.

Mr. REILLY. The great majority?

Mr. O'CONNOR. Yes.

Mr. REILLY. You would really think that the Insurance Deposit Corporation—if all of the depositors in a bank which was above the insured limitation, would sign a request that the liability be wiped out, there would be no reason why it should not and could not be wiped out or eliminated?

Mr. FORD. Might I make a suggestion?

The CHAIRMAN. Yes.

Mr. FORD. Would it not be wise to have it printed on the bank pass book, that on and after such and such a date there was no double liability on the part of the stockholders, and give every depositor ample notice, and print it in the part of the rules in that pass book? Why not, in a commercial bank, have it brought to the attention of the depositor, by being printed on his pass book?

Mr. O'CONNOR. I think, Mr. Congressman, that is a very sound suggestion. Mr. Hollister has the same suggestion, without being specific. Mr. Hollister suggested that that would eliminate the constitutional objection, by notification to the depositor, and you suggest a specific method, and that method by you brings the direct knowledge to the depositor, and he would not be injured, because I think we have all agreed that it is a contractual relationship that can be terminated and there is no injury done, because that depositor can do as he likes.

The CHAIRMAN. I am not sure—I do not mean to put my judgment in the matter against that of lawyers competent to pass on it; but I am not sure that any party to a contract can abrogate it merely by notifying the other party that he is not going to live up to it.

Mr. O'CONNOR. Can I answer that, Mr. Congressman?

The CHAIRMAN. Yes.

Mr. O'CONNOR. You can, if it is a contract that can be terminated by either party on notice, and that is what this kind of contract is.

The CHAIRMAN. All right, Mr. Cross.

Mr. CROSS. I want to make this suggestion, or ask him a question: Two methods have been suggested by which that could be done, that contractual relationship could be terminated, but if you notified all of the stockholders—I am speaking now from the psychological standpoint and expediency—that, at a certain date, the double liability of the stockholders will end, or if you put in the pass book that notice, would not that have a tendency to frighten the average citizen, because he does not know anything about that? He would say that the bank is in bad shape, or it is weakening. But you could put that in the law and nobody would know anything about it, and that would settle the whole thing, and it would go along smoothly, without any difficulty at all.

Mr. O'CONNOR. Mr. Congressman, I do not think it is possible to frighten depositors today, with Federal Deposit Insurance Corporation.

Mr. CROSS. Well, some of them have more than $5,000 in the bank.

Mr. O'CONNOR. Well, we just covered the point of the amount which is involved. In the national banks, we have got 98 percent of the number, so that the people that have the large deposits—I think they probably are in a better position to know.

Mr. CROSS. A little more intelligent than the other fellow would be?

Mr. SISSON. Mr. O'Connor, I would like to get this information, if you have it at hand.

Mr. O'CONNOR. Yes, Mr. Sisson.

Mr. SISSON. When you proceed to collect double liability, and in case that you have to go to court, what is the percentage that you collect, what do you get out of it, after it is all done?

Mr. O'CONNOR. I can give you that very accurately, as it is in the annual report. It is 49.78, and that is for a period of 70 years, Mr. Congressman.

Mr. SISSON. There is one other thing about this: I suppose your department had no other resource but to proceed to collect?

Mr. O'CONNOR. No.

Mr. SISSON. But it is a terrible thing to happen to a community, to have to do that. It is just too bad that a situation of that kind has to come up, where the whole community interest may be destroyed. You are very familiar with what I have in mind. I am thinking of a city in my own district right now.

Now, what I am particulary interested in is this: If this H. R. 5357 becomes the law, what is it going to do with the State banking system?

Mr. O'CONNOR. If what, Mr. Congressman?

Mr. SISSON. If this bill which we have under consideration right now, H. R. 5357, becomes law, what is going to happen to the State banking situation?

Mr. O'CONNOR. You are asking a question on this title?

Mr. SISSON. We practically forced the State banks into the Federal Reserve System, or do it in the next 2 years, and I want to know what we are going to do for those State banks, to make it easy for them to get in; or how many of these banks are we going to put out of business?

Mr. O'CONNOR. I can only answer that in a general way: I have taken this position, and it is also one of the recommendations in my annual report, that we ask the Congress to liberalize the assets that are in these State banks, what we call under here "nonconforming assets", so as to permit State banks to more easily become members of the Federal Reserve System. In other words, if we are going to compel the State banks to do something, we have got to be careful that we do not do an injustice to those institutions; and if a certain institution has got sound assets that are not conforming, I feel that the Congress should give the Comptroller permission to permit those banks to qualify, or permit them to come into the Federal Reserve System, and permit the Federal Reserve System to accept them, which it could not do today under the existing laws, because of the assets being as we say, "nonconforming." I believe with you, Mr. Congressman, if we compel then—if we compel that to be done, we have got to be exceedingly liberal in permitting State banks—nobody wants a bank that is not sound, but we have got to be liberal in permitting them to join. When you, by an act, compel them to do that, you have got to be careful that you do not do them a great injustice.

Mr. SISSON. Do you think that could be written into the law, do you think that would be possible?

Mr. O'CONNOR. You have got to write—you would have to change the law, because you have fixed certain standards of membership, and they must have what we call "conforming" assets. You would have to change that, and we will be very glad, at the proper time, to go in and analyze that section with you, and check up on it.

Mr. WOLCOTT. May I suggest that the Federal Reserve System waive, in whole or in part, the capital requirements of nonmember banks, as an inducement to get them in; and if that were true, I assume the Board would be liberal in its interpretation of the law and liberal in its requirements.

The Chairman. Mr. O'Connor, have you any further matter that you would like to discuss relating to title I? If you have, I would suggest that you do so, because we will be glad to hear you, and then will resume our questions.

Mr. O'Connor. Well, I have given my general approval, Mr. Chairman, to this bill. I feel that it has been very carefully worked out, and I think that the fundamental parts of it are very important in looking forward to the successful operations of the Federal Deposit Insurance Corporation.

This bill has been passed by the Banking Committee of the Treasury, and I want to say that I think it is in very excellent shape. I did tell the committee that one provision of it I thought was not just in harmony with my ideas, but the committee thought otherwise. That is with reference to receiverships.

I feel that the present system should be continued. The Comptroller should appoint the receivers of all national banks, particularly based on the record of the office of 70 years, without any reference to myself, because I think we have done a good job in years past, and I hope in the present, when we have returned, out of every dollar collected, 93 cents to the depositors, and we have only taken 7 cents out of any dollar for expenses of salaries of the receivers, and attorneys' fees and rent, and every other item that you can possibly conceive of, which has been included in the 7 cents, and we have returned 93 cents to the depositors.

I doubt the wisdom of setting up two insolvent divisions in Washington. The Comptroller's Office has handled nearly fifteen hundred and I believe that, particularly in view of the fact that only 42 percent of the deposits in national banks are protected by the Insurance Corporation—still, the Comptroller is responsible for the administration properly of the balance of nearly 60 percent and——

Mr. Hollister. Fourteen hundred since the office was established?

Mr. O'Connor. Yes. It would probably be just as well for it to continue without duplication. I am very much opposed to the use of duplication in Government or private business.

I wanted to make that clear, and then say that the bill before you has the endorsement of the committee and I have their comments on it.

There is one other section of the bill that I, frankly, have not discussed with anybody, because I just ran across it yesterday, but I believe——

The Chairman. Before you leave that, Mr. Comptroller, it might be well to call attention to the fact that, under the existing law and under the original Deposit Insurance Corporation law, the Deposit Insurance Corporation could take over any national bank that was closed and operate it as a clearing house for a period of 2 years; meanwhile giving an opportunity for the reorganizing, or for the organizing of a national bank.

The thought back of that was not so much to secure the wise administration of the assets of the closed banks, but to permit the corporation to continue to operate the bank, and to avoid paying the actual cash to the depositors, by being authorized to issue new deposit receipts by the new institution operated by the Deposit Insurance Corporation.

Mr. O'CONNOR. When banks fail because of lack of business, I think it is unwise to attempt to establish another bank on the ashes of the old.

Only one national bank went into receivership in 1934, and it was in Montana, with a deposit liability of approximately $30,000. For several years there were no rains and the surrounding country, the country surrounding it practically dried up, as illustrated by the fact that it only had $30,000 in deposits. The community just could not sustain another bank.

The CHAIRMAN. Then you think it would be uneconomical and unwise to require the Deposit Insurance Corporation to continue to operate a bank, even in a limited way, in that community?

Mr. O'CONNOR. Absolutely.

The CHAIRMAN. But any such institution should at once be placed in liquidation?

Mr. O'CONNOR. Yes. Now, we have a right whereby we may, under this law, establish a national bank, but we do not do it, because I am so anxious to avoid establishing banks which will only result in distress to investors and depositors in the community.

Now, so far this year, we have had only one and——

The CHAIRMAN. In the instance to which you have referred, or to the particular case to which you have referred, that was not a case where there would have been a national bank organized, or would have been required to operate the bank for 2 years, but there would have been no likelihood of reorganizing it?

Mr. O'CONNOR. That is correct. Now, Mr. Chairman, following that out, we only had one national bank fail this year, and they did not fail because of the lack of business or of the lack of necessity for a bank in the community. I would rather not give the State, because that is not necessary, but it was due, unfortunately, to the fact that one of the officers had embezzled some $70,000, and who later confessed the embezzlement. That is something that cannot be avoided. There is need for a bank there and we have set up a bank and made excellent progress, or are making excellent progress in the sale of the old bank to the new bank and the sale of the stock to the people of that community, because they must have banking facilities there, and that gives them the option to do it.

Those are the only two, Mr. Chairman, in the national banking system last year and this year that failed.

The CHAIRMAN. So that, as a matter of fact, you have had, last year and this year, only two national bank failures?

Mr. O'CONNOR. That is right.

The CHAIRMAN. The insurance of deposits under the temporary plan of $2,500, and under the $5,000 limitation provided in the act last year, was not very harmful to the national banking system in this country, was it?

Mr. O'CONNOR. I think it is one of the things that has reestablished confidence all over the country, Mr. Chairman, and I think it is one of the justifications for the contribution on the part of the large banks to sustain the banking system of the country, because when the banks started to crack up, outside of New York, they immediately drew out the reserves from the large centers, and the large banks immediately drew upon the market stocks, in order to meet the cash withdrawals, and we thereby started a vicious cycle of depression; and if we can secure or reestablish the confidence of the depositors of the country, so that will not happen, we have saved the banking situation. The big banks that suffered by that did not close, but they suffered in those trades, and they should be willing to go a long way to prevent that again.

The CHAIRMAN. The fact is that a good many big banks actually closed before the holiday?

Mr. O'CONNOR. I am talking about the big centers, where the big cash reserves are kept, like New York and the other centers; but some very large ones did close, Mr. Chairman, which started the withdrawals from these centers, which, in turn, shut the banks. I am talking about the effects on the good banks, how they suffered, even though they said, "You can't close it"; but they suffered just the same, and the whole country suffered by the throwing of hundreds of millions of dollars worth of securities on the market, in order to realize cash to take care of their customers in the country.

Mr. GIFFORD. Mr. O'Connor, I want to ask a question. I think you have made a very good report here relating to the examination of your banks, but as I recall, even the White House, itself, issued a warning last fall that the bank examiners were still rather too strict, and that they could not expect money to be loaned as long as the banks were worried about collecting their slow loans and liquidating their loans.

I remember your speeches over the country, and I think perhaps you may recall that I may have written you a letter regarding your own viewpoint, and you seem to agree, in those addresses, that the banks should loosen up.

But in my section, whenever I visited the banks, and I visited a great many, there existed a fear of your examiners, especially relating to slow loans. Now, you are claiming in your report that you gave your examiners no instructions relating to the demanding payment of the slow loans, but simply marked them "slow." That, naturally, was effective on the banks and the people who owned that money, by marking them "slow loans." As I think the White House expressed it, there were two branches of the Government, the Reconstruction Finance Corporation and yourself arguing with the banks that they should loosen up, and another branch, which is the examination branch, frightening the banks so they did not dare make loans.

If I may pursue that, I realize that most of the banks—the chief thing they had in mind was to reduce the slow loans, and they did not want to get into any more trouble. You acknowledge in your report, if you are not quite ready to answer——

Mr. O'CONNOR. Yes, I am.

Mr. GIFFORD. You say here that there has been considerable controversy and misunderstanding with reference to the examination of banks; that they may have been harassed by the Reconstruction Finance Corporation's examinations, by the Federal Deposit Insurance examinations, though you examine but twice a year, but, while they were only supervisory examinations, they probably did intimidate and perhaps harass some banks by so many of these examinations.

Mr. O'CONNOR. First, Mr. Gifford——

Mr. GIFFORD. Comment on that, please, on the slow loans.

Mr. O'CONNOR. There is no harassment of banks by several examinations. No national-bank officer in the United States, at no time and at no place, has made criticism of a duplication of examinations, because no such thing exists. The only man who has authority to step into a national bank to examine it is an examiner from the Comptroller's office, and you have provided by law that we must make at least two examinations a year. No other examiner from the Federal Government ever goes into a national bank, with one exception: When a national bank asks the Reconstruction Finance Corporation to become a partner—because that is what they are when they buy preferred stock in a bank—when they ask the R. F. C. to become a partner, the banker and the Reconstruction Finance Corporation sit down and agree on how the deal shall be made, and in that deal the R. F. C. and the bank may agree that a R. F. C. man may come in at a certain time and look over their assets or check up certain matters, which is a matter entirely between the bank and the R. F. C. The bank does not have to do that, or the bank may yield to it, just in the deal between themselves.

The bank has a right to ask that an independent auditing firm make audits—and many of them do that—aside from our examinations. Many of the larger and better banks have independent audits made by some of the large auditing firms to be sure that they have completely checked up on that bank. That disposes of the point of harassment of different examinations.

Now, I want to direct myself to the instructions that were sent out in October 1933 to the national-bank examiners, and then I want to show you the results that followed those instructions.

Mr. SISSON. May I suggest, Mr. O'Connor, that you give Mr. Gifford the figures as to the way you have classified the loans which were placed in the loss column and the loans which were placed in the doubtful column?

Mr. GIFFORD. I have read that, Mr. Sisson. There are very few in the loss column. That is why I limited my question to the slow loans.

Mr. O'CONNOR. I was coming to it, Mr. Gifford, but I have to lay the foundation to get the figures, if I might be permitted to do that.

Mr. GIFFORD. Yes; but I wanted to tell Mr. Sisson that I understand those figures, but I limited it to the slow loans.

Mr. HOLLISTER. Might I ask a question, Mr. Chairman?

The CHAIRMAN. Yes.

Mr. HOLLISTER. Mr. O'Connor, to go back, temporarily, to that question of the taking of debentures in place of preferred stock, is it not true that, in a great many cases, debentures were taken by the Reconstruction Finance Corporation rather than preferred stock in some States, because the laws of the State did not permit the issuing of preferred stock, but also because, in some States where the preferred stock might have been issued, it would have covered double liability and the Reconstruction Finance Corporation did not want to take stock that carried double liability?

Mr. O'CONNOR. Yes; I think that is true.

Mr. HOLLISTER. To show you what I am leading to, whether you take preferred stock or notes or debentures of banks, it is exactly the same, and it was merely to get additional capital?

Mr. O'CONNOR. Yes.

Mr. HOLLISTER. That brings me to the question I am going to ask you, not that it has anything particularly to do with this bill, but I believe it ought to be brought out, and this is a good opportunity: Is it not true that, at the present time, for income-tax purposes, a bank which has notes and debentures outstanding, may deduct the obligation of paying interest on those notes or debentures from its income, and thereby pay less income tax; whéreas a bank that has preferred stock outstanding is not so permitted to deduct it, but the amount which is ultimately paid out upon preferred stock must be paid by the bank for income tax purposes; is that not the case?

Mr. O'CONNOR. You are absolutely correct, Mr. Congressman.

Mr. HOLLISTER. So, would it not be proper to have—I realize you have come from the Ways and Means Committee—would it not be proper to have some sort of legislation passed, which would permit the deduction by the bank of what it has to pay out, the same way that the other banks that have debentures outstanding may deduct the interest on those debentures?

Mr. O'CONNOR. On page 7 of my report to Congress, I make this statement:

Section 23 of the Revenue Act of 1934, paragraph (b), provides for certain deductions from gross income. It is understood that State banks which have sold capital notes or debentures to the Reconstruction Finance Corporation may under this paragraph deduct interest paid thereon in computing their net income for taxable purposes.

National banks in strengthening their capital structure have issued preferred stock to the Reconstruction Finance Corporation, paying dividends thereon, which payment of dividends is substantially equivalent to the payment of interest made by State banks on capital notes sold by them to the Reconstruction Finance Corporation.

You used my language.

Mr. HOLLISTER. I knew that was in the report, but I thought it well to bring it out. . Can you tell the committee whether your office is suggesting to the Ways and Means Committee that they take up that matter?

Mr. O'CONNOR. Yes, we have submitted it.

The CHAIRMAN. Mr. O'Connor, let me suggest that you conclude your discussion of the matter of examinations.

Mr. O'CONNOR. Oh, yes; thank you.

The CHAIRMAN. As I understand, you had not finished.

Mr. SISSON. Mr. Chairman, may I interrupt?

The CHAIRMAN. Yes.

Mr. SISSON. Mr. O'Connor, you spoke, a short time ago, about the fact that—or you mentioned the fact that 97.5 percent, I believe, of the total number of deposits were—I assume you were referring then to the member banks, or just to the national banks?

Mr. O'CONNOR. National banks.

Mr. SISSON. Were covered by deposit insurance. I am not sure whether Mr. Crowley testified—he testified yesterday quite fully on that, but I am not sure whether he gave the aggregate amount, in dollars, of the deposits that were covered. If you have that conveniently, I think it might be well to have that in the record at this point.

Mr. O'CONNOR. National banks, 5,450, insured deposits, $8,488,-554,000, uninsured deposits, $11,583,949,000, and total deposits, at this time, or on October 1, were $20,072,503,000, which shows that 42.29 percent of the deposits are insured by the Federal Deposit Insurance Corporation, insuring $25,972,035,000 deposits, and 405,811 deposits are partly insured, which makes a total of 26,377,846 depositors, and 98.46 percent of the depositors are insured; and in State banks, which are members of the Federal Reserve, we have 969 banks, with insured deposits of $3,582,449,000, and uninsured $7,382,986,000, making a total of $10,965,435,000, which shows that 32.67 percent of the total deposits are insured, with 9,361,278 depositors, and 119,082 partly insured, with a total number of depositors of 9,560,360, and the percentage of depositors insured is 97.92 percent; and State banks, which are not members of the Federal Reserve, exclusive of the mutual savings banks, number 7,638, with insured deposits of $3,580,803,000; uninsured deposits of $1,363,262,000, and total deposits of $4,944,-065,000; and the ratio of insured to the total deposits is 72.43 percent; and the depositors fully insured are 13,687,403; and depositors partly insured, 142,947, making a total number of depositors of 13,812,350, or 99.10 percent of the number of depositors in State banks are insured.

The CHAIRMAN. As State nonmember banks?

Mr. O'CONNOR. Yes; that gives us a total there which is rather interesting in these three divisions: 14,057 banks with insured deposits of $15,651,806,000; uninsured, $20,330,197,000, with total deposits of $35,982,003,000, with the ratio of insured to total deposits of 43.50 percent; and depositors fully insured, 49,020,716; depositors partly insured, 729,840; and total number of depositors, 49,750,556; and the total number of depositors insured in the three classes, under the $5,000, is 98.53 percent.

Mr. SISSON. That gives the complete picture there.

Now, may I say, in a preliminary way to one question that I want to ask, and I am not indicating any opinion that I have, because I do not know whether I have any positive conviction about the advisability of increasing the maximum of insurance deposits, but I just wanted to ask you, before you pass from it, if you are going to discuss it at some later date before the committee, that is, as to your opinion of the advisability of increasing the maximum limit of deposits, insured deposits? If you do, I do not care to ask you to go into it now, because that is perhaps breaking up the continuity of your statement.

Mr. O'CONNOR. Well, Mr. Sisson, I feel that we have presented all of the statistics and figures, and the amount is a matter that ought to be a matter of policy of this committee.

Mr. SISSON. Yes, sir; but guiding the committee, unless the majority of the committee have decided already that there will be no increase, the committee probably before voting upon or deciding upon it, would like your opinion.

Mr. O'CONNOR. Then, may I put it this way?

Mr. SISSON. I am not asking you to give it now.

Mr. O'CONNOR. If the committee agrees to it, or gets to that point, I will be very glad to give you my opinion.

The CHAIRMAN. Mr. O'Connor, have you given any thought in that connection? I am asking this question: Have you given any thought to the difficulties that the banks will find themselves in, in relation to their obligations to other banks, when they fail;

what that picture would disclose, if we should have any considerable number of bank failures in the country?

Mr. O'CONNOR. Yes, we have thought a good deal about that, and it is pretty complicated.

The CHAIRMAN. I am wondering how much noise we will hear around here about the amount of deposit insurance after the banks gather some experience and they find they are not insured against one another. That thought is reconciling me somewhat to the idea of limiting this insurance, for the time being. I have the idea that the banks will take care of the matter of increases, as soon as they gather some experience, in case we have a large bank failure. I would like to be here when that happens.

Mr. GIFFORD. Mr. Chairman, do you want me to continue on the examination?

The CHAIRMAN. Gentlemen, if nobody objects, let me suggest that Mr. O'Connor conclude his discussion of this matter of examinations, if he desires to say anything further.

Mr. O'CONNOR. I started, several times, and there is just two pages, and as a foundation, I would like very much to put this in the record and be subject to any questions.

The CHAIRMAN. There will be no objection to your incorporating that in the record. You may do so right now, and if you desire to say anything further, we will be glad to hear you.

(Here followed discussion off the record.)

Mr. O'CONNOR. Mr. Chairman, I would rather that speech would stand, because it is so knit together.

The CHAIRMAN. We will be glad to have it.

Mr. O'CONNOR. But at this time I would like very much to call the committee's attention, for the purpose of laying the foundation for future questions on a very important matter that the country has been greatly interested in, and which has been considerably misrepresented until this was given to the country, and I would be glad to give some reactions that I got after this speech was made by depositors as well as bankers and others.

The Comptroller of the Currency sent, on October 26, 1933, to each of the 12 chief national-bank examiners in the United States instructions to this effect:

"After the 'Bank Holiday', national-bank examiners were largely engaged in the examination of banks which did not receive a license for the purpose of reorganization. It appears that some examiners in making examinations of licensed national banks have become what might be termed 'Reorganization Minded' and have lost sight of the President's recovery program and its relation to licensed banks. It is the administration's desire that credit channels be opened through licensed banks, and this policy cannot be accomplished if examiners follow a deflation policy in examinations. We are all concerned in having solvent banks, but there is a wide distinction between the potential and intrinsic value of assets of a going institution, and liquidating values. Examiners in appraising and classifying assets of licensed banks will not apply liquidating values but will appraise on the basis of fair values on a recovery basis.

"As an example—in dealing with bank buildings, the examiner must realize that a bank building of a going bank has an intrinsic value, as distinguished from present depressed values, which, combined with the element of recovery, may fully substantiate the carrying value given to it by the bank. The same is true of mortgages, and in this connection the examiners should familiarize themselves with the instructions given with respect to real-estate mortgages by the Federal Deposit Insurance Corporation to its examiners.

"You will advise examiners who are examining licensed banks of this policy and see that it is carried out. Any examination now in process, or any future examination, will be governed by these instructions and where an examination has been completed, the examiner making the report will review the report on the above basis and rewrite such report if found necessary. If the examiner is not now available it may be necessary to make a new examination on the proper basis."

Again on March 13, 1934, the following instruction was sent to all chief national-bank examiners:

"Reports of examinations received by this office recently clearly indicate that some few of the examiners throughout the country have not fully grasped the meaning of instructions communicated to the chief examiners under date of October 26, 1933, and are making more drastic classification of assets of the banks examined by them than is necessary under the circumstances and more severe than is contemplated by the instructions contained in office letter referred to above.

"If there are in your Federal Reserve district any examiners who, in your opinion, are making unnecessarily drastic classifications of assets, please confer with them promptly, looking towards having their classifications as lenience as circustances in each case will permit and in order that they will be in accord with the policies of this office.

"While you are familiar with the character of examinations made by your examiners, it is suggested that in determining whether or not any of them are too severe in their classifications, you give particular attention to their appraisals of banking houses, furniture and fixtures, and loans secured by real estate."

No system is perfect because men are not perfect. Here and there isolated cases appear where examiners have been too harsh. These instances are sometimes called to the attention of the proper officials; but where examiners are too lenient, that fact seldom appears. The instructions which I have cited have never before been made public. However, I believe the time has come to clarify a criticism which is unfair. The question naturally arises—what were the results obtained under the instructions? Again, for the first time, I will give you a complete picture of the examinations made by the national bank examiners as shown by 1934 reports of examination. As is well known to bankers, examiners classify loans under three headings—slow, doubtful, and loss. There is little room for argument when assets are placed in the loss column and very little question arises in the doubtful column. The slow column attracts the most attention and controversy. An examination of the reports filed with the Office of the Comptroller of the Currency in each of 5,275 banks reveals the following interesting figures: The total amount of loans was $7,740,596,000. The examiners placed 2.88 percent of these loans in the loss column and 4.19 percent in the doubtful column and 27.05 percent in the slow column. The country has been advised of the definition of slow paper as follows:

"The examiners when classifying loans as slow should state briefly the reasons for such classifications, but should bear in mind that the responsibility for determining and taking such action as may be necessary to place such slow loans in proper bankable shape rests entirely with the bankers. The examiners therefore, should refrain from instructing the bankers as to what course they should pursue with their customers whose paper is classified as slow."

Now, I want to answer specifically, Mr. Congressman, the question you raised with reference to the reaction to the slow column or classification. My general experience is that bank directors, aside now from the operating officials of banks, are very anxious that we retain in our reports these slow columns. The purpose of that is to direct the attention of the directors to what our examiners find in the banks, so that a bank will not gradually find itself in a very frozen condition.

We merely point out certain paper to be slow; it is good, it is sound or it would not be in that column; and by specific directions, we say to our examiners, "You shall not tell that banker what he shall do with that paper." Now, we say, "You are to make comments to us." Everyone will agree that a bank should not have an undue amount of slow paper, and without giving places, which I trust you will not ask me for, because it is not necessary for the purpose of discussion, two most serious cases that arose in this country, and in one where the greatest distress was found because of the lack of dividends to depositors, was due to the fact that the bank became frozen with slow paper, which should not have happened.

Therefore, it seems to be the common opinion among directors, and in most instances now they are much more careful than they were before, and they asked to have read and in the directors' minutes, and our reports are read to them, and they are generally discussed, and if they find the amount of the slow paper the directors themselves can make inquiry of the officer as to that particular paper, what it is, and make some investigation of it; and we find, Mr. Congressman, notwithstanding the fact that there has been some discussion as to the elimination of the slow classification, my judgment is it would be a serious thing to do.

Mr. GIFFORD. Mr. O'Connor, I think you fully understand why I am asking the question. The public at large is interested, because they thought there were two branches of the Government, one working against the other; and when I got your report as to the slow loans, I thought you did not even imply that putting them into that column meant that they ought to be paid.

Our bankers say, "We run our banks. We must pay 6 percent to get this paper renewed." They have an abundance of property or assets, and we have to harrass them. But those slow loans—I got notice from the banks that the examiners had criticized their loans, and when they put them in that column it was implied criticism, although not an implied order that they must be collected.

Mr. O'CONNOR. The banker who said that was dishonest. The banker who made that statement was dishonest with the borrower, unless he accompanied it with the instructions that we sent to the banker and to the examiners.

Mr. GIFFORD. If the banker had told you it was put into the slow column and is must be made an active account, something must be paid on it, what would you thing about it? Of course, I could bring up specific instances now, but I just do not want to. I could give you several that I am sure you would agree to, I think, from your letters to me, which I believe show your viewpoint.

Mr. O'CONNOR. Yes, I know. I appreciate that very much.

Mr. GIFFORD. You acknowledge, yourself, your second letter to your examiners, that in matters of real estate, they have been too strict. Of course, there had been many cases where they were marked off as a complete loss, certain real estate loans, that might later prove of some value; and in many cases, the bank claimed the loss, so they had to go to the R. F. C.

All of my questioning is specifically founded upon the fact, in this article, or in this title I, you ask the banks to furnish burglar insurance, and a whole lot of things, and that they be subject to further examination. If the examinations have been an irritating factor to a sufficient degree, to have caused the banks, in the last 2 years to be unwilling to loan money, and that has been their chief——

Mr. O'CONNOR. Alibi?

Mr. GIFFORD. You agree with that?

Mr. O'CONNOR. An alibi?

Mr. GIFFORD. Yes; call it an alibi, if you wish.

Mr. O'CONNOR. Which is not true.

Mr. GIFFORD. I doubt if it is true, myself, but we have been faced with it by men who wanted to borrow money and——

Mr. SISSON. Mr. Chairman, if the committee will pardon a personal allusion, I used to manage a baseball team and I fully realize how an alibi can be used, because when a player, when he missed a ball, he said that the field was uneven and the ball did not bounce right. I think the most interesting alibi the bankers have had is, that they have laid the blame upon the Comptroller's examinations.

That is what I have been trying to bring out before this committee.

The CHAIRMAN. The truth is, that the Comptroller's Office, for several years, has been criticized because of its liberality, and it risked a great deal in going as far as it did in liberalizing the policy of examinations, to try to deal constructively with the difficulties we have had in the past years, and I commend you and your predecessors for what you have done, and I believe the people who understand it feel the same way.

Mr. GIFFORD. Mr. Chairman, I am trying to bring out the facts that the banks have not loaned money the last 2 years, call it alibi or anything else you like; they have not done it, and there has been no reason for it.

The CHAIRMAN. When you call it alibi, I agree with you.

Mr. GIFFORD. I am allowing that word to go in, but some definite reason has been back of it for 2 years.

The CHAIRMAN. They are scared to death.

Gentlemen, let me ask if there are any other questions from Mr. O'Connor; and if there are not, I am going to suggest we excuse him and conclude with his statement on title I, and the committee will not meet again until Monday.

Mr. WOLCOTT. Just a moment, please, let me ask you a question: The Federal Reserve System, I am given to understand, have about $2,400,000,000 of excess reserves. What is your opinion, Mr. O'Connor, as to why that money has not been loaned?

Mr. O'CONNOR. Well, Mr. Congressman, a rather careful analysis was made of that in Dr. Viner's report, which he made sometime ago, a few weeks ago, or probably a month ago, and he sent some very efficient men, I believe, and compared very carefully the reasons—now, I am just giving you what I think about it, not having anything to do with it, but I believe that he sent men to follow through the loans of the banks that were rejected and get an analysis of why the people were not borrowing and why the loans were rejected, and I believe the Doctor concluded that there was not such a demand for loans. He concluded that the demand was not there for legitimate loans that the people thought.

Now, I am just stating that, because I read the report very briefly and hurriedly, but the report is available and that was his conclusion, and I think that the report—I would rather refer to it and refresh my memory about it than to give you an offhand opinion, without any facts.

Mr. WOLCOTT. That would seem to be true, in view of the fact that the Reconstruction Finance Corporation, I understand, has had demands made upon them for only about $100,000,000 of the money we made available for loans to small industries, and have paid out actually less than $7,000,000.

Mr. O'CONNOR. That is right.

Mr. WOLCOTT. What I am getting at is an expression of my own personal feeling in that connection, that undoubtedly the lack of demand on the part of borrowers is due to the uncertainty of the economic future of the country; and possibly we might be able to overcome that by maintaining—by establishing and maintaining definite policies concerning our money and our attitude towards business. Do you not think that might help some?

Mr. O'CONNOR. As I say, that report, Mr. Congressman, is something new, and it is a particular question that I have not gone into, and I would have to refresh my memory; but he actually went into the field and made an investigation. The only way we can get at these things is by the actual facts, and whatever they are, let us have the facts. If it is a fact, let us look at it. Dr. Viner did send his men out, made a very careful analysis, and got reports back of a number of applications and why they were rejected and the amount of them, and he follows great detail in it and made his conclusion in that report; and I would like awfully well to refer you to that report.

Mr. WOLCOTT. Yes; I will read it with a great deal of interest. I assume, from your statement, that he came to the conclusion it is due to a lack of demand for the money?

Mr. O'CONNOR. I think that is one of his conclusions. Well, put it in another way, I think my impression from the report was, that there was not as great demand as some people believed.

Mr. WOLCOTT. Following that through, the panacea for all of this seems to be to create a condition of confidence, in which business will get started to borrowing money from the banks and demanding money from the banks for constructive purposes. I will not expect you to answer that, Mr. O'Connor.

Mr. O'CONNOR. I do not know. I am only referring you to the only authentic report that I know of.

Mr. FORD. Could you not send copies of the report to the members of the committee?

Mr. O'CONNOR. It is a very voluminous report.

Mr. WOLCOTT. What is it, a very long report?

Mr. O'CONNOR. Yes, sir.

Mr. HOLLISTER. You have only to read about two pages of it, which is a summary of the thing.

The CHAIRMAN. Do you desire to say anything further right now?

Mr. O'CONNOR. Yes, there was one other section that I thought we ought to give some discussion to, and I want to briefly state that, in our banking law—and as I said, I had not given it consideration until yesterday, but I feel we should not go along without at least one comment on it, and that will conclude my troubles. On page 34, section 18, the bill provides, in title I, 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 purposes of this section and fully provided for all of the obligations of the corporation.

I find some objection, Mr. Chairman, I am sorry to say, to this section, because the Comptroller of the Currency makes a report to Congress, the Federal Reserve Board makes a report to Congress, and this is mandatory upon the Board, and I do not think that we can justify an expense of as much as $50,000 or $100,000 to get that additional information, which is now available through the Federal Reserve and the Comptroller of the Currency, all of which is worked in connection with our board, and I do not believe that section is necessary and I think it would be a useless expenditure of money.

The CHAIRMAN. Mr. O'Connor, before you conclude, there is one matter I would like to draw your attention to for a brief discussion by you, and that is the provision respecting the payment of interest on deposits.

Mr. O'CONNOR. Have you special reference to the act which provides for the elimination of interest on demand deposits?

The CHAIRMAN. Yes.

Mr. O'CONNOR. Now, that is very important, Mr. Chairman, and I am glad you mentioned it. There has been a great deal of discussion about the assessment on banks for the purpose of the Federal Deposit Insurance Corporation. In the Glass-Steagall Act of 1933, you provided that no longer should banks pay interest on demand deposits. I believe that was one of the very serious matters in our banking structure, and I think was a wrong system of banking.

The little depositor never got anything, anyway, and it inured entirely to the benefit of the very large depositor, and it led to such competition between banks for the large banks in their rates of interest.

So you eliminated that by the act of 1933, and I called attention to what that sum amounted to in my address before the American Bankers in Chicago in September 1933, and discussed rather fully that and other provisions of the insurance corporation, and I would like to call attention to that particular point, Mr. Chairman, if you will permit me to put that address in the record.

The CHAIRMAN. We will be very glad to have you do so.

Mr. O'CONNOR. On page 6 of the printed address, I said:

> The elimination of interest on demand deposits will save the banks many billions of dollars. The total amount paid during the past 5 years by member banks on demand deposits was $1,230,242,000, making an average of $246,-048,500 per annum.

And I believe out of the amount we collected from the banks upon the levies of assessments we made—we levied the assessment and they collected one-half of the levies—and I believe it was around $70,000, and here we have just the member banks, because we do not have available the figures on all banks, that the banks have paid out approximately $250,000,000 a year that you prevented them from paying out, is not considered by Congress as good banking. Now, I think that is rather a striking statement.

The CHAIRMAN. Well, if we were to leave the assessments against the member banks, which would amount to $250,000,000 annually to support the deposit insurance fund, we would not have added that burden upon the banks; is that a sound conclusion?

Mr. GIFFORD. What are you going to do with that amount of money?

Mr. HOLLISTER. That is the total?

The CHAIRMAN. Yes; that is the total.

Mr. REILLY. Mr. O'Connor, have you got any report upon any banks in recent years on the service charges that they did not charge some years ago?

Mr. O'CONNOR. No, sir; we have not.

Mr. REILLY. Can you get that report?

Mr. O'CONNOR. I am glad you asked that question, because we have had a great many letters, Mr. Congresman, asking about those matters, and we have no jurisdiction in the Comptroller's office to regulate or to fix in any way those charges. That is a matter entirely at the present with the banks themselves.

Mr. REILLY. Do they not report their income items?

Mr. O'CONNOR. Yes.

Mr. REILLY. Have you not got any idea what they collect for service charges?

Mr. O'CONNOR. Not a separate item, Mr. Congressman; no, not the separate items.

Mr. REILLY. Some of the banks are making some awful charges for handling accounts.

Mr. WOLCOTT. When they are prohibited from paying interest on demand deposits, that likewise carries with it the fact that those funds are more or less static and not being used by the banks for the purpose of making money, yet I do not find any restriction in the act which protects those depositors against their use for long-term investments. Do you not think that would be in keeping with the act, that they do not pay interest on them, but they collect a service charge for handling the accounts, that they maintain a little higher degree of liquidity with reference to demand deposits than they do with respect to time deposits and——

Mr. O'CONNOR. I think that is sound, Mr. Congressman.

Mr. WOLCOTT. In other words, it has been considered unsound banking to invest commercial funds in long-time paper, has it not?

Mr. FORD. Mr. Chairman——

The CHAIRMAN. Just a moment, until Mr. Wolcott gets through, please.

Mr. O'CONNOR. Would you read the Congressman's question?

(Thereupon the reporter read the pending question of Mr. Wolcott.)

Mr. WOLCOTT. Perhaps I should say it should be considered unsound banking to do that.

Mr. O'CONNOR. Yes, that is correct.

Mr. FORD. At the opening of this hearing, Mr. Crowley was in the chair, and I made this statement, and I think that this discussion verifies it, that as a matter of fact, the banks are not paying the insurance premium on the insuring of deposits, but the depositors were paying it, because they have been relieved of paying interest on time or demand deposits.

Mr. REILLY. Mr. Ford, those were the big depositors, not the great mass of depositors.

Mr. FORD. Well, big or little, that is the situation just the same.

Mr. SISSON. Mr. Chairman, if Mr. O'Connor is not coming back here for several days, I think perhaps it might be proper to have him state the witness to whom we may ask these questions, because there is a question I am rather ashamed to ask, but frankly, I have had, I think, four letters from bankers in my district, and they were men in charge, you might say, of the administration of the banks, but they were rather small banks, and I told them that, if they wished to I thought the chairman would give them permission to appear here, and they asked me to bring this to the attention of the committee, in the passage of the act, which is perhaps a more complete revision of the Banking Act, than anything for a long time.

They object to the prohibition against borrowing money by members of a bank, his own bank, because, if they wished to borrow anything, they could go to some other ank and borrow, but because it places them in the category, or a category that seems to them to rather reflect upon them.

The CHAIRMAN. Mr. Sisson, that is a matter of wide interest throughout the country, and of course of interest to the community. Let me suggest to you that there is a provision entitled "III" in this bill dealing with that particular matter, and it will come up for discussion when we reach it; and I might say, in that connection, you might advise your friends that we are attempting, and we expect, if the legislation passes, to liberalize that provision of the law.

Now, gentlemen, I am going to suggest, if you are through with Mr. O'Connor, we will meet again at 10:30, Monday morning, and Mr. Eccles will appear before the committee at that time.

Mr. MEEKS. Mr. Chairman, may I ask a question?

The CHAIRMAN. Yes.

Mr. MEEKS. Mr. O'Connor, are you putting your Chicago speech in the record?

Mr. O'CONNOR. Yes, I can do so.

Mr. MEEKS. I wonder if you have copies available that you can pass to the members? I would very much like to have a copy in advance, because we may not get to see it soon.

Mr. O'CONNOR. Thank you, Mr. Meeks.

(The address of Mr. O'Connor is as follows:)

ADDRESS BY J. F. T. O'CONNOR, COMPTROLLER OF THE CURRENCY, BEFORE THE CONVENTION OF THE AMERICAN BANKERS ASSOCIATION, AT CHICAGO, ILL., SEPTEMBER 7, 1933

Our common purpose justifies the acceptance of your gracious invitation. In this my initial appearance before the American Bankers Association, if some slight suggestion can be made to strengthen the financial structure of the Nation, my effort will be fully compensated. At your last annual convention had anyone predicted that every banking institution would be closed for several days, credit paralyzed, and tickers silenced, ridicule, sharp criticism, and condemnation would have greeted the suggestion. It happened. The old order had completely broken down. Will such a condition reoccur?

No finer example of patience and self-restraint can be found in our history than was exhibited by our people in these black days of March. With the storm raging in mad fury, with destructive waves breaking over the deck, a firm hand grasped the wheel, changed the course, substituted hope for despair, and arrived safely in the harbor. Other storms will come, no one will deny. Possibly we cannot prevent the storm, but we can build a ship the elements cannot destroy. The challenge is yours. The thrill of the opportunity appeals to us all.

Probably no provisions in the Banking Act of 1933, sometimes called the Glass-Steagall Act, have attracted so much attention as the insurance provisions. It is my sincere belief that the future of American banking rests in a large measure on proper and courageous management and the adoption of sound policies in the administration of the insurance provisions of the act. Fully realizing the magnitude of the operations involved, the pitfalls which must be avoided, and the nondiverging path which must be followed, as one member of the board of the Corporation, I approach the task humbly but with a grim determination of success.

The principle of guaranteed deposits is not new. Our Government established this on June 25, 1910, when President William Howard Taft advocated and secured the passage of the Postal Savings bill. Some deny this is an insurance or a guarantee. Let us not quibble about words. No one denies that the full faith and credit of the United States is pledged to the return of every dollar in the Postal Savings banks. Today our Government guarantees, or insures or promises, to return approximately $1,184,948,200. No one questions the ability of the Government to pay these deposits. The growth of these deposits during the past 2 years is interesting, if not alarming. Let me give them:

June 30, 1931	$347, 416, 749
June 30, 1932	784, 819, 402
April 30, 1933	1, 159, 794, 016

As already noted, the estimate for June 30, 1933, indicates an increase over April 30, 1933, of $25,154,184. No comment to bankers is necessary on these figures. Even a lawyer appreciates their significance. The Government requires security from the banks to insure these deposits. In this manner the banks guarantee their safe return. The postal depositor becomes a preferred creditor. The ordinary depositor in the bank is merely a creditor. Unlike a story I heard some time ago: A creditor called the president of a large corporation and said, "I see we're in the bosom of a receiver." The president corrected him saying, "You mean the hands." "Well, I do not know about such things." "Oh, don't worry, you are a preferred creditor." "A preferred creditor, am I? What does that mean?" "It means you know now you won't get anything while the common creditor won't know for a year or more."

No individual is permitted to deposit over $2,500 in the Postal Savings bank. There has been a growing demand from all parts of the country to permit unlimited deposits. If nearly $1,190,000,000 has been deposited in Postal Savings under a $2,500 limit, what would the deposit be if the individual deposit were unrestricted? When the insurance feature of the Glass-Steagall bill becomes operative, most of this huge sum should find its way back into the banks. Indeed, Congress would be justified in repealing the law entirely.

Let me briefly outline a few of the main provisions of the Banking Act of 1933 on this subject:

1. The Corporation has three directors: The Comptroller of the Currency and two directors, appointed by the President, who shall not be of the same political faith.

2. A "temporary Federal deposit insurance fund" will become operative on January 1, 1934, which will insure deposits in each member of the fund up to $2,500. Members of the fund will be all member banks licensed before January 1, 1934, by the Secretary of the Treasury and nonmember State banks with the approval of the State supervising authority, after certification to the Corporation of solvency and examination and approval by the Corporation. Both member and nonmember banks must pay to the Corporation an amount equal to one-half of 1 percent of the insured deposits certified as of the 15th of the month preceding the month they were admitted to the fund. One half of this payment will be made upon admission and the other half upon call by the directors of the Corporation.

3. The permanent insurance is effective on July 1, 1934, as to all national banks certified by the Comptroller of the Currency and all State member banks certified by the Federal Reserve Board upon such banks becoming class A stockholders in the Corporation, and nonmember banks have the benefit of such insurance until July 1, 1936, by becoming class A stockholders of the Corporation in compliance with the terms of the act.

4. In becoming class A stockholders, the banks must apply to the Corporation for class A stock in an amount equal to one-half of 1 percent of its total deposits

as computed in accordance with regulations of the Federal Reserve Board, with certain exceptions in the case of banks organized after July 1, 1934. One-half of the amount due for the stock shall be paid into the Corporation upon admission and one-half upon call by the directors of the Corporation.

5. Under the permanent insurance features of the act, net deposits are insured as follows:

One hundred percent not exceeding $10,000.

Seventy-five percent of the amount exceeding $10,000 but not exceeding $50,000, and

Fifty percent of the amount exceeding $50,000.

You will be interested in the progress made to date:

The Government, through the cooperation of the Federal Reserve banks, the Comptroller's Office, and the Reconstruction Finance Corporation, is making a survey of all the banks in the United States. The President called the attention of the governors of the various States to the provisions of the Banking Act of 1933 in a letter dated July 6. The letter was as follows:

MY DEAR GOVERNOR: You have no doubt given serious consideration to the provisions of the Glass-Steagall bill, known as the "Banking Act of 1933", which was approved by me on June 16, 1933.

This act contains far-reaching provisions with reference to State banks. In a very short time, to wit, January 1, 1934, certain State banks which secure a certificate of solvency from the proper State banking authority, and which after examination are found satisfactory to the Federal Deposit Insurance Corporation, will be admitted to the benefits of the insurance fund.

In order that State banks may receive the benefits of the act, it will be necessary in many States for additional legislation; in others, amendments to existing laws, and in others, constitutional changes. You will appreciate the necessity of immediate action in order that the benefits of this act will be as widely distributed as possible.

May I suggest to you that you call together representatives of your State banking department, together with leading State bankers, to discuss with you the necessary legislative changes or constitutional amendments to bring about the desired effect.

I call your particular attention to the following paragraph of the Banking Act of 1933, which is found under subsection (y) of section 8 (last paragraph), which reads as follows:

"It is not the purpose of this section to discriminate, in any manner, against State nonmember and in favor of National or member banks; but the purpose is to provide all banks with the same opportunity to obtain and enjoy the benefits of this title. No bank shall be discriminated against because its capital stock is less than the amount required for eligibility for admission into the Federal Reserve System."

Thanking you for prompt consideration of this matter, I beg to remain,

FRANKLIN D. ROOSEVELT,
President.

The general outline of the set-up of the Corporation has been tentatively approved by the President. I am in possession of the names of over 1,500 qualified men who are available to make examinations. These names have been submitted by the State banking commissioners and others, and they are qualified examiners who have had 5 years or more banking experience and who known the values in the States. Arrangements have been made with the Treasury for the necessary funds to carry out the preliminary work of the Corporation. Our first task is the examination of approximately 8,000 State nonmember banks which are on an unrestricted basis. I shall make the following suggestions to the Board immediately upon reorganization:

First, that each bank applying for insurance be furnished with blank forms to be completed by the banks setting forth each asset under a proper heading and the amount of its deposit liabilities and obligations to other creditors. This will save much time and the examiner will then check the item and appraise the same.

Secondly, that an examiner who knows the values in the particular State, with necessary assistants, be assigned to each State capital to work with the banking commissioner and all examiners in the State clear through the examiner at the capital. In this way the work will be decentralized. It is my belief that whenever a piece of work can be done in a State just as well as at the National Capital, it should be done in that State.

Thirdly, that the names of the banks insured and their location be given simultaneously.

There has recently been sent out to many of the banks of the country a letter in reference to the Federal Deposit Insurance Corporation from which I quote two sentences as follows:

"In the parlance of the street, the independent bank is to be 'ironed out.'"

"Powerful influences are at work to wipe out the small banks and the independent banker has been placed on the defensive."

I know of no more vicious, unwarranted, and untruthful propaganda. The present administration has demonstrated its policy of protection for the little fellow, whether individual or corporate. At a conference with the President on Tuesday afternoon, he authorized me to say to you, and through you to the country, that the object of the insurance provisions of the new bank act was to insure as many nonmember banks as possible. He discussed the details of the act with an amazing knowledge of its provisions. He discussed real values, appraised values, and liquidating values with a fine discrimination. "Injustice must be avoided." In that sentence, the Chief Executive summarized all his comment and direction.

No greater demand came from the people during the past session of Congress than that some form of guarantee or insurance for deposits be passed. The fact that the bill passed the House with but six dissenting votes and passed the Senate without a dissenting vote is evidence of the demand. It could not be ignored. Whether we favored the provision or opposed it, bank insurance is part of the Federal law. Let us examine some of the higher grounds which possibly justify its existence:

First, every depositor in theory has a right to his money. This law makes the theory a fact.

Second, it will banish the fear in every banker's mind of runs upon his bank. We should not again witness the very serious crisis which developed with the beginning of 1933 and which produced grave runs on practically every bank in the country, culminating on March 4 with currency demands amounting altogether to $1,630,000,000. This huge sum was withdrawn in cash by panic-stricken depositors.

Third, it will obviate the necessity for a postal savings bank and return to the banks over a billion in deposits.

Fourth, it will permit an extension of credit and a modification of cash reserves. This will particularly benefit small country banks and their customers. Liquidity means immediate marketability. The average town or small city has sound values but not a high degree of liquidity. Probably nothing in banking parlance has been so much misunderstood as the term "liquidity." The law provides that a certain percentage of a bank's assets shall be in cash and sound banking requires other assets to be liquid. Some well-meaning individuals and other demagogic persons have aroused communities because banks with frozen assets have not been permitted to reopen. They say while certain securities are not worth much today they will be worth face value in 5 or 10 years. If the depositor would accept this viewpoint and take a mortgage or a bond worth $500 for his deposit of $1,000 on the theory that the security would be worth $1,000 in a few years, our problem would be simple. The depositor may rightly demand his entire deposit in cash.

Fifth, the elimination of interest on demand deposits will save the banks many millions of dollars. The total amount paid during the past 5 years by member banks on demand deposits was $1,230,242,000, making an average of $246,048,500 per annum. Again the Federal Reserve Board fixes the rate of interest paid by member banks on time deposits. Is there any depositor who would not accept one-half of 1 percent less interest and know his deposit was insured, if such a step were necessary to save the insurance provision? Would any nonmember bank not cooperate to this extent? No depositor would object to paying two and one-half or up to five dollars to insure a $1,000 deposit. Besides, the United States Government is contributing $150,000,000, and approximately $139,000,000 will be contributed by the Federal Reserve banks, in addition to the one-half of 1 percent by the banks.

Sixth, now a point not generally discussed and offered here as a matter of opinion. It is my firm opinion that the insurance features of the law will save millions to our people. The high pressure and not too scrupulous salesman often plants the seed of suspicion as to a bank's solvency in the prospective purchaser's mind. The life savings of men and women have been withdrawn and invested in worthless securities or enterprises because of this fear. When the

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suspicions becomes a belief, the confidential relation between the banker and the depositor is destroyed. The very fact that the honest, highly trained, conservative banker has made errors in making investments is proof of the great danger of loss by those not trained in making investments.

The insurance feature of the bill differs from laws heretofore passed in two main respects, first, the participation of the United States Government in making a substantial investment in the capital structure, and secondly, in recognizing the sound insurance feature that risks should be spread over a large territory and not localized.

The test of admission of a bank to the insurance fund is determined upon its ability to pay all of its liabilities to depositors and other creditors, as shown by the books of the bank. In other words, the assets must be sufficient to accomplish this purpose (sec. 12B(e)). Information gathered from 4,836 national banks at the close of business on May 13, 1933, showed that 96.76 percent of the total depositors in national banks had deposits of under $2,500. The survey further showed that the average deposit was $183.17, and that these 96.76 percent, totaling 21,748,754 depositors, had 26.72 percent of the total deposits in the national banks as of that date, while 0.13 percent of depositors, totaling 28,356, had deposits of over $50,000, or 40.29 percent of the total deposits, which represented an average deposit of $211,820.85. It must be remembered that the deposits of over $50,000 represent deposits of State governments and their subdivisions as well as the large corporations of the Nation. No effort was made to distinguish between individual and corporate deposits.

The President has authorized me to give you the names of the men he has selected as directors of the Federal Deposit Insurance Corporation. The law requires that one of these members be a Democrat and one a Republican. The Comptroller of the Currency is named by law as the third member of the Board.

As the Democratic member, the President has selected Walter Joseph Cummings, of Chicago. Mr. Cummings is at present executive assistant to the Secretary of the Treasury of the United States. He was appointed by Secretary William H. Woodin on April 8, 1933. He was born in Chicago, Ill., on June 24, 1879, and is the son of Walter J. Cummings and Mary Cummings, of Chicago. He attended the Chicago public schools and Loyola University. In 1902 he entered the plant of the Cummings Car & Coach Co. at Chicago, Ill., for the manufacture of cars and trucks, acting as secretary and treasurer. In 1907 he became vice president of the company, and in 1918 was elected president of the Cummings Car & Coach Co. He also holds many important directorships, including the American Car & Foundry Motors Co., of New York; J. G. Brill Co., of Philadelphia; and is president of the Chicago & West Towns Railway Co., of Chicago; the Chicago & Calumet District Transit Co., of Chicago; and the Des Moines Railway Co., of Des Moines. Mr. Cummings was appointed by the Governor of Illinois in January 1933 as commissioner of Lincoln Park, Chicago. He has been identified with and acted in many civic organizations of Chicago, and at the present time is a trustee of Loyola University, a member of the executive committee of the Associated Charities of Chicago, and has taken a deep interest in the civic betterment of the city. He had conferred upon him the honorary degree of doctor of laws by Loyola University.

The delay in making the appointments on this Board was no doubt caused by the selection of the next member. As I have stated, the law requires that one of the members shall be a Republican, and the President had considerable difficulty in finding a Republican. Mr. E. G. Bennett, of Ogden, Utah, has been appointed by the President.

Mr. Bennett was born in York, Nebr., on April 23, 1888. He received his early training under Judge George W. Post, who controlled 12 banks in eastern Nebraska now operated by the McLeod interests. He was employed for 8 years by J. S. & W. S. Kuhn, Inc., who built irrigation, power, and other projects in the Snake River Valley of Idaho, and then became vice president and general manager of the First National Bank of Jerome, Idaho, and the Jerome Loan & Trust Co. During this period he made loans for Holland interests, loaning approximately $1,500,000 on irrigated farms in Snake River Valley. He acted as secretary of the Idaho agency of the War Finance Corporation, loaning $6,000,000 on livestock without loss. During the past 6 years and at the present time, Mr. Bennett has devoted his time to the Eccles and Browning interests in the capacity of vice president and general manager. These interests own and operate 28 banks in Utah, Idaho, and Wyoming, all but 3 of which are State banks. For the 4 years from 1924 to 1928, Mr. Bennett was a member of the executive council of the American Bankers Association, representing Idaho. In 1923 he was appointed by the Governor of Idaho with two others to the Bank Code Commission. The code prepared by the commission was adopted by the legislature in 1925. In the preparation of this code an exhaustive study was made of all the banking laws of all the States.

Some of Mr. Bennett's other connections are—president of J. M. & S. M. Browning Co.; president Browning Arms Co.; president Lindsay Land & Livestock Co., which company owns a 130,000-acre ranch (18,000 ewes and 4,000 cattle); president Lion Coal Corporation operating mines in Utah and Wyoming; president Eleventh Regional Agricultural Credit Corporation (Utah, Nevada, Arizona, and California).

Mr. Bennett's companies do not owe any money to anyone. His banks and companies are in excellent financial condition. No man knows better the problems of the State banker than Mr. Bennett. He will bring to the Board a sympathetic understanding of all those bankers who have assisted in building the West. No man has a better knowledge of the present banking situation in the country than Walter J. Cummings. For 5 months he has devoted his time at great personal loss to assist in rehabilitating the banking structure. He was drafted into the service by his close personal friend and business associate, Hon. William H. Woodin, Secretary of the Treasury. His experience in handling large financial problems makes him a valuable member of the Board. He knows the Treasury and all of its departments. This insures us that there will be no delay in getting the machinery in motion. These two sound and successful business men the President has called to a difficult task. All we ask is a fair trial.

There are several features of the Banking Act of 1933 which have raised innumerable questions of interpretation and of administration in which you may be interested. First and foremost are the problems which have arisen in connection with affiliates as definied by the Banking Act of 1933. The definition of affiliates of member banks as laid down by the act is very broad and technical and a literal interpretation of the law may lead to many situations which could not be foreseen and which I doubt the framers of the act meant to bring about. Let me give you a few illustrations:

We have a national bank, 96 percent of the stock of which is owned by a packing company. The packing company is a holding company affiliate. This corporation in turn owns or controls 200 other corporations scattered throughout the world. Is each one of these 200 corporations also an affiliate of a national bank? The national bank is required under the act to furnish report of its affiliates and to publish the reports of its affiliates under the same conditions as govern its own condition reports. I venture to state that the depositors of this national bank will be somewhat mystified by the publication of the reports of the 200 corporations.

The majority of stock of another national bank is owned by a church, a corporation sole. The church is an affiliate. It in turn has furnished all or part of the funds for other church buildings, a hospital, orphans' home, and other charitable institutions in a particular State, all incorporated and controlled by the first church. Are all of these institutions affiliates of the bank? Must the bank furnish the statements of these institutions and publish them?

A bank had as collateral to a loan the majority of stock of a hosiery corporation and foreclosed on the collateral to protect itself, thus becoming the owner of the stock. Is the hosiery corporation an affiliate? If it is, the bank cannot make a loan to it except on collateral which the corporation does not have and since the corporation is unable to borrow from other sources, the bank cannot protect itself.

There are but three illustrations of the thousands of problems which arise in connection with affiliates, and the Attorney General of the United States has been asked for his opinion with respect to some of these problems.

The Banking Act of 1933 provides in part:

"No executive officer of any member bank shall borrow from or otherwise become indebted to any member bank of which he is an executive officer."

Violation of the prohibition is a criminal offense. No definition of "executive officer" is given in the act. The question of what is an "executive officer" immediately faced the banks and the examiners. No ruling on a criminal statute by my Department would protect the banks. The opinion of the Attorney General was requested. He has advised that: "It is not the designation under which one is known, but the nature of his duties which characterizes him as an "executive officer." *Small* v. *Gibbs Press*, 225 N. Y. S. 141, 142."

He further stated: "It is the duty of the banks and of all officers who by any possibility might be affected to keep within the statute and to weigh carefully all the facts and circumstances (peculiarly within their provision) before acting."

He refers with approval to the statement in *Arkansas Amusement Corporation* v. *Kempner* (33 S. W. (2d) 42) to the effect that:

"An executive officer or employee is one who assumes command or control and directs the course of the business, or some part thereof, and who outlines the duties and directs the work of subordinate employees, as usually provided for in the articles of association, the bylaws, or a resolution of the directors.'

The practical administration of this section of the Banking Act of 1933 from an examining standpoint requires the Comptroller's Office to take the position that the following officials of a bank will de deemed, prima facie, to be "executive officers" for the purposes of said section, it being understood that such presumption may be rebutted on a sufficient showing: The president, a vice president, the cashier, an assistant cashier.

The facts in any given case may, as indicted by the opinion of the Attorney General, constitute other officers or employees, "executive officers" within the scope of the act.

It, of course, would be more satisfactory to have the definition of "executive officer" laid down by Congress, especially when, in weighing facts, one has a penal statute involved.

The section of the Banking Act with respect to extension of branch banking for national banking associations outside of the limits of the city, town, or village in which the association is situated, has raised some problems, particularly the language: "* * * If such establishment and operation are at the time authorized to State banks by the statute law of the State in question by language specifically granting such authority affirmatively and not merely by implication or recognition, and subject to the restrictions as to location imposed by the law of the State on State banks."

Under the wording of this provision of the Banking Act, national banks are not permitted to have branches outside of the city, town, or village in which they are located in some States where State banks are permitted to establish such branches. Two outstanding cases are those of Maryland and South Carolina, where nonmember State banks may establish branches, but member banks, whether National or State, may not establish branches under the wording of this particular statute. In connection with the establishment of branches, it was of course, stated before the act was passed by many that there would be a great rush for branches and they would be established rapidly. The statute became effective on June 16 of this year; practically 3 months have elapsed since its enactment. Only 37 branches of national banks have been established under its provisions. Of this total, 9 branches were established in communities which were without banking facilities, 2 branches were established for the purpose of taking over banking institutions in the hands of conservators, 12 were established to take over going institutions, and 8 were established to replace 8 branches of State banks taken over by a national bank. Accordingly, only 9 branches represented new banking facilities.

There is not time to go into all of the various problems which have arisen under the Banking Act of 1933, but I have given you a few illustrations which should be of interest.

There seems to be a great deal of misunderstanding by banks and the public generally with respect to receiverships of national banks. These statements are being made repeatedly:

"1. Receivership means all assets thrown on the market at once—forced liquidation."

In the first place it is obviously impossible to throw the assets on the market at once and, even could it be done, it would be poor policy. The Comptroller acts in a trustee capacity and his duty is to realize as much as possible for creditors. The average time required to fully liquidate a receivership is 5½ years.

"2. Receivers get commissions—expenses are heavy and eat up the trust."

The facts are that receivers of national banks are not paid any commission but a flat salary and the average salary is around $350 per month, varying as to the size of the receivership; and since one receiver in many cases handles more than one bank, the average salary per bank is about $1,713 per annum.

The total average cost of liquidation last year was but 3.2 percent of actual collections and the average for fully liquidating all banks in the past has been 3.9 percent of book value and 6.65 of actual collections.

I desire to touch for a few minutes upon the growth and work of the Comptroller's Office, as now constituted, as compared with the past. It is interesting to note from the first report of the Comptroller of the Currency to Congress, dated November 28, 1863, that there were 134 national banks and that the personnel of the Comptroller's bureau consisted of 8 persons, including the Comptroller. In 1865 the Comptroller reported 1,601 national banks with the personnel of the bureau 77 in number. It may be rightly said that those were the good old days with few problems. Let us see the condition in 1893—a panic year. Quoting from The Romance and Tragedy of Banking, by T. P. Kane, former Deputy Comptroller of the Currency:

"Every hour of the day and late into the night telegram after telegram was received announcing additional suspensions of banks or new complications which had to be promptly met. As many as 30 suspensions occurred in a single day, and for a time it looked as if every national bank in the system would succumb."

The Comptroller of the Currency that year in his report to Congress stated that 154 national banks suspended, receivers being appointed for 65. Problems? Yes, but today we face trust departments, savings departments, bond departments, affiliates, preferred stock, organizations, reorganizations, bond depreciation, other real estate, banks in conservatorship, and 1,123 banks in the hands of receivers. In touching on these 1,123 receiverships, the old story of the borrower who asked the banker if he had ever been in the pants business and, upon receiving the answer "No", stated: "Well, you are in it now", is certainly applicable to banks in receivership. I find that among the enterprises the Comptroller of the Currency is directing are: Hotels; coal mines; quarries; lumber manufacturing; vineyards; apartment houses; office buildings; farming; raising sheep and cattle; growing cotton, pecans, and citrus fruits; operating pickle factories, cold-storage plants, motor freight terminals, and a railroad. Incidentally, the railroad is operating at a profit.

At the present time in the Comptroller of the Currency's Office there are 216 national examiners, 297 assistant examiners, and 156 other employees; in the Reorganization and Conservators Division there are approximately 305 employees; and 271 employees in the Insolvent Division, not including receivers, conservators, their employees, or their attorneys. Besides using all available space in the Treasury Building, it has been necessary to secure the major part of a large modern office building opposite the Treasury.

A picture of what has been achieved in giving relief to depositors by the various governmental agencies is presented by the following figures:

On December 31, 1932, deposits in national banks amounted to approximately $18,500,000,000. On March 16, 1933, the frozen deposits in unlicensed national banks amounted to $2,200,774,000, representing approximately 12 percent of the aggregate amount of deposits on December 31, 1932. On September 5, 1933, frozen deposits in unlicensed national banks amounted to $746,731,000, representing 4 percent of deposits as of December 31, 1932. If we deduct the amount of frozen deposits of $440,099,000 which will be released immediately upon the consummation of the approved plans, the total amount of frozen deposits in unlicensed national banks will be $306,632,000, or 1.66 percent of the total amount on deposit on December 31, 1932.

On March 4, 1933, there were 5,938 operating national banks in the United States. Of this number, 4,509 were licensed to resume normal banking functions on March 13, 14, and 15, leaving 1,429 national banks unlicensed as of the beginning of business March 16. Within 174 days there have been 423 old banks licensed, 100 new banks chartered, and 372 plans of reorganization approved.

I desire to reaffirm what I stated in my address over the National Broadcasting System from Washington on July 19:

"No discrimination has been made between Republican dollars and Democratic dollars in closed banks. My department has assumed that the Republican depositor, although probably much less in need of his money than his Democratic friend, is just as anxious to get his share of the remaining 5 percent now in closed national banks. Of the many hundreds of depositors, creditors, stockholders, and officers with whom I have discussed plans of reopening, I have never inquired and do not know the politics of any. Let me say definitely and positively that the Comptroller of the Currency is interested in your plans for reopening of your bank and giving relief to the depositors and not in your politics. There have been some fine illustrations of self-sacrifice and true Americanism by officers and stockholders of many banks. Men and women have come forward and volunteered their 100 percent assessment, waived their deposits, subscribed for new capital, in order that the depositors should not lose a single dollar. I mention this because some are prone to mention only those connected with the banks who have tried to evade their legal and moral responsibility and have been compelled by legal proceedings to make their just contribution."

In conclusion, let me say that as politics have never entered into the consideration of any plan for reorganizing or reopening or the establishment of any bank or branch in any of the divisions of the Comptroller's Office, can I ask you to bear with me in the solution of difficult problems in the same spirit. In the great divine scheme of life, as individuals we play our part and pass on. Our places can be filled without the slightest interruption in the march of progress. My purpose is to serve a great country with my limited ability. If uncounted hours in the day and long into the night will bring forth a better understanding between my Department and the people, will make for a more permanent banking structure, the effort will not be counted in vain. Let us bring cold figures to life. Let us put a heart back into banking and let profits be subservient to service. Let us bring a great profession back to the leadership it once enjoyed. Let the inspiration of the names of great bankers of the past—men who tossed their fortunes into their country's exchequer to save its credit and win its wars—touch the inner recesses of our souls that we may imitate and serve.

(Thereupon, a recess was taken in the hearing until Monday Mar. 4, 1935, at 10:30 a. m.)

BANKING ACT OF 1935

MONDAY, MARCH 4, 1935

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

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

The Chairman. Gentlemen, we have with us this morning Governor Eccles of the Federal Reserve Board, who will discuss title II of H. R. 5357, and I think Governor Eccles would like to proceed without interruption until he shall have concluded a preliminary discussion of the bill, after which, of course, he will be glad to answer any questions and furnish any information that may be desired by members of the committee.

Governor Eccles, we shall be glad to have you proceed in your own way for such time as you desire, without being interrupted.

STATEMENT OF GOV. MARRINER S. ECCLES, OF THE FEDERAL RESERVE BOARD

Mr. Eccles. I am sorry that I do not feel entirely up to par today. I have been laboring under a rather heavy cold. I had thought, at first, to make a rather extended verbal statement with reference to the legislation. I decided, however, on account of the way I feel, to make a brief written statement of the general outline of the legislation. I believe this will in a general way cover the philosophy underlying section 2 of the bill.

The Chairman. Title II?

Mr. Eccles. Title II of the bill. So that I will just proceed to read this statement, if I may.

In recommending banking legislation at this time, it is recognized that the Congress has before it an unusual number of urgent matters that are engaging its attention, and that legislation in order to deserve your consideration at this session must not only be important in general but must also be urgent at this particular time.

We are not unmindful of the fact that within the past 2 years you have passed the Emergency Banking Act, the Banking Act of 1933, the Securities Exchange Act, and other important pieces of legislation dealing with banks. One purpose of this legislation has been to meet emergency conditions, and it is now proposed to incorporate into permanent legislation the features of the emergency laws that have proved to be valuable.

Another purpose of recent banking legislation, and particularly of the banking bill of 1933 and of the portions of the Securities

Exchange Act that deal with powers of the Federal Reserve Board, has been to prevent the recurrence of speculative excesses which preceded the recent break-down of our banking machinery and were partly responsible for this collapse. These bills were largely inspired by the difficulties that came to a head in 1928 and 1929, and it is gratifying to know that we now have on our statute books measures that will go far toward preventing the recurrence of conditions such as prevailed during the speculative orgy of these years.

At the present time, however, there appears to be no immediate danger of excessive speculation. The present need is to so modify our banking law as to encourage the banking system to give a full measure of cooperation to efforts at economic recovery. It is even more important from the longer time point of view to so modify our banking structure and administration as to have it become an influence toward the moderation of fluctuations in employment, trade, and business. This would tend not only to avoid the particular evils that came to a head in 1928 and 1929, but to so regulate underlying conditions as to diminish the possibility of a speculative boom getting under way. For when speculation is once under way it is extremely difficult to control, and the only means of preventing excesses is to combat conditions that are favorable to their inception and early development.

In order to accomplish this it is necessary to improve our machinery of monetary control, which is the principal objective of title II of the proposed bill.

More specifically these objectives are to increase the ability of the banking system to promote stability of employment and business insofar as this is possible within the scope of monetary action; as a necessary step in that direction, to concentrate the authority and responsibility for the formulation of national monetary policies in a body representing the Nation; to modify the structure of the Federal Reserve System to the extent necessary for the accomplishment of these purposes, but without interfering with regional autonomy in matters of local concern; and finally to relieve the banks of the country of unnecessary restrictions that handicap them in the proper performance of their functions and thus to enable them to contribute more effectively to the acceleration of recovery.

In my opening remarks I wish to direct your attention particularly to four proposals incorporated in title II of the bill. Other provisions of the bill I wish to leave for your consideration, with the understanding that I shall be glad to answer any questions that you may wish to ask about them.

The four questions which I wish to discuss this morning are: (1) The proposal to combine the offices of chairman of the board of directors and governor of the Federal Reserve banks, and to have the appointments to this combined office subject to approval by the Federal Reserve Board (sec. 201 (1), pp. 38–41); (2) modification of the machinery for determining open-market policies of the Federal Reserve System (sec. 205, pp. 43–44); (3) transfer of the determination of eligibility requirements from the statute to the Federal Reserve Board (sec. 206, pp. 45–46); and (4) liberalization of provisions relating to real-estate loans (sec. 210, pp. 49–51).

1. COMBINING GOVERNORS AND CHAIRMEN

As you know, the present law provides that the Federal Reserve Board appoint 3 directors of each Federal Reserve bank and that 1 of the directors appointed by the Board be the chairman of the board of directors. It appears to have been the intention of the framers of the Federal Reserve Act that the chairman of the board of directors be the principal executive officer of each bank and the law makes him also the official representative of the Federal Reserve Board at the bank. In practice, however, it has developed that the directors appoint an executive officer for whom they have adopted the title of governor of the Federal Reserve bank, a title that is not mentioned in the law, and that these governors have become the active heads of the Federal Reserve banks.

The proposal in the bill is to recognize the existing situation by giving the governor of a Reserve bank a status in the law and to combine his office with that of the chairman of the board of directors. It is, of course, essential that the holders of these combined offices be approved by the Federal Reserve Board. The Board, you will note, will no longer appoint a chairman of the board, but will merely have the power to approve or disapprove the appointment of the governor, who will also be chairman of the board. In this proposal there is no encroachment on the autonomy of the individual Reserve banks. It merely reestablishes the original principle of the Federal Reserve Act that the Federal Reserve Board, which has responsibility for national policies and for general supervision over the Reserve banks, shall be a party to the selection of the active heads of the 12 Reserve banks. This change will work towards smoother cooperation between the Board and the banks and will establish within the banks a greater unity of administrative control than now exists. It will also result in considerable saving through the elimination of one of the two highest officers in each Federal Reserve bank.

2. OPEN-MARKET OPERATIONS

From the long-time point of view the recommendations dealing with changes in the machinery for determining and carrying out the open-market policies of the Federal Reserve System are essential. Open-market operations are the most important single instrument of control over the volume and the cost of credit in this country. When I say credit in this connection I mean money, because by far the largest part of money in use by the people of this country is in the form of bank credit, or bank deposits. When the Federal Reserve banks buy bills or securities in the open market, they increase the volume of the people's money and lower its cost; and when they sell in the open market, they decrease the volume of money and increase its cost. Authority over these operations, which affect the welfare of the people as a whole, must be vested in a body representing the national interest.

Under existing law open-market operations must be initiated by a committee consisting of representatives of the 12 Federal Reserve banks, that is, by persons representing primarily local interests.

They must be submitted for approval or disapproval to the Federal Reserve Board, and after they have been approved by the Federal Reserve Board, the boards of directors of the Federal Reserve banks have the power to decide whether or not they wish to participate in the operations. We have, therefore, on this vital matter a set-up by which the body which initiates the policies is not in a position to ratify them; and the body which ratifies them is not in a position to initiate them or to insist on their being carried out after they are ratified; and still a third group has the power to nullify policies that have been initiated and ratified by the other two bodies. In this matter, therefore, which requires prompt and immediate action and the responsibility for which should be centralized so as to be inescapable, the existing law requires the participation of 12 governors, 8 members of the Federal Reserve Board, and 108 directors scattered all over the country before a policy can be put into operation.

It requires no further explanation to show that the existing machinery is better adapted to delay and obstruction than it is to effective operation, and that it results in a diffusion of responsibility which prevents the necessary feeling of complete authority and responsibility by a small group of men who can be held accountable by the Congress and the Nation for the conduct of this matter that is of national importance.

The proposal in the bill is to set up a committee of 5, 3 of whom shall be members of the Federal Reserve Board and 2 governors of Federal Reserve banks. This proposal would have the advantage of creating a small committee with undivided responsibility. It is not clear, however, that this arrangement is the best that can be devised for the desired purpose. The Federal Reserve Board, which is appointed by the President and approved by the Senate for the purpose of having general responsibility for the formulation of monetary policies, would under this proposal have to delegate its principal function to a committee, on which members of the Board would have a bare majority, while governors of the banks would have 2 out of 5 members.

From the point of view of the Board the disadvantages of this arrangement are that a minority of the Board could adopt a policy that would be opposed to one favored by the majority. It would even be possible for one member of the Board by joining with the two governors to adopt a policy that would be objectionable to the seven other members of the Board.

The placing of this authority in such a committee would also have the disadvantage of giving one important power, the power of open-market operations, to the open-market committee, while other fundamental powers are vested in the Board. These powers could be utilized to nullify the actions of the open-market committee. For example, the committee might adopt a policy of easing credit, while the Federal Reserve Board would be in a position to tighten credit, either by raising discount and bill rates or by increasing member-bank reserve requirements. Also the Board, through its power of prescribing regulations for open-market operations, could conceivably interfere with the carrying out of the policies of the committee. While it is not contemplated that such extreme situations would occur, it does not seem desirable to amend the law in a manner that might result in such unreasonable developments.

Upon further study it would appear that the best way in which to handle this proposal would be to place the responsibility for open-market operations in the Federal Reserve Board as a whole and to provide for a committee of five governors of Federal Reserve banks to advise with the Board in this matter. The Board should be required to obtain the views of this committee of governors before adopting a policy for open-market operations, discount rates, or changes in reserve requirements.

Such an arrangement would result in the power to initiate open-market operations by either a committee of the governors or by the Board, but would place the ultimate responsibility upon the Federal Reserve Board, which is created for that purpose. In this connection I should like to quote President Woodrow Wilson, who in his address to the joint session of Congress on June 23, 1913, said:

> The control of the system of banking and of issue * * * must be vested in the Government itself, so that the banks may be the instruments, not the masters, of business and of individual enterprise and initiative.

3. ELIGIBILITY OF PAPER

It is proposed to give the Federal Reserve Board authority by regulation to determine the character of paper that may be eligible as a basis of borrowing at the Federal Reserve banks. This is particularly important at this time because it would encourage member banks to pay less attention to the form and maturity of paper that is offered by would-be borrowers and to concentrate their attention on the soundness of such paper. At present many banks are unwilling to extend loans to borrowers who have assets that are unquestionably sound because they lack the assurance that in case of a withdrawal of deposits they would be able to liquefy these assets at the Federal Reserve banks.

In times of emergency it has been necessary to remove existing restrictions and to give discretion in the matter to the Federal Reserve authorities, as was done under the Glass-Steagall Act of 1932. This act, however, was passed after a great many banks had gone to the wall at least partly because of lack of eligible paper and its provisions insofar as they relate to borrowing from the Reserve banks, have now expired. I think they expired yesterday.

What is proposed is not, as has been sometimes alleged, a policy of opening the doors of the Federal Reserve banks to all kinds of paper, regardless of its soundness. On the contrary, it is proposed to place emphasis on soundness rather than on the technical form of the paper that is presented.

Experience under emergency laws shows that the Federal Reserve banks and the Federal Reserve Board have exercised caution and, though they have extended credit on ineligible assets to the extent of $300,000,000, all but $1,500,000 of this has been paid back and the banks have suffered no considerable losses. It would appear safe, therefore, to intrust discretion in the matter to the Federal Reserve Board, which is always in session and, therefore, in a position to consider emergencies promptly without being under the necessity of proclaiming them by an appeal to Congress and thereby aggravating the situation, and being obliged to wait for Congress to be in session and to act on the matter.

Another phase of this problem is that the total volume of paper eligible for discount held by member banks at the present time is only about $2,000,000,000, or less than 8 percent of the resources of the banks, and even in 1929 it was only about $4,000,000,000, or a little more than 12 percent. While this amount is sufficient in the aggregate to provide access to the Federal Reserve banks, there were many individual banks that did not possess sufficient eligible paper. Even more important than that, is the fact that in a period of timidity the banks tend to refrain from making loans, except on paper eligible for discount at Federal Reserve banks. This is even now a factor causing liquidation in many communities and preventing adequate expansion of credit in others.

A bank that would conduct its business on the theory of having only such assets as can be disposed of at will in times of crisis, when the national income has been cut in two, cannot serve its community adequately. Such a bank would confine its operations to the purchase of the most liquid open-market paper, with the consequence that it would neglect its local responsibilities and would nevertheless find it difficult to earn enough from the low returns on such paper to cover expenses and dividends. The banks should be in a position to meet the needs of their communities for all kinds of accommodation, both short and long term, so long as the credits are sound, and they ought to have the assurance that all sound assets can be liquefied at the Federal Reserve bank in case of an emergency.

4. REAL-ESTATE LOANS

Closely allied to this matter of eligibility is the proposal that the limitations on real-estate loans be modified so as to permit member banks better to supply the needs of their communities for mortgage loans. This proposal does not introduce a new character of loan, it merely relaxes existing limitations on real-estate loans which national banks have made for 20 years. What the bill proposes is to modify the requirements so as to make them more realistic and to enable the member banks better to serve their communities. Coupled with the provisions in regard to eligibility, these proposals ought to result in greater willingness of member banks to lend on real estate and, therefore, to an improvement in the mortgage market and a stimulation of construction which is essential to business recovery.

Member banks hold about $10,000,000,000 of the people's savings, and it is therefore proper and necessary that they invest a part of their funds in long-time undertakings. The separation of commercial banking from savings banking may be theoretically desirable, but it cannot be accomplished in this country without disrupting existing machinery, while the need for increased activity in building is urgent. Member banks are suffering from the competition of many Government and other agencies that are entering the field of real-estate loans, and it is a matter of self-preservation for the banks to be able to hold and expand their activities in this field.

The details of the bill as proposed may have to be modified. The problem is a difficult one because the laying down of specific percentages of value presents many perplexities. In some regions, and at some times, a 75-percent loan on real estate is conservative, while at other times a 50-percent loan may be too liberal. It may be best in this matter, as in others, to vest discretion in the Federal Reserve Board to prescribe such rules and regulations about real-estate loans as in its judgment would operate most effectively in the public interest.

OTHER PROPOSALS IN TITLE II

Other sections of title II of the bill which I have not discussed may be briefly enumerated: Provision that directors of the Federal Reserve banks shall not serve for more than 6 consecutive years. This would prevent crystallization of any one interest in the management of a Reserve bank. A change in the qualifications of members of the Federal Reserve Board to make these qualifications more descriptive of the functions of the Board. An increase in salary of future appointive members of the Board and provision for pensions. Grant of power to the Board to assign specific duties so as to be relieved of detail. Placing of obligations guaranteed by the United States Government on the same basis as direct obligations of the Government. Repeal of collateral requirements against Federal Reserve notes. These requirements serve no useful purpose and have been sources of serious trouble at critical times. Clarification of the authority of the Board to raise or lower reserve requirements—the bill as introduced authorizes changes in reserve requirements for different districts or classes of cities. It might be modified by eliminating changes by districts and classifying cities into two groups—(1) Reserve and Central Reserve cities and (2) other cities. Authority for the Federal Reserve Board to waive capital requirements for admission of insured banks into the system prior to July 1, 1937, when all banks, in order to be insured, must be members of the Federal Reserve System. This might be broadened so as to authorize the Board to waive not only capital but all requirements and to permit existing banks to continue permanently with their present capital, provided it is adequate in relation to their liabilities.

TECHNICAL PROVISIONS

Title III of the bill contains a number of sections proposed by the Comptroller of the Currency and by the Federal Deposit Insurance Corporation. Sections in which the Federal Reserve Board is interested are in the nature of technical improvements of a noncontroversial nature of the same general character as those contained in the so-called " omnibus banking bill " which was reported favorably by the Banking and Currency Committees of both Houses of Congress in June 1934, but failed of enactment in the closing days of the Seventy-third Congress.

For example, a provision that a holding-company affiliate, which is a holding company by accident and is not engaged in the business of holding bank stock, shall be exempted from the requirement of obtaining a voting permit. Another example is the provision that member banks for the purpose of calculating reserve requirements shall be allowed to deduct from gross deposits the amounts that are due them from other banks rather than be allowed to deduct these amounts only from the deposits they hold for other banks. The existing provision has resulted in injustice to country banks, which hold no deposits for other banks, and are, therefore, unable to get the benefit of the deduction which city banks can make. There is also a proposal intended to simplify the provisions of the Clayton Antitrust Act in regard to interlocking bank directorates and to facilitate the administration of these provisions by the Federal Reserve Board.

Provisions in title III, as well as in title II, are still being studied and improvements and modifications in technique and in phraseology are being developed. I shall, therefore, appreciate an opportunity to submit to the committee for its consideration a number of amendments to the bill before final action is taken. It would also be helpful if the committee would permit the Board's counsel to cooperate with the committee's counsel in the final perfecting of the phraseology of the bill.

Thank you.

The CHAIRMAN. Gentlemen, in view of the physical difficulties under which Governor Eccles is laboring this morning, I have assured him that we would excuse him, when he had finished his general statement. Governor Eccles, if you desire that we do so, we shall be glad to let you go on tomorrow morning, and the committee will meet at 10:30 o'clock.

(Whereupon the committee adjourned until 10:30 a. m., Tuesday, Mar. 5, 1935.)

BANKING ACT OF 1935

FRIDAY, MARCH 5, 1935

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

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

The CHAIRMAN. Gentlemen, we will come to order. Governor Eccles, the committee will be glad to have you resume your discussion of title II of the bill. You may proceed as far as you desire without interruption.

STATEMENT OF HON. MARRINER S. ECCLES, GOVERNOR, FEDERAL RESERVE BOARD—Resumed

Mr. ECCLES. I made a general statement yesterday, and it occurred to me that it might be helpful to the members of the committee if I discussed, more or less informally and possibly in more detail, some of the features of the bill.

It is proposed to combine the office of the chairman of the board of directors and the Governor of the Federal Reserve bank. At the present time each of the 12 Reserve banks has 9 directors. Six of those directors are elected by the stockholders of the banks, that is, the member banks; three of them are appointed by the Federal Reserve Board.

These directors are appointed for 3-year terms. Of the 6 directors appointed or elected by the member banks, 3 are bankers, known as "class A" directors; 3 must be selected from commerce, agriculture, or industry, and are known as "class B" directors. One of the three directors appointed by the Federal Reserve Board, known as "class C" directors, is selected or appointed as chairman of the board of directors of each Federal Reserve bank. He is also the Federal Reserve agent. He is a full-time, highly paid official; and originally it was conceived that he would be the executive head of each Federal Reserve bank.

The governors of the Federal Reserve banks are not mentioned in the Federal Reserve Act. The act provides that the directors of the bank shall select such officers and employees as are necessary to conduct the affairs of the bank.

The title of "governor" was given by the nine directors to the person selected by them as the operating head of the bank. In practice, the position of the governor has become an outstanding and important position, and in nearly every instance he has become the head of the bank. He is not a director of the bank; he is elected by the board of directors; the nine members of the board of directors.

The Federal Reserve Board has no legal relationship with the governor of the bank, has no responsibility in his selection except that it passes on his salary. Its official relationship with the bank is through the chairman and Federal Reserve agent, whom the law designates as the Board's official representative at the Federal Reserve bank.

It is proposed, in this legislation, as a matter of efficiency, coordination, and good organization, to do away with this dual relationship and to combine the office of governor with that of chairman, making the governor and the chairman a class C director. The board of directors of each Federal Reserve bank will select the governor and the chairman; but this selection must be subject to the approval of the Federal Reserve Board.

You will observe that the Federal Reserve Board will not have the power of appointment of the chairman, which will be given to the local board and combined with the office of governor; the appointment will be subject to the approval of the Federal Reserve Board.

This will make for better coordination and economy, will do away with the possibility of cleavage, by reason of the dual organization of the chairman, appointed by the Board in Washington, and the governor, selected by the local board.

Although the directors of the banks are appointed for a period of 3 years only, in practice many of the directors have served since the beginning of the Federal Reserve System. It is thought advisable to limit the term of office of all of the directors to two consecutive terms, totaling a period of 6 years. This is proposed to avoid the crystallization of control or authority in any one group or combination.

It is felt that, in each Federal Reserve district, there are many able men to represent the bank members and also commerce and industry, as well as the Board at Washington, which appoints the three class C directors; and that the public nature of the Reserve System is such that it would be to the interest of the System to have a limit upon the terms of the directors.

It is recognized that there may be a loss of some very able men as the result of this restriction, but it is believed that there will be more gained as a result of this policy than will be lost.

It is interesting to note that two, and I believe three, of the Federal Reserve banks have adopted the policy, without it being prescribed by law, of limiting the terms of their class A and class B directors, that is, the directors elected by the member banks, to 3 years. The New York bank and the Dallas bank, and I think the Atlanta bank, rotate the offices of their class A and B directors. They find this in the interest of harmony among their member banks; and it is felt that, if it is in the public interest to do that in the case of those banks, it would be well to do it in the case of all banks and to place the limitation to 6 years in the law.

Since this proposal was made, there has been considerable discussion, and I find that, almost universally, it is looked upon with a great deal of favor by the banks throughout the country. I find that there is considerable feeling among many of them that there has been a certain amount of crystallization of control in small groups.

I met with a group of bankers on Friday, and without exception, they were all very favorable to that restriction.

Admission of insured nonmember banks: I am discussing this briefly, in the order in which the proposals appear in the bill—the admission of insured nonmember banks is in section 202. It is recognized that many of the nonmember banks could not readily qualify as members of the Reserve System, and that a very great hardship and injustice would be imposed upon them, if they were required to become members of the Federal Reserve System under the present legislation, and under the rules and regulations for membership. It is, therefore, proposed that the Federal Reserve Board should have authority to waive the capital requirements.

I suggested yesterday, in connection with this particular feature of the bill, that the authority for the Federal Reserve Board to waive the capital requirements for admission of insured banks into the System, prior to July 1, 1937, when State banks are required to be members of the Reserve System in order to be insured, might be broadened, so as to authorize the Board to waive not only the capital requirements, but all requirements, and to permit existing banks to continue permanently with their present capital, provided it is adequate in relation to their liabilities.

I think it is desirable to have unification of the banking system, and I recognize that possibly the most likely way of getting it is through all banks becoming members of the Federal Reserve System.

In many instances, the capital of nonmember banks, is less than the minimum amount required—$50,000, and their volume of business is such that they do not require and cannot possibly use and support a capital of $50,000 with an adequate surplus, which is also desirable.

It is also recognized that certain of the rules and regulations for membership would make it very difficult for many banks to qualify under those rules and regulations; and it is, therefore, the desire of the Federal Reserve Board to so modify the law and its rules and regulations as to make it possible, under reasonable conditions, for nonmember banks to get the benefits of membership. I believe those benefits are very real. Particularly would that be true if the present law is amended in some of the particulars as provided for in the proposed bill. I refer to the change in the present eligibility features; also the recognition of the desirability of using the savings and time funds in longer term lending, or in the real estate loan field. These provisions would give to many of the nonmember State banks the support that otherwise would not be available to them, if it were possible for them to continue to operate as nonmember banks.

In section 203, it is recognized that it would be desirable to change the present language with reference to the qualifications for membership on the Board, as a recognition of the fact that the functions and duties of the Federal Reserve Board are such as to make it a body representing the Nation, rather than any group or combination of groups. In recognition of that, it is provided in the bill that future appointive members of the Board shall be men who are qualified by education or experience or both to participate in the formulation of economic and monetary policies, which seems to me to be the central and most important function of the Federal Reserve Board.

It is recognized that membership on the Federal Reserve Board is one of the most important, responsible, and powerful positions of the Nation. It is, therefore, believed that the position should attract, by reason of its importance and responsibility, the best qualified men in the Nation to deal with these monetary and economic problems. It is felt that the men on the Board should be independent and, therefore, it is recognized that their compensation should be such as to enable them, without having to have an independent, private income, to live in Washington in the manner that their position would require. It is proposed that the compensation for future appointive members be increased to $15,000 per year, the salary now received by members of the Cabinet. Their salary was originally equal to that of Cabinet members, but later the Cabinet salaries were increased. The proposal is to reestablish this equality. It is also proposed that there be a pension or retirement provision, so that members of the Board who have severed their outside connections and serve in this position, will not feel a dependency that otherwise they may feel.

I do not believe the pension provision in the bill fully and adequately meets the situation. It provides that any of the present members may retire at the age of 70, and that future appointive members must retire at the age of 70. It also provides that, upon retirement, they will receive a pension of $12,000 per year, when they have served the full period of 12 years, or more, and a proportionate amount when they have served not less than 5 years. It would seem to me that, in order to attract the ablest men obtainable for this position, to make them willing to accept positions on this Board as careers, and to sever all other connections, a pension should be provided for future appointive members, irrespective of the age at which their terms may expire.

It seems to me that this would have the effect of inducing these men to accept positions of this sort during the most active and remunerative period of their lives; otherwise, they might not be willing to accept.

It does not seem fair to ask a person, of the caliber that Board members should be, to accept a position and serve for a 12-year term—we will say from the ages of 48 to 60—and at the end of the period of 12 years, if not reappointed, to be obliged to go out and undertake to reestablish connections, which were severed and neglected for a period of 12 years.

It would seem to me that, in the public interest, it would be well to provide that, if a member is not reappointed, he would receive the full pension, if he has served a full term or longer; but if he is offered a reappointment and prefers not to serve, of course he should not be given a pension. I believe that would make for greater independence on the part of the members of the Board.

As to the term of the office of Governor of the Board: There has been a good deal said about the provision in the proposed legislation that the term of the Governor as a member of the Board shall expire when he is no longer designated as the Governor by the President.

The present law provides that the Governor shall be designated by the President to serve at his pleasure, the designation being from among the Federal Reserve Board members. As a practical matter, when the Governor is no longer designated as Governor by the President, it is because the President is desirous of having someone else serve as Governor.

Mr. GOLDSBOROUGH. As I understand it, you approve of that provision?

Mr. ECCLES. What is that?

Mr. GOLDSBOROUGH. You approve the provision allowing the President to remove the Governor, whenever he sees fit?

Mr. ECCLES. Well, I have no objection to it. I think that, as a practical matter, it is reasonable. In some of the other central banks there are similar provisions with reference to the executive heads of the banks.

It seems to me that an administration is charged, when it goes into power, with the economic and social problems of the Nation. Politics are nothing more or less than dealing with economic and social problems. It seems to me that it would be extremely difficult for any administration to be able to succeed and intelligently deal with them entirely apart from the money system. There must be a liaison between the administration and the money system—a responsive relationship. That does not necessarily mean political control in the sense that it is often thought of.

Does that answer your question, Mr. Goldsborough?

Mr. GOLDSBOROUGH. Yes; from your standpoint, I think it does.

Mr. ECCLES. Referring again to the term of office——

The CHAIRMAN. Suppose you let me ask a question right there: Is not the practical situation such that the administration has that power and may exercise it, but under this bill there will be a technical recognition of that power and a definite fixing of responsibility, at least within limitations?

Mr. ECCLES. Well, the only change—I do not think it will be material, but the only change in this bill over the present legislation is that when the Governor is no longer designated as Governor by the President, his term as a member of the Board will expire, whereas, at the present, when he is no longer designated as Governor, his term as a member does not expire. This means that if he is no longer designated as Governor and he does not resign as a member, there will be no vacancy on the Board to which the President could appoint the person he desires to designate as Governor, unless he designates an existing member of the Board. There is this disadvantage under the existing law: When a member is no longer designated as Governor and resigns as a member—which is the only thing that a Governor could do, and a person who would not do that would certainly not be a proper person to act as Governor—he is precluded for a period of 2 years from entering the banking field. That is a deterrent in the present law to a man accepting that office. If he is taken from the banking field, he is required to sever all connections with the banking business for an indefinite time, that is, for as long as he is designated as Governor, and that may be for 2 or 3 or 4 years. When he is no longer designated as Governor, he resigns as a member: and, if he has not served out his term as a member, he is precluded for 2 years afterward from entering the banking field again.

If he has served out his term as member, he may immediately enter the private field.

Now, what I should like to propose here is that the Governor's term as a member do not expire when he is no longer designated as Governor; that is, leave the law as it is with reference to his term as a member, but provide that, if he chooses to resign as a member when he is no longer designated as Governor, his term as a member be considered to have been fulfilled.

Mr. HOLLISTER. That is not what this new statute says, is it?

Mr. ECCLES. No; I am offering this as a suggested change: Whereas the bill provides that he shall automatically cease to be a member of the Board when he is no longer designated as Governor, I am suggesting that it be changed so as to provide that, if he does not choose to continue to serve as a member when he is no longer designated as Governor, he would be free to enter the banking field, without taking a 2-year vacation.

Mr. GOLDSBOROUGH. Your view is that they should resign voluntarily, and the 2-year application should apply; but if they are removed as Governor and they see fit——

Mr. ECCLES. It should not apply.

Mr. GOLDSBOROUGH. It should not apply?

Mr. ECCLES. That is right.

Mr. GOLDSBOROUGH. That seems to me to be sound.

Mr. ECCLES. It seems to be fair and will remove a deterrent; and it seems to me that it will accomplish the object of making it a more attractive position in the future than it has been in the past.

Mr. HOLLISTER. Would it not also attract something else, or accomplish something else? This is drafted to give the President the opportunity, if he cares to do so, to make a clean sweep, to completely clean up the whole Federal Reserve Board in a few days, does it not?

Mr. ECCLES. Well, of course, I think that if we are going to conceive of a President that would resort to what would be considered sharp practice, he would possibly have more direct ways of cleaning it up than that. I think a President that would resort to that sort of thing would possibly have other ways of meeting the situation.

Mr. HOLLISTER. Presidents have in the past, unfortunately, done things that some of us would not back up; but, as a matter of fact, as the bill is drafted, it permits the President, if he cares to, to remove successively every member of the Federal Reserve Board, appoint him as Governor, and undesignate him; whereupon, he immediately retires from the Board?

Mr. ECCLES. Yes; that is correct.

Mr. HOLLISTER. So the suggestion you make would at least eliminate the possibility of that happening, when we had a man in the White House that might adopt such sharp practices?

Mr. ECCLES. Yes.

Mr. CROSS. Mr. Chairman, may I make a suggestion as a member of the committee?

The CHAIRMAN. Certainly.

Mr. CROSS. I would like to make this suggestion: That Mr. Eccles be permitted to go ahead and finish his statement; and then that he submit the amendments that he would suggest; and then when he gets through with his statement, just as Mr. Goldsborough suggested the other day, each member of the committee be given a chance to ask questions, because every member has many questions, or a number of questions, on this section that they would like to ask. I am afraid that, if we start like this, we will never finish or get anywhere. That is my suggestion.

The Chairman. Well, I certainly expect that every member of the committee will have the opportunity you refer to, and I will recognize members in an orderly way, so that every member will be allowed to ask questions.

Mr. Cross. The point is, we will not have a coordinated idea of this by going in and out, and I think it is much better to let him finish, and then later on let him bring his proposed amendments to the bill, and then we can take up those amendments and let him discuss those amendments in a much more uniform way, and every member will get a grasp of the bill. That seems to me to be the best way to proceed.

The Chairman. All right, Mr. Eccles, you may proceed.

Mr. Eccles. Assignment of duties: There is no controversy over that question. It is just a practical way of enabling the Board to meet the problems of increased responsibility that are placed upon them by delegating to others many of the routine duties, so long as they do not involve questions of policy.

Open-market operations: Inasmuch as this was covered quite fully in my statement yesterday, I do not believe that I can add very much to it. There will likely be a good many questions that will develop in connection with that, because, under that heading, the whole question of monetary control heads up.

I explained yesterday the way the open-market operation is now organized, the manner in which the bill provides for it to be operated, and the amendments suggested to the proposals in the bill.

Eligibility for discount: The eligibility requirements of the present law do not seem to me to meet the changed conditions that we now have in the Nation, compared with the conditions that existed at the time the Federal Reserve was established. The amount of eligible paper available now held by banks is a very small part of the total resources of the banks. Even in 1929 it was only slightly over 12 percent of their loans and investments, and today I understand it is less than 8 percent. Approximately $2,000,000,000 is the total amount of the paper which would be considered eligible by the banks themselves. It was found, when the depression commenced and as it continued, that the banks did not have eligible paper to meet their shrinking deposits, brought about by the general liquidation of bank loans and by hoarding; and that, in order to avoid closing they were forced to sell such bonds as they had upon the market. These bonds were considered, at one time, to be secondary reserves, because they were listed. Banks also brought pressure upon all loans which came due during the period, and were forced to refuse new credit, feeling, of course, that they had to have as large cash reserves as possible and be as liquid as possible. They were bringing pressure to collect loans that came due, and to sell the securities that they had, wherever they could do so without taking too large a loss. That attitude on the part of the banks throughout the Nation was largely due, it seems to me, to the fact that they did not have eligible paper in sufficient quantities to meet the demand and could not get help at the Federal Reserve banks unless the paper was eligible.

Therefore, in an effort and under pressure to get liquidity, they froze themselves so completely that they finally closed the entire banking structure. So it was found out that, in the final analysis, in a depression, there is no liquidity, except that liquidity which can be created by the Federal Reserve or the central bank through its power of issue.

This was finally recognized when great damage had been done, when thousands of banks had been closed unnecessarily, when millions of individuals and institutions had been forced to the wall through the lack of available credit, or through pressure to pay existing debts. Millions of depositors lost hundreds of millions of dollars as the result of those closings.

We finally recognized that we did not have to have eligible paper and we did not have to back our currency with gold or eligible paper or even with Government bonds. We finally recognized that, in order to get the banks open, we could take any sound asset into the Reserve bank and issue Federal Reserve bank notes. When that happened nobody wanted their money, the runs stopped, and liquidation stopped to a very great extent. Certainly, the pressure was very greatly relieved.

Now it seems to me that it is only being a realist to recognize that the Reserve banks, subject to rules and regulations made by the Reserve Board, should have the power to meet emergencies, should have the power to loan to member banks upon sound assets, rather than see the banks close, or rather than see unnecessarily drastic liquidation forced upon the community.

This provision does not mean inflation. Before the banks today, as a whole, would have any occasion to use the Reserve System, they would have to extend billions and billions and billions of dollars of credit, because of the excess reserve position that they now occupy. But, if the provision is there, it will make the banks feel altogether different about extending credit today. It will make them recognize that they do not have to have 90-day or 6-month paper in order to make loans, when that type of demand for credit does not exist to more than a very limited extent.

This, to my mind, is one of the most important features of the legislation at the present time. It will tend to do more toward inducing recovery through credit expansion than any other feature of the bill. The banking system must be made, to provide the money and credit required, if it is going to justify its existence. At the present time, that is largely provided by the Government. The banking system, the commercial banking system——

Mr. GOLDSBOROUGH. You say it is being provided by the Government?

Mr. ECCLES. To a very large extent.

Mr. GOLDSBOROUGH. We were under the impression that the Government borrowed the money that it is now providing, from the banks; is that not correct?

Mr. ECCLES. That is very true. The banks are willing to extend credit on Government bonds.

Mr. GOLDSBOROUGH. We have provided the banks with $13,000,000,000, about, have we not?

Mr. ECCLES. Well, I do not know the exact amount, but——

Mr. GOLDSBOROUGH. That is an approximation.

Mr. ECCLES. But whatever amount of Government bonds the banks have purchased—it is not $13,000,000,000, but, including what the Federal Reserve System has, I think it is nearly $13,000,000,000—the Government is doing the lending through the various Government lending agencies, such as the Home Owners' Loan Corporation, the Farm Credit Administration, and the Reconstruction Finance Corporation. Those are the three most important agencies and, of course, we know they have put out billions and billions of dollars, and the banks have largely taken Government bonds and bonds guaranteed by the Government, and the Government, in substitution, has taken the loans of the individual and the corporations. So that it has been a process of the banks liquidating their private loans, and the Government taking them over, and the banks providing the funds to take Government bonds or bonds guaranteed by the Government. And, of course, if continued, it seems to me that the banks are going to have very great difficulty in justifying their existence.

Mr. GOLDSBOROUGH. When they can only live by the Government furnishing nearly one billion dollars a year in interest, which they do not earn, it seems to me your statement is worthy of very serious consideration.

Mr. ECCLES. I recognize that, and I have also told many of the banks that the provisions of this legislation with reference to this eligibility feature, and with reference to this real-estate loan feature, are to give them an opportunity to utilize their funds in the direct field of lending and get the Government out. Otherwise they will find that the Government will have taken over the banking business, not because the Government wanted to, but because the banks forced it to.

Purchase of United States guaranteed obligations: It is provided that obligations guaranteed by the United States Government should be put on the same basis as direct obligations. There seems to me to be no justification for discrimination; that they should be eligible for purchase by the Reserve banks without regard to their maturity, in the same manner that direct obligations of the Government are eligible for purchase by the Federal Reserve banks.

Collateral for Federal Reserve notes: It is provided that the position of Federal Reserve agent as such shall be eliminated and that the position of chairman of the Federal Reserve bank shall be combined with that of the governor. The Federal Reserve agent acts as a trustee, holding the collateral against which Federal Reserve notes are issued, at least 40 percent in gold certificates and the balance in eligible paper or Government bonds, or both. It was thought, originally, that the amount of currency outstanding at any time was influenced or regulated by the amount of commercial paper, which represents the activity or the volume of trade or business. It has been found that there is very little relationship between the volume of Federal Reserve notes and the volume of commercial borrowing. Of course, that is due to the fact that currency, as such, plays so small a part in our money system and that bank credit or deposit currency plays a major role. The amount of currency or Federal Reserve notes outstanding will depend upon the demand for currency by member banks. The member banks discount or borrow from the Reserve banks in order to maintain their required reserve balances with the Reserve banks. Member banks draw currency to meet the demands of their customers. It is not felt that the collateral put up back of the Reserve notes in any way restricts the use of currency. It is not felt that collateral adds anything to their security. They are now guaranteed by the United States Government; they are a first lien on all the assets of the Reserve banks. Whenever notes are issued or deposits created by the Reserve banks, there are assets to offset the liabilities of the Reserve banks, whether the liabilities consist of notes or of deposits of their member banks.

There would seem to be no more reason to secure notes which they issue than to secure deposit liabilities to their member banks. The Reserve banks are required to hold gold certificates equal to not less than 40 percent of their notes outstanding, and gold certificates or lawful money of not less than 35 percent of their deposit liability and——

Mr. Wolcott. Gold certificates?

Mr. Eccles. Well, of course, they have no gold. There is no proposal to change that. The assets of the banks, on the other side, consist of gold certificates and other money that they may hold, and Government bonds and bills or rediscounts.

Mr. Hancock. Could you properly call those notes "asset currency"?

Mr. Eccles. What is that?

Mr. Hancock. Could you properly call those notes "asset currency"?

Mr. Eccles. I do not just understand what you mean.

Mr. Hancock. I do not want to begin questioning you, but right on that point you made the statement that it was not necessary that notes have any particular banking value.

Mr. Eccles. Yes.

Mr. Hancock. In that they constitute a lien against all of the assets of the banks.

Mr. Eccles. That is right.

Mr. Hancock. Now, would you consider such notes as asset currency?

Mr. Eccles. Well, they are the obligations of the banks that issue them and are guaranteed by the United States Government. They are not asset currency, in that they are not backed specifically by this or that particular asset or assets, except to the extent that there is at least 40 percent of gold certificates held, and there would be other certificates back of them. The liabilities of the bank would be offset by its assets. So, to that extent, there are assets in the form of gold certificates, Government bonds, or loans and discounts, back of all the notes issued, just as there are back of all of the deposits of the bank. The value back of the Federal Reserve notes is determined by the assets of the Reserve banks. In 1932 it was found impractical to restrict the issue of these notes as they were restricted, when gold was leaving the country very rapidly and when the banks held very limited amounts of commercial paper. The requirements of the law had to be suspended in 1932, and Government bonds had to be accepted as substitutes for commercial paper as the basis for issuing notes, in order to release the excess amount of gold that had to be held in the absence of commercial paper. So it was found that the restriction imposed at the time, and the only time when the provisions of the law were tested at all, they had to be suspended.

The CHAIRMAN. It might be well to remember definitely the date of that action.

Mr. ECCLES. Well, you probably remember it. It was in 1932, February 27, 1932.

Reserve requirements: The Federal Reserve Act, as amended by the act of May 12, 1933, provides that, with the consent of the President, when an emergency is declared to exist, the Federal Reserve Board has power to change the reserve requirements of member banks. It is proposed to recognize this emergency provision as a permanent provision and to give to the Board the power to change reserve requirements, without declaring that an emergency exists and without the approval of the President. This is a function of monetary control almost equal in importance to open-market operations,. and it is felt to be necessary that the Board have this power, particularly in order to control an inflationary condition, should one develop.

It is conceivable that the reserves of the member banks may be greatly in excess of the amount of Government bonds and paper held by the Reserve banks. The sale of those securities in the market would not be sufficient to absorb the excess reserves; and therefore, the increase of reserve requirements would come into use as a means of controlling an inflation of credit. It would be expected to be used only as a method secondary to open-market operations. Changes in reserve requirements would be used at a time when open-market operations failed to meet the situation.

Mr. CROSS. I might suggest that I remember the conditions that existed in the world, the speculation on the stock exchange; do you think it would be wise to have a provision so that you could designate certain particular banks, where they had increased their reserve, rather than apply to all banks, everywhere, at any time?

Mr. ECCLES. I do not believe so. I think money is too much like water; it seeks a place where it can——

Mr. FORD. Seeks it own level?

Mr. ECCLES. Yes; it seeks a level, and of course that level is based upon the return it can get.

We have proposed here that changes in reserve requirements might be a pplied to two classes of cities: Central reserve and reserve cities in one class and country banking areas in the other. It is conceivable that different reserve requirements could be applied to the reserve cities, if that is where speculation was going on and where the excess of reserve was, which is usually the case. There is an element of time in money seeking its level. Just what it is, I do not know that anybody can say. But increases in reserves might be applied first to the reserve cities and then later to the other areas, if it seems to be necessary, rather than to apply them at the same time universally. I do not believe that you could consider it beyond that. I do not believe it would be practicable to apply it to individual banks. The Federal Reserve Board has the power now to regulate margin requirements on collateral and brokers' loans, which is one of the most effective instruments of speculation control, I think, now available. I believe that, had it been available in 1928 and 1929, it would have possibly been helpful in controlling or restricting the speculative orgy that we went through.

The CHAIRMAN. Governor Eccles, the House has been in session for a little while, and there are matters that require the attendance of Members, and I am sure you will be glad to desist until tomorrow, anyway. We will adjourn until 10.30 o'clock tomorrow morning, and we expect to have the pleasure of having you back again with us.

(Whereupon the committee recessed until 10.30 a. m., tomorrow, Wednesday, March 6, 1935.)

BANKING ACT OF 1935

HOUSE OF REPRESENTATIVES,
COMMITTEE ON BANKING AND CURRENCY,
Washington, D. C., Wednesday, March 6, 1935.

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

The CHAIRMAN. Gentlemen, we will come to order. Some of us have to appear before the Committee on Rules this morning, and I have to leave in a few minutes. I am going to suggest that, unless Governor Eccles decides to proceed further without interruption, that the committee will now proceed to discuss with him title II of the bill. If you desire further time without interruption, we shall be glad for you to have it. We do not want to hurry you in the least. It is our desire to permit you to have ample time to express your views, in your own way, fully, after which the committee, of course, will desire to interrogate you.

Mr. ECCLES. I have finished my principal statement.

Mr. KOPPLEMANN. May I ask a question?

The CHAIRMAN. Certainly.

Mr. KOPPLEMANN. There may be some questions that I want to ask on title II, but I am not prepared to do that today. I suppose that Governor Eccles will be here tomorrow?

The CHAIRMAN. Yes; you will have ample opportunity to do that. I am taking it for granted, of course, that that will be done, if it is necessary to meet your convenience.

Mr. ECCLES. I finished the discussion yesterday of the proposals, with the exception of the one relative to the real-estate loans.

The CHAIRMAN. The committee will be glad to hear you further on that provision, or any other, without interruption, if you so desire.

Mr. ECCLES. I finished them all with the exception of that yesterday, and it seems to me to be one of the important issues, and it might save time to say something about that.

The proposal is to amend the act to permit the national banks, as well as other member banks, to make first-mortgage loans on improved real estate for a period up to 20 years; that is, if the loans are amortized so that they would be paid off over that period of time; to reduce the period from 5 years to 3 years in cases where the loans are not amortized, and to increase the amount that they can loan from 50 to 60 percent of the value of the real estate.

It is also proposed to increase the amount, the total amount of bank funds that can be loaned, from 50 percent of time funds of a bank up to 60 percent, including in the amount loaned, however, other real estate excepting the banking houses.

You recall that I suggested yesterday that the proposed bill be amended, if we think it advisable to amend it, so as to give the Federal Reserve Board the power to determine the conditions of real-estate loans by regulation, the reason for this being that to try to put into the statute a limitation of 60 percent of the amount of savings will work a very great hardship on many State banks. We find that some of the State member banks and many of the State nonmember banks already have in excess of 60 percent of their time funds in real-estate loans. It would seem, therefore, that they would be required to cease making real-estate loans and to liquidate the loans they had as they fell due.

Also, it seems that to try to fix in a bill or in a statute a provision permitting 75 percent of the appraised value of property might not be desirable. It is felt that the situation would be better met if the Board had the power to fix the rules and regulations to meet this matter; that it would make it much more flexible than if it is put in the statute.

The member banks of the country have about $10,000,000,000 of savings or time funds. The New England area and the New York area are largely served by mutual savings banks. More than 50 percent of the deposits of the banks, outside of that area, consist of savings deposits. These funds are equivalent to the funds that the mutual savings banks are receiving from the people in the area that they serve. The banks are required to pay interest on these time funds. The maximum rate of interest at the present time is fixed at 2½ percent. It is impossible for these banks to pay that interest and to loan these funds on short-time paper.

In the first place, there is not available a sufficient amount of short-time commercial loans to utilize more than a fraction of the demand deposits, much less the savings deposits; and as a result the banks hold a very large volume of idle funds.

There has been no restriction imposed upon banks with reference to their investments in long-term bonds. They have been permitted not only to invest all of their savings funds but as much of their commercial funds as they desire, in long-term bonds, railroad bonds, utility bonds, foreign bonds, and industrial bonds. I cannot see that it is so much more desirable to permit banks to invest in long-term listed bonds than it is to loan their funds on improved real estate on an amortized basis in their local communities.

The fact that bonds were listed and, therefore, supposed to be marketable, was considered a justification for the investment of funds in bonds as compared with the investment in real estate. The depression proved that the ready market for bonds was only there at prices that bankrupted the banks, if they were forced to sell in the market that existed. More banks became insolvent as a result of the depreciation of their bond accounts than as the result of their real-estate loans. The fact that bonds were listed and were greatly depreciated put the banks, when the examiners came into a condition of insolvency, because of the difference between the quoted market price and the cost of the bonds; whereas in the case of real-estate loans it was not expected that there should be a ready market for them, and so long as they were not in default, they were considered to have the value of the amount of the loan. It was the depreciation shown on the bonds and stocks, because of the quoted market, that impaired and in many cases wiped out the capital of the banks.

It seems to me that, if we want to be so restrictive in the matter of real-estate loans, because they are long-term investments of funds which are likely to be drawn out on demand, we should also be restrictive with reference to the investment of funds in long-term bonds. I believe that the banks should be permitted to invest their funds in long-term bonds and in long-term amortized mortgages. Particularly is that true with reference to their savings or time funds. The reason is that otherwise they have no way to use their funds, except to buy Government bonds, or bonds guaranteed by the Government.

Mr. GOLDSBOROUGH. You mean you think it is the duty of society to support the banks?

Mr. ECCLES. No; I am not saying that. I am talking about the condition that exists.

Mr. GOLDSBOROUGH. As far as society is concerned, it is interested in banks only insofar as the banks are useful to society?

Mr. ECCLES. That is correct. Either the banks holding these $10,000,000,000 of time funds must be prepared to lose those funds to the savings and loan associations, to mutual savings banks, or to others, or they must be put in a position to use the time funds in the long-term investment field.

I am convinced that it is not possible for the majority of banks in this country to operate with demand deposits alone. The volume of these funds is not adequate for profitable operation except in the larger institutions, and to take time deposits away from the banking system would reduce the size of many banks to the point where they would be unable to exist.

If our private banking system is expected to provide credit in other ways besides buying Government obligations or obligations guaranteed by the Government, then it seems to me that some of the provisions of this proposed legislation are essential, the one with reference to eligibility and the one with reference to real-estate loans.

There is nothing new about national banks loaning on real estate, since they have made such loans for 20 years. They have loaned, however, for a limited period of 5 years on a straight mortgage, which makes for a much more unsound loan than a longer-term amortized loan.

I believe that covers what I have to say, Mr. Goldsborough, and I will be glad to answer any questions.

Mr. GOLDSBOROUGH. Suppose we begin the regular examination. Mr. Cavicchia has a question.

Mr. CAVICCHIA. Mr. Chairman, I think this would be the proper place in the record for the Governor to tell us, if he knows, to what amount the mortgages of national banks are held or were held in 1933 or today, if he knows.

Mr. ECCLES. I do not know off-hand, but I have it here. On October 17, 1934, under the law in effect, the national banks had authority to lend up to $3,400,000,000. Under the new proposal the limit would be about $4,400,000,000 for national banks and about

$6,800,000,000 for all banks. The total amount of actual loans on real estate by all member banks at the end of 1934 was $2,273,000,000.

Mr. GOLDSBOROUGH. Governor Eccles, you wanted to say something else?

Mr. ECCLES. I was going to say that in connection with my discussion of the provisions of the bill I have suggested certain proposed amendments or revisions for your consideration. I would like, in closing, to call those to your attention in the order in which they were suggested.

Mr. GOLDSBOROUGH. As this hearing naturally will be protracted, we are not going to hurry you, and you may do so.

Mr. ECCLES. In section 201, the first section discussed, it was suggested that the governors and chairmen of the Federal Reserve banks be approved by the Federal Reserve Board every 3 years rather than annually so that their terms as governors and chairmen would coincide with their terms as class C directors.

Mr. GOLDSBOROUGH. What page is that on, please?

Mr. ECCLES. That is section 201. That is the one with reference to combining the offices of chairman and governor.

Mr. WILLIAMS. On page 39 of the bill.

Mr. ECCLES. This, as you will notice, is a slight modification, and it is just offered as a suggestion.

There has been some criticism about the necessity of approving the appointment of the governors each year, whereas they will be appointed as class C directors for 3 years. I personally can see no necessity of approving their appointments every year and feel that it is well to consider the suggestion that they be approved every 3 years instead.

Section 202: On the question of admitting insured nonmember banks to the Federal Reserve System, the suggestion is that the Board have authority to waive not only the capital requirements but all other requirements for admission, and that the Board be permitted to admit existing banks to permanent membership, without requiring an increase in capital, provided that their capital funds are adequate in relation to their liabilities.

Mr. GOLDSBOROUGH. When you refer to the capital, you mean the capital and surplus combined?

Mr. ECCLES. What is that?

Mr. GOLDSBOROUGH. You mean the capital and surplus combined?

Mr. ECCLES. The law requires $50,000 capital at the present time, and many banks——

Mr. GOLDSBOROUGH. I know, but I think you say, "Providing its capital is adequate"?

Mr. ECCLES. No; I would think you should take the capital and surplus in determining the adequacy.

Section 303: The suggested modification of the pension provision is for the purpose of giving Board members a greater degree of independence. It has been suggested that each member of the Board, regardless of age, who has served as long as 5 years, whose term expires and who is not reappointed, shall be entitled to a pension on the same basis as though he were retiring at the age of 70. I discussed that to some extent yesterday.

Section 203: It has been suggested also that a Governor of the Federal Reserve Board, who is not redesignated by the President may, if he chooses, continue his membership on the Federal Reserve Board. That is the way the law is now, and the new bill that is being considered, as you will recall, provides that his term as member of the Board shall cease when he is no longer designated as Governor. It has been suggested that, as a result of that, the President could designate each member of the Board and then no longer designate him, and finally create a new Board completely. So, in order to eliminate that criticism, this is the suggested amendment: That the Governor could continue as a member of the Board even if he is not designated as Governor; but that if he resigns from the Board upon not being redesignated, it would be considered that he had served out his term and he would not be precluded, by reason of having resigned under those circumstances, from entering business for a period of 2 years.

In section 205, it is suggested that authority over open-market operations be vested in the Federal Reserve Board, but that there be created a committee of 5 governors of the Federal Reserve banks selected by the 12 governors of the Federal Reserve banks, and that the Board be required to consult this committee before adopting an open-market policy, a change in the discount rates, or a change in member bank reserve requirements.

Mr. GOLDSBOROUGH. Is there any interpretation in your suggested amendment as to what the consultation would consist of? Expressing it another way, would the Board be bound to accept the suggestion of these five men, or any one of them?

Mr. ECCLES. No. It is a question of giving the governors a hearing and making a record before the Board can act; but the Board would have the final responsibility for the action.

Mr. GOLDSBOROUGH. That is the intent, but I am not sure it is entirely clear. Of course, that can be clarified.

Mr. ECCLES. Yes; that is the intent. The Board would be charged with the responsibility and they would have the power to initiate, but before taking action they would be required to advise with and get an expression of the views of the committee of the governors, or the governors could initiate and come to the Board and make their recommendations for the consideration of the Board.

Mr. FORD. Should there be a time limitation on how long you have to wait for that consultation?

Mr. ECCLES. Well, I would provide that, of course, the Board should be able to make rules with reference to that.

Section 209: It is suggested that the Board should not have the power to change the reserve requirements by Federal Reserve districts. I discussed that, I think, to some extent yesterday. It has been suggested, further, that the member banks be classified in the two groups, one comprising member banks in the central reserve and reserve cities, and the other all other member banks. Changes in the reserve requirements, therefore, would have to be either for the country as a whole, or for the financial centers, as against the country districts.

Section 210: Real-estate loans: It has been suggested that the conditions on which real-estate loans may be granted by member banks be left to the discretion of the Federal Reserve Board, to be determined by regulations. I see no objection to accepting also some geographical limitation as to where loans could be made, that is, some specified distance from the banking houses. Of course, there is no limitation as to the field where banks can loan funds on bonds, but there seems to be a good deal of opposition to the elimination of the geographical limitation on real-estate loans. I do not believe it is of sufficient importance to have any disagreement over.

Well, now, those are the suggested modifications.

Mr. FORD. Just one word on that geographical limitation: In cities where the Federal Reserve banks to whom the various banks have to go for these loans, if the geographical limitation is put in there, very often there is very keen competition between cities and the city in which the Board is located, and if it were limited, it might mitigate against another city that did not have a bank, as to the character of loans that they would be willing to discount. With the geographical limitation, I think, in many instances, it might have a very bad effect.

Mr. ECCLES. You mean in the case of real-estate loans?

Mr. FORD. Yes, sir.

Mr. ECCLES. Well, I do not just get the point of your question.

Mr. FORD. Let me illustrate it in another way: Let us say that the main branch of the Federal Reserve is at San Francisco. Well, now, the geographical limitation, for instance, leaves the city of San Diego out of that limitation; and if there were some loans coming in from there, and there happened to be competition, for instance, in water transportation between those two points, and somebody on that Board was anxious to work a little against San Diego, it might be possible and something like that might come up, because it has come up in other things.

Mr. ECCLES. Well, in the case of San Diego, in that case San Diego would discount with the Los Angeles branch.

Mr. FORD. That limitation would not touch the branches?

Mr. ECCLES. The limitation is a mileage limitation from the bank that makes the loan, the idea being that the bank in an area should loan funds in the area in which it is acquainted, where the officers can personally be informed as to the property upon which they are lending; whereas, if there is no geographical limitation, the funds may be loaned in far-removed areas, a thousand or two thousand miles away, as the case may be.

Mr. FORD. If it applies to branches, that is all right.

Mr. ECCLES. The advantage of taking the limitation off is this: That in an area that has a surplus of funds beyond the demand for real-estate loans, it could invest those funds through some correspondent institution where there is a shortage of real-estate money, just as our insurance companies in New York and other points loan money over the United States and building and loan companies have loaned in a more or less wide area, and as the mutual banks loan in far-removed areas.

Mr. GOLDSBOROUGH. Mr. Hancock, you may proceed, if you desire.

Mr. HANCOCK. Mr. Chairman, I have listened with intense interest to the very able and enlightening statement made by the Governor of the Federal Reserve Board with respect to the purpose and philosophy of this important measure, and to his detailed explanation of its mechanics. It occurs to me, however, that since it is such an important and far-reaching measure and is somewhat intricate, that the committee should arrange immediately to have the Governor's testimony reduced to writing so that we may have a chance to fully analyze and digest it before we go into the questioning of the Governor. I hope the clerk will arrange to have this done at once.

I am not so much concerned with the mechanics as I am the purpose and philosophy of the bill. How it will be administered is, of course, vitally important.

I want to ask the Governor what is the difference between this measure and an outright central bank?

Mr. ECCLES. Well, I do not know just what you mean by "central bank." You mean by that a bank that is owned by the Government, and a bank with branches?

Mr. HANCOCK. I would like to have an explanation of that, and then I will ask you another question.

Mr. ECCLES. There are a good many different kinds of central banks and——

Mr. HANCOCK. Well, let me ask you this, Governor: What would be the practical difference between the system proposed herein and the Federal monetary authority that the committee last year studied, conducted hearings on, and considered?

Mr. ECCLES. I am not familiar with what the committee worked on last year. I could not give you a comparison between Federal Reserve operations and what was proposed under that bill, because I am not familiar with it.

Mr. HANCOCK. Well, briefly, here is what the Federal monetary authority undertook to do: It undertook to set up what you might term a supreme court of finance insulated against political and commercial banking domination, and vested in that supreme court of finance or authority the sole note-issuing power of the Nation. It would have owned and controlled all of the gold, all of the metallic base; and it would have had the right to control the open-market operations through the sale and purchase of Governments, the control of the rediscount rate, and other essential powers to control or regulate the volume and cost of money for the national welfare.

Mr. ECCLES. Speaking of the central bank, the Federal Reserve System has always been expected to perform certain functions of a central bank. It was set up on the basis of a certain regional autonomy, due, I suppose, in part, to the opposition to centralization in this country at the time the Federal Reserve System was set up, and due, also, in part, to the size of the country and the different economic conditions that existed in the different regions. The Reserve Board was set up as a coordinating agency for these 12 banks, which have 25 branches.

The proposed bill in no way changes the physical structure. The ownership of the Federal Reserve bank is left with the member banks. In most of the countries of the world, the central bank is a privately owned institution. Instead of being owned by the member banks, it is owned by the public.

There is no change being made in the number of directors, 9 directors, and the majority of them are selected by the stockholders of the member banks—6 of the 9. A limitation is being put, however,

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upon the terms of these directors. The general structure of the bank is not being changed.

It is proposed, however, that the appointments of governors should be approved by the Board. That is so that they would be in a more direct relationship, a more responsive relationship to the Federal Reserve Board, so that the Board's coordination of the system would be through the governor, rather than through the chairman and agent. This is the reason for the proposed combination of the offices of Governor and Chairman. Such coordination would be further effected through the Board's control over open-market operations and discount rates. The Board today approves the discount rates. There is no change in the matter of the discount rates proposed in the bill, but there is a change regarding the open-market operations.

Mr. Hancock. And that is the heart of the bill, is it not?

Mr. Eccles. Well, it is the most important feature and——

Mr. Hancock. That is the main method or means by which you control the supply of money?

Mr. Eccles. Well, the question of reserve requirements is also a feature secondary——

Mr. Hancock. Secondary?

Mr. Eccles. I think secondary to the other features.

Mr. Hancock. But the open-market operation is the primary and most effective feature?

Mr. Eccles. That is right. The other is secondary. The open market is the primary feature.

Mr. Hancock. And under the terms of this bill, the open-market operations are vested entirely in a Government board?

Mr. Eccles. No; vested in the Federal Reserve Board under this bill if changed in the manner which has been suggested.

Mr. Hancock. Yes, but under this bill, that Board is appointed by the President and confirmed by the Senate?

Mr. Eccles. That is right, for terms of 12 years, and the open-market power is vested in the Board. Today the Board has a veto power over open-market policy. The governors have an open-market committee. The 12 governors elect a committee of 5, and that committee is a committee charged with the responsibility for the initiation of open-market operations. The Federal Reserve Board either approves or disapproves or induces them to modify their program; but the Board cannot initiate. And then, if the policy is initiated by the open-market committee and is approved by the Board, the Board is not in position to require that the banks carry out the policy. So it is proposed in this bill to place the authority and responsibility in a small body, and the Board——

Mr. Hancock. Under the bill proposed you can initiate the policy and then enforce its execution, can you not?

Mr. Eccles. That is right.

Mr. Hancock. So it really gives you complete control over the money supply?

Mr. Eccles. That is right. Now, to that extent, it is centralizing that function to a greater extent than it has ever been centralized. Responsibiliy is always felt more keenly when it becomes a personal responsibility, and it seems to me it is desirable to place that responsibility in a small body, either in the Board or somewhere else.

The responsibility for the exercise of these important functions of monetary control should be in one body, either the Board or some other body. It should not, to my mind, be divided to such an extent that it can result in obstruction, lack of action, lack of coordination, and lack of a feeling of responsibility.

There are many important functions the Reserve banks have outside of the open-market operations, and there is no idea of taking away from the regional banks all of the functions which they now have. As a matter of fact, if the Board is given the authority it is requesting here in the bill, to delegate some of its authority, I believe that there are some of the duties that the Board could delegate to the regional banks beyond the responsibilities the banks now have. The regional banks carry the reserves of the member banks. The regional banks pass upon the credits to the member banks. It is through the regional banks that the Board operates in the approving of banks for membership, in the issuing of voting permits, in the examinations of banks, in the matter of reduction of capital structure, or in the matter of consolidations. All of the important relationships with all of the banks and the public in the area where the Reserve banks are, are handled by the management and directors of those banks; and there is no idea of taking away any part of this, or attempting to centralize those functions here in the Federal Reserve Board.

Mr. HANCOCK. In effect, Governor, does not this bill undertake to bring back home the sovereign power vested in the Congress to coin money and regulate the value of it?

Mr. ECCLES. Well, it brings to the Federal Reserve Board the power, and, of course——

Mr. HANCOCK. And through that Board back to Congress?

Mr. ECCLES. That is right, because——

Mr. HANCOCK. Is it not an unpleasant fact, Governor, that this power has been farmed out to private interests for years and years?

Mr. ECCLES. Well, the power really has not been exercised to any great extent. Up until 1922 there was not any recognition of the fact that, by the open-market operations, you affected the supply of money. There was no special machinery for open-market operations in the original Federal Reserve Act. In 1922, during a period when some of the banks were buying securities as investments, it was observed that it influenced the situation in New York, and they began to realize that these 12 Reserve banks, acting independently, in buying and selling for their own investment account, from a purely earning standpoint—in other words, operating as commercial banks would—had a real influence and effect on the money market. The result of that was a self-appointed committee of governors to work together, so as to have a coordinated program of buying and selling; and I believe it was not until 1933 that the open-market committee was recognized in the law.

Mr. HANCOCK. Governor, based on your statement yesterday, would it be unfair to interpret this bill as the last clear chance to save the autonomy of private banks of America?

Mr. ECCLES. Will you state that question again?

Mr. HANCOCK. I said, would it be fair to interpret this bill as the last clear chance to save the private commercial banks in America from their own destruction?

Mr. Eccles. Well, that would be a question rather difficult for me to answer.

Mr. Hancock. I am asking you the question, Governor, in the light of what you said yesterday.

Mr. Eccles. I think this bill will certainly tend to make it possible for the private banking system to function in a much more satisfactory and adequate manner than it has in the past.

Mr. Hancock. Nothing could be more desirable.

To use the expression that you used before the Senate committee in 1932, this measure, idealistically speaking, is designed to bring the money world back into relations with the real world, is it not?

Mr. Eccles. Well, it is designed to create a condition of stability, stable business, we will say, so far as it can be done through monetary policy. The important thing today is not so much, as so many people believe, to increase the quantity or volume of money, as it is to increase the velocity of money that is already in existence.

Mr. Hancock. I believe you take the position as I do that the velocity of money has a greater effect upon business activity than the quantity or volume?

Mr. Eccles. The volume of money is a very important element, and I think that, in a period of great business activity and full employment, or reasonably full employment, to reduce the quantity of money is very effective in controlling inflation. A small reduction in the quantity of money, through open-market operations, in certain periods, would be very effective.

Mr. Hancock. It always, however, tends to decrease business activity?

Mr. Eccles. That is right, and it is—well, it would tend to decrease business activity, and possible excess reserves would be wiped out. That would force the banks into borrowing, and that would materially restrict credits and raise rates, and tend to slow up the volume of business. However, when you permit a condition to develop, such as has developed during the past 4 or 5 years, when you first had a great period of deflation, of loans held by the banks, and bills held by the Reserve banks were allowed to run off, the volume of money was being extinguished at a terrifically rapid rate. From 1929 to the period of the bank holiday, about one-third of our total bank deposit money was extinguished, largely, through the liquidation of bank credit. This liquidation was forced upon the banks in part by their inability to go to the Federal Reserve banks with assets and meet the withdrawals of depositors, who were hoarding their funds, because of banks failing.

Mr. Hancock. It was an emergency situation and the very time the banks should have stepped in boldly as a rescuer or savior? Of course they were no able to go as far as they could go if this bill is passed.

Mr. Eccles. Well, two things seem to me to have been necessary.

Mr. Hancock. In other words, the Reserve banks were affected by the same emotional disease that the member banks were; is that not correct?

Mr. Eccles. They were increasingly restrictive in the kind of paper on which they would extend credit, and, of course, the law put limitations on the type they could take. Now, as to whether or not, by acting sooner or acting more vigorously in the open market, they could have stopped the period of deflation, that is, of course, a debatable question. Some will argue that had they acted more vigorously and sooner than they did, when there was a tremendous shortage of funds due to hoarding and due to the gold that was pulled out of the country and went abroad, that it would have turned the tide of deflation.

Mr. HANCOCK. There was never, during that period, coordinated action on the part of the Federal Reserve System as a whole, was there? Were not some banks operating at cross purposes with others?

Mr. ECCLES. I do not know. I do not know exactly what you mean by "coordinated."

Mr. HANCOCK. I mean this: That some of their actions were not in unison or accord with a national policy, looking to unified operations for the good of the entire country?

Mr. ECCLES. Well, I think the governors met and discussed the problem, and I think they also met here in Washington with the board and——

Mr. HANCOCK. I do not think there is any question about their having met, but what unified effective policy did they agree on?

Mr. ECCLES. Well, they reduced the discount rate, and they bought securities in the market, beginning with the autumn of 1929, but more vigorously after the passage of the Glass-Steagall Act in February 1932.

Mr. GOLDSBOROUGH. I will say that they continued that until the danger of the passage of the Goldsborough bill was over, and then it immediately stopped.

Mr. HANCOCK. Governor, what constructive thing did the Federal Reserve Sytem do, after deflation was halted, to aid in bringing about recovery? Would you mind telling this committee that?

Mr. ECCLES. Well, of course, in view of the fact that the entire banking structure collapsed and had to completely close, it is difficult to imagine how anything very much worse could have happened.

Mr. HANCOCK. Well, I believe in your statement made before the Senate committee in 1932——

Mr. ECCLES. 1933; in February of 1933.

Mr. HANCOCK. You referred to the fact that you considered the Federal Reserve System an emergency system; is that correct?

Mr. ECCLES. Well, I do not think so. I would not consider the Federal Reserve System an emergency system; it is a system that certainly should be able to regulate the volume of money. If the banks and the money system under capitalism cannot meet the emergency, the Federal Reserve System is the only agency we now have to do it. In other words, through the Federal Reserve System, we say that we succeeded in financing a war; and we know now this contributed very greatly toward the financing of the extraordinary expenditures of the war, in the absence of putting on taxes high enough to do that.

The Reserve System has, of course, been very helpful in the clearing of checks, and it has been a very great improvement over the system that was employed prior to the Federal Reserve System. It has speeded up immensely, immeasurably, the clearing of financial transactions throughout the country.

Mr. HANCOCK. Governor, if we had put on sufficient taxes during the war period, a large part of our present financial difficulties would have been avoided, would they not?

Mr. ECCLES. Well, I do not know that I could agree to that. I do not think that the financial troubles of the present are due to the war. We do not lack and did not lack in 1929 any material and physical thing that we had before the war and after the war. We had an increase in our total man power and in our capital production facilities.

The CHAIRMAN. Let me interrupt. Did not we experience our greatest period of prosperity in all of our history subsequent to the war and prior to this panic?

Mr. ECCLES. We had replaced every physical loss, and even the loss of man power as the result of the war by a very great amount from the end of the war up to 1929.

Mr. HANCOCK. Well, Governor, is it not a fact that our present war debts largely represent profits made during and out of the war?

Mr. ECCLES. Well, certainly, during the period of the war, we did not consume and use, as a nation, more than we produced. As a matter of fact, during that——

Mr. HANCOCK. And in that way, we did not impoverish ourselves?

Mr. ECCLES. We did not impoverish ourselves at all, because we used much less than we produced, because we furnished the Allies a tremendous amount of goods, which created the interallied war debts; so there was no occasion for a huge war debt, if the population had all been put upon a basis whereby there would have been no advantages to any group or class, and there would have been no profits as a result of that operation.

In other words, if the resources of the Nation had been mobilized in the interests of the Nation, for war purposes, we would not have needed any inflation, we would not have needed the credit that was extended. Our present situation indicates we are just as able now, in this country, to meet the problems of the depression as we would be to meet the problems of war. No one would question the fact that our ability to fight a war would depend upon the men and materials and our capital facilities in the form of our factories, systems of transportation, and so on. The question of money would not be the measure of our ability to fight a war in this economy of abundance. Neither is our ability to fight the depression in this economy of abundance a problem of money.

Mr. HANCOCK. It is a question of distribution?

Mr. ECCLES. Yes; it is a question of distribution. The depression, to my mind, was not brought about through a shortage in the volume; and by an increase in the volume of money after 1929 it would not have been possible to have avoided the depression. It might have deferred it or delayed it; but so long as we had such an inequitable distribution of wealth production as currently produced, so that our capital production facilities were all out of balance with the buying power of the people, the velocity was sure to slow up and a depression was inevitable.

Mr. HANCOCK. Governor, with respect to the question of debt—and then I will get to this bill again—I want to ask you this question, do you think a nation can impoverish itself by employing its men and materials in improving its equipment and resources?

Mr. ECCLES. No; I cannot see how a nation can impoverish itself by adding to or producing wealth. In my opinion, we might impoverish certain individuals if we do not distribute the wealth that is produced through giving employment.

Mr. HANCOCK. Then all we need today in this country of rich resources is, for our money to go to work; is that correct?

Mr. ECCLES. That is correct.

Mr. HANCOCK. Will this new bill help to restore confidence and put it to work?

Mr. ECCLES. Well, I cannot answer that; I can only express an opinion. It is my belief that it will; it is one of the factors that will help; it will make it possible for the banks to lend funds in fields in which they have been unwilling and unable to lend before. Whether or not they will find borrowers is another question. There is a great absence of people who are willing to borrow, even on long terms, or on any terms.

In connection with what I said, in order that I may not be misunderstood, I happened to read the other day an account of the last report of the Brookings Institute, which finds that the excessive savings went into speculation: Too much thrift held slump cause. It seems to me that has a very important bearing upon this question of the volume and quantity of money and the velocity of money.

Mr. HANCOCK. Said in a different way, you mean that too much labor went into capital goods?

Mr. ECCLES. That is right. [Reading:]

The institution, in the third of a series of investigations to ascertain whether maldistribution of income is a primary cause of the depression, found that the first need is for greater spending for goods rather than more savings.

Money going into savings, the report made public last night points out, is not immediately spent for consumption, and the rapid growth of savings in the twenties resulted in too much money going into speculation and not into actual buying of goods.

The report disputed several traditional economic concepts. Theoretically, according to one school of thought, savings go into the expansion of plant and other physical facilities, but the institution found that so much money was saved that there was a plethora.

Instead of going into either consumption goods or capital goods, it went into speculation which served to inflate the prices of securities and to produce financial instability.

In announcing the report, the institution cautioned that it did not suggest the individual of moderate means should, as a matter of policy, save less, but that "the problem is one of aggregate savings in proportions to aggregate consumption."

The phenomenon of an excessive supply of savings is, the report said, something new. In the past there has usually been a dearth of savings, with resulting difficulties in expanding the Nation's productive facilities.

The report further disputed the theory that business expansion begins with expansion of capital goods, holding rather that such expansion begins after people begin to buy.

The report noted that "a large part of the savings of individuals and business corporations has gone to finance Government deficits" since the depression.

The same institution, as I recall, gave the figures ofthe distribution of the national income—I think it was in 1929—showing that one-tenth of 1 percent of the families at the top of the list received the same income as 42 percent of the families at the bottom of the list; or in other words, the average income, per family, at the top, was equivalent to the average income of 420 families at the bottom.

Mr. HANCOCK. In the peak year, Governor, in 1929——

Mr. HOLLISTER. Pardon me, but I want to ask what report that is that he is quoting from?

Mr. ECCLES. That is the report of the Brookings Institute, The Capacity to Consume.

Mr. GOLDSBOROUGH. And that is the 42 percent the Brookings Institute wants to spend?

Mr. ECCLES. Well, the thing that they find is that that 42 percent was not responsible for very much saving. The one-tenth of 1 percent, of course, were unable to use their income in consumers' perishable and durable goods; and they, therefore, had to find an outlet in the investment field, or in the field of capital or producers' goods, until we reached a point where our capacity to produce was all out of relationship to our ability to consume but not our capacity to consume and——

Mr. HANCOCK. Which is a whale of a difference?

Mr. ECCLES. Yes; our problem is no longer one of production, which it has been for generations, while we were building the country, while we were a debtor Nation, and when we had a rapidly increasing population.

Our problem is one of distribution. By distribution we mean not the distribution of the existing wealth but the distribution of the wealth production as it is currently produced; and the most effective day to do that, in times of prosperity, is through the income-tax system. One of the greatest mistakes, I think, that was ever made during a period of prosperity was to reduce income taxes rather than to maintain them at the high war point and use the funds collected to reduce the Federal debt; and then when unemployment developed to use the Federal credit to take care of unemployment.

Mr. HANCOCK. Governor, I think that same report to which you referred just now also showed this startling information: That in the peak year, 1929, 68.9 percent of the American families had gross incomes of less than $1,500.

Mr. FORD. May I make an observation there, Mr. Chairman?

The CHAIRMAN. Yes, Mr. Ford.

Mr. FORD. In 1929 there were 22,000,000 people in the United States, at the peak of our prosperity, who were living at or below the subsistence line; there were 45,000,000 people that were just getting by; there were 25,000,000 that were fairly well off; there were 15,000,000 that were rich; and there were 10,000,000 wallowing in wealth; and those are figures which were gotten out by a responsible organization.

Mr. FISH. And what is the subsistence line?

Mr. FORD. It is just being able to live by a little help from the country or relatives or somebody else; just getting by.

Mr. FISH. On the basis of income, it depends on the cost of living, but what is a subsistence income?

Mr. FORD. Well, I do not know what it is, because it depends on the section. It might be $15 in one part of the country and might be $25 in another and $40 in another, depending on what part of the country you live in.

Mr. HANCOCK. Governor, do you subscribe to the thought or belief that the control of a nation depends upon the control of its credit?

Mr. ECCLES. I do not know that I understand your question.

Mr. HANCOCK. By that question I mean that unless the Nation, through its central Government, controls the credit or note-issuing power of the Nation the Nation cannot be used for the protection and welfare of all of the people?

Mr. ECCLES. Well, I think there must be a control over the money system.

Mr. HANCOCK. That means credit, does it not?

Mr. ECCLES. It is not necessary to control the credit relationships of individuals among themselves, nor the credit corporations extend on accounts, and so forth.

Mr. HANCOCK. Of course not; but our money system is 90 percent credit or check currency. You made that statement before the committee.

Mr. ECCLES. Well, 90 percent of our payments are made by checks on deposits, which is credit money; and it is necessary for a nation to exercise control in the public interest over the money system.

Mr. HANCOCK. Well, now, this bill is designed to insure control of the credit of the Nation in the interest of the Nation as a whole, is it not, and without interference with the normal functioning of the banks?

Mr. ECCLES. That is correct.

Mr. FORD. Otherwise, socialize it?

Mr. ECCLES. Well, it depends on what you mean by "socialize." Of course, I read yesterday a statement of Woodrow Wilson's conception of the Federal System, and I do not need to go beyond the statement of the President in whose administration the organization of this System was set up.

Mr. HOLLISTER. What is the purpose of that statement, Governor?

Mr. ECCLES. It is the purpose of setting up the System. He said:

> The control of the system of banking and issue must be vested in the Government itself, so that the banks may be the instruments, and not the masters, of business and of individual enterprise and initiative.

Mr. HOLLISTER. Did anybody ever suggest that the Government should have the control of issue?

Mr. ECCLES. He has suggested the control of issue——

Mr. HOLLISTER. Did anybody else ever set up the contention that the Government was only for issue?

Mr. ECCLES. The theory was that these banks would control the issue.

Mr. HOLLISTER. It was not the Government. The banks were not identical with the Government, and nobody ever suggested that, did they?

Mr. ECCLES. That is true, but the thought was, that the Federal Reserve Board and the chairmen of these banks, who were appointed, were the representatives of the Government, or the people through the Government.

Mr. HOLLISTER. The Federal Reserve Board was, but not the Federal Reserve System?

Mr. ECCLES. The chairman of the Federal Reserve banks was appointed by the Federal Reserve Board, and was at that time looked upon as the executive head of the banks.

Mr. HOLLISTER. And the chairman appointed by the Board was to completely control the individual Federal Reserve banks?

Mr. ECCLES. No; the Federal Reserve banks, of course, were to be controlled by their board of directors.

Mr. HOLLISTER. Who were not Government appointees?

Mr. ECCLES. That is right.

Mr. HOLLISTER. Except certain of them?

Mr. ECCLES. That is correct.

Mr. HANCOCK. Governor, I wanted to ask you one more question. Do you think that the legitimate consumer demand or requirements for credit in this country can and will be met, as long as banking is a career?

Mr. ECCLES. Why, yes; I think so.

Mr. HANCOCK. I asked you that question because I understood you to refer to the fact that by providing independence or competence for Federal Reserve Board directors they could take hold of such positions and make careers of them and not have to look to outside income.

Mr. ECCLES. That is right.

Mr. HANCOCK. It is my thought that banking should never have been a career but always a profession. I hope you understand what I mean.

Mr. ECCLES. Are you speaking of the private commercial bank, or are you speaking of the Federal Reserve bank?

Mr. HANCOCK. I am speaking of all kinds where the public is involved and their welfare at stake.

Mr. Chairman, they are all the questions I care to ask at this time, but I reserve, of course, the right to discuss with the Governor the various sections of the bill. In your absence I made a request that the hearings up to now be printed, because it is humanly impossible for any man to digest all of the statements and suggestions made by the Governor, without having a written statement before him.

Mr. ECCLES. Let me answer Mr. Hollister's question about the control of issue because my associate has brought to my attention this statement in the law:

> The Board shall have the right, acting through the Federal Reserve agent, to grant in whole or in part, or to reject entirely, the application of any Federal Reserve bank for Federal Reserve notes.

Mr. HOLLISTER. In other words, the Federal Reserve Board may limit the issue of notes, but may not increase the issue of notes at will?

Mr. ECCLES. That is right.

The CHAIRMAN. Gentlemen, it is probable that the H. O. L. C. bill will be taken up in the House tomorrow. I am not in a position to say definitely about that, but I will know in a little w hile. I thought we would not have any meeting of the committee tomorrow, and we appeared before the Rules Committee and asked for a rule, and we asked that we be given 1 day for debate of something like 4 hours on the bill. We are hoping that request will be granted. As soon as I can see the Speaker I can ascertain whether the bill will come up tomorrow or not. If it does, I wish you gentlemen would help me give information about it. If the bill comes up tomorrow, I suggest that the committee hold a meeting tomorrow afternoon at 3 o'clock, and just as soon as I can get that information I will have it telephoned to your office.

Suppose we say that we will meet at 3:30 this afternoon if the bill comes up.

Mr. HANCOCK. If the bill does not come up tomorrow, Governor Eccles will come back. Is that correct?

The CHAIRMAN. If the bill does not come up, Governor Eccles will come back; yes.

(Thereupon, the hearing in the above-entitled matter was adjourned temporarily.)

BANKING ACT OF 1935

MONDAY, MARCH 11, 1935

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

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

The Chairman. Gentlemen, we have Governor Eccles with us this morning to resume the discussion of this bill, H. R. 5357, and it is Mr. Williams' time to ask questions, if you desire, Mr. Williams.

Mr. Williams. All right. Governor Eccles, I understand the main purpose of title II of this act is to enlarge and further centralize the powers of the Federal Reserve Board, in order that it may have increased influence and power over the expansion and contraction of credit of this country. That is to be done mainly through the open-market committee, fixing discount rates and controlling the reserves of the member banks. Those are the agencies through which it is to operate. Am I correct in that assumption?

Mr. Eccles. That is correct.

Mr. Williams. Now, to what extent by the operation or by the use of these agencies by the Federal Reserve Board, can the general commodity price levels in this country be controlled, in your judgment?

Mr. Eccles. It is impossible to say. The proposal to give to the Federal Reserve Board, with the advice of the Governor's committee, the responsibility for the use of these monetary controls, the discount rate, the reserve requirements, and the open-market operation is for the purpose of maintaining stable business conditions, insofar as this is possible by monetary means. A stable price level does not necessarily mean stable business conditions.

It seems to me that we are far more interested in full employment than we are in stable prices. If stable prices at some given index figure would leave an army of unemployed, it does not seem to me that this is the objective that would satisfy this country.

Mr. Williams. Well, you will agree, will you not, that it is very desirable, as far as possible, to have stable prices?

Mr. Eccles. Yes; I agree to that.

Mr. Williams. And that the purchasing power be the same yesterday, today, and forever, you might say, so far as we can make them so?

Mr. Eccles. I agree that wide and rapid fluctuations in prices are inflationary and deflationary and tend to create conditions that are unfavorable to business stability.

Mr. WILLIAMS. I judge you are not in favor of fixing certain commodity price levels as the goal toward which the Board should strive in its expansion and contraction policy?

Mr. ECCLES. I would prefer that it be not made the central objective of the banking bill.

Mr. WILLIAMS. Do you think it is practicable to do that?

Mr. ECCLES. I do not think it is.

Mr. WILLIAMS. On the other hand, there is considerable criticism in the country of the policy which places, entirely without any limitation, the matter in the hands of a few men, or the Board, this great authority; do you think there is any danger along that line?

Mr. ECCLES. The control over the volume of money and credit that the Federal Reserve Board can exercise through its use of three instruments of monetary control, would not necessarily tend to expand the amount of money in use in a depression such as we have at the present time.

Mr. WILLIAMS. Right in that connection, in the use of this word "money", what do you mean?

Mr. ECCLES. I mean demand deposits and currency.

Mr. WILLIAMS. Bank credit?

Mr. ECCLES. Yes; bank credit, deposits in commercial banks and currency. More precisely it is deposits subject to check, exclusive of bank float and interbank deposits, plus United States Government deposits.

Mr. WILLIAMS. Bank demand deposits?

Mr. ECCLES. That is right.

Mr. WILLIAMS. And currency?

Mr. ECCLES. Yes; that is right.

Mr. WILLIAMS. Is that what we mean when we talk about money now?

Mr. ECCLES. That is right.

Mr. WILLIAMS. I want to have that understanding as we go along.

Mr. ECCLES. That is correct.

Mr. WILLIAMS. Now, you say it would not necessarily result in expansion, that the policy should not or might not result in expansion during a period of depression?

Mr. ECCLES. You may create excess reserves through your open-market policy, but unless the borrowers are willing to borrow from the banks, and the banks are willing to lend to borrowers, you would not create a further increase in your money supply. You would increase the reserves of member banks, which would make for an inducement for the banks to lend and tend to result in a reduction in rates of interest, making for cheap money; but you must have borrowers who are willing and able to borrow before you can create additional money.

Mr. WILLIAMS. Is there no relation between the quantity of money and the volume of business that the country does?

Mr. ECCLES. No exact relation. The volume of money is an important factor, but the use of that money is an equally important factor in determining the amount of business.

Mr. WILLIAMS. Well, now, going back, for instance, to 1928, with a certain volume of money at that time and amount of business, how does that compare, we will say, with 1933?

Mr. Eccles. In 1928 it was estimated that the national income was about $83,000,000,000. According to the Department of Commerce's figures, in 1933 the national income was about $47,000,000,000. The money supply in June 1928 was $26,400,000,000 and in 1933 it was $19,900,000,000. The ratio of the national income to the volume of money was 3.12 in 1928 and 2.35 in 1933. That brings out the point that I think you have in mind. I would estimate that in 1934, with a national income somewhere between $50,000,000,000 and $55,000,000,000, with an average volume of money of around $23,000,000,000, the number of times that your volume of money turned over was very little over two times. At the same rate of velocity that existed in 1928 and 1929, with the present volume of money, the national income should now exceed $75,000,000,000, which indicates that simply increasing the volume of money does not increase the national income proportionally. It seems to me that the reason for that is quite obvious.

The distribution of the ownership of money determines whether or not it is going to be put into use. Money is put into use by corporations and individual investors, who are led to believe that there is a profit in the investment or use of funds.

Mr. Williams. Well, then, did the increase in the volume of money build up reserves in the banks of the country? Would that not stimulate business itself, to the extent that it would make more money available, and would lead the banks, by reason of the unusual and unnecessary amount of money on hand, to try to get it out into the field of action? In other words, it would not be earning them anything, and it would furnish them an incentive to lend on more reasonable and better terms, would it not?

Mr. Eccles. It has caused a very great reduction in interest rates, which is an inducement to the borrower, to the extent that the borrower can use the money profitably. Money is created by debt. Our banking system creates money——

The Chairman. Right there, Governor Eccles, you say money is created by debt; you mean by that, bank credit?

Mr. Eccles. Yes; that is right. I mean that the banking system, the process of loaning money, extending credit, increases bank deposits. In the absence of individuals and corporations who are willing and able to borrow, the banks have created additional funds by purchasing Government bonds. The purchase of Government bonds has increased bank deposits.

Mr. Williams. Well, the volume of money times the velocity represents the national income, does it not, but they have both got to be there——

Mr. Eccles. They have both got to be there; yes.

Mr. Williams. You have got to have volume and velocity like you have in physics to have momentum?

Mr. Eccles. That is right. You cannot have velocity of the means of payment unless you first create a means of payment. You may create a means of payment and if it is in the hands of those who are unwilling to spend it, you do not create business activity.

Mr. Williams. Now, Governor, let us go to the question in this second title here of issue by the Federal Reserve banks. This act, as

I understand it, removes the necessity for any specific collateral back of any particular issue?

Mr. Eccles. That is right.

Mr. Williams. And simply permits the banks to issue upon their assets? Of course, all of that is to be done under the rules and regulations of the board, I assume, the Federal Reserve Board? Now, in other words, who is going to control how much they issue?

Mr. Eccles. The volume of notes issued depends in the first instance on the demand for cash by the public and more remotely on the amount of deposits the Federal Reserve banks have created for their member banks, either by extending loans to them or by open-market operations.

Mr. Williams. Who is going to determine whether an issue has back of it sound assets, or not?

Mr. Eccles. The Federal Reserve banks' credit departments will determine that by the type of loans or type of credit which they extend to the member banks.

Mr. Williams. Now, let me see that I understand. The policy that has been heretofore followed has been that the Federal Reserve agent has had charge of that, has he not, or a representative of the Board?

Mr. Eccles. The Federal Reserve agent holds the collateral, consisting of gold certificates, eligible paper, and Government bonds. Originally it had to consist of gold and eligible paper. The Glass-Steagall Act of 1932 permitted Federal Reserve notes to be backed by Government bonds in the absence of a sufficient amount of commercial paper.

Mr. Williams. The application for issue is made to the Federal Reserve agent?

Mr. Eccles. That is right.

Mr. Williams. And he was required to have sufficient assets, in his judgment, back of that issue; that is, they were required to put up with him particular assets on a particular issue that they called for; is that correct?

Mr. Eccles. It was figured as a whole, the total amount of notes that each Federal Reserve bank had outstanding, backed by gold certificates and bonds and other collateral that was deposited with the Federal Reserve agent. But it seems to me that, in order to understand what is back of the Federal Reserve notes, we must consider the balance sheet of the Federal Reserve bank. The liabilities of the Federal Reserve bank to the public consist chiefly of deposits of the member banks and of Federal Reserve notes.

Against these liabilities the Reserve banks hold assets, consisting of investments in bills, Government securities, discounts to its member banks, and gold certificates.

It is impossible to issue Federal Reserve notes as liabilities without either an offsetting decrease in deposits or an offsetting increase in assets, in the form of gold certificates, Government bonds, eligible bills, or loans to member banks; and the only question that could arise regarding the security back of Federal Reserve notes would be in connection with loans which the Federal Reserve bank made to the member banks. If they made loans which were bad, whether eligible paper or whether loans secured by what would be considered as sound assets, and the losses on those loans were in excess of the capital and surplus of the reserve bank, then in theory the United States Government would have to be called upon to make good the guaranty of the Federal Reserve notes outstanding. But that is the only way in which there could be any question as to the backing of the Federal Reserve notes. At all of the central banks, except the Federal Reserve System and the Bank of England, notes are issued without any specific backing.

Mr. Williams. Now, Governor, I want this clear in my mind——

Mr. Hollister. May I ask one question right there, Mr. Williams?

Mr. Williams. Yes.

Mr. Hollister. Is it not true, however, that there is a statutory limit in most of the countries as to the amount of that issue?

Mr. Eccles. Well, I could not say.

Dr. Goldenweiser advised me there is no such statutory limit.

Mr. Williams. Let me ask you this question: In the application of a reserve bank under our present system, to the Federal Reserve agent for an issue, has that application ever been denied?

Mr. Eccles. I do not think so.

Mr. Williams. When an application is made, who passes on it?

Mr. Eccles. That is a formal matter; it is almost an automatic operation. The amount of notes that any Reserve bank requires to meet the demands of its deposits would be turned over to it by the Federal Reserve agent in exchange for the necessary collateral lodged with the Federal Reserve agent.

Mr. Williams. Now, are you saying that would be left entirely to the Federal Reserve banks?

Mr. Eccles. The amount of issue will be determined by the call which the member banks make for currency, and when they make a call for currency they must have deposits with the Reserve bank, just as an individual who wants currency must have funds in a commercial bank to be able to draw down that currency.

Mr. Williams. The part I am trying to get at is whether or not the central Board, the one that has control or the one you want to place more power in—whether or not they have control over the amount of issue of each one of these Federal Reserve banks?

Mr. Eccles. The Federal Reserve Board has technical control over the amount of issue under the present law, but it has found that it is useless to control note issue after the member banks have acquired deposits, and under the proposed law the Federal Reserve Board would not have this purely technical or theoretical control. The reason that the control is only theoretical is that, when member banks wish to withdraw their deposits in cash, no Reserve bank can refuse to pay out the cash, and the Federal Reserve Board cannot take the responsibility for preventing it.

Mr. Williams. Then, the Federal Reserve agent simply is an administrative officer; he has no discretion about it, but he is simply a trustee with these funds in his hands?

Mr. Eccles. The Federal Reserve bank would have to close if the member banks asked for currency in lieu of their accounts and were refused.

There is no more justification for requiring specific collateral back of Federal Reserve notes, which are the liabilities of the Reserve banks, than there is for requiring specific security to be pledged against the deposits of the Federal Reserve bank. Why should Federal Reserve notes outstanding be given a preferred status over the deposit liability of the Reserve banks?

Mr. WILLIAMS. Then, do you think it is a sound policy for the Government to guarantee these notes and at the same time have no control over their issue at all?

Mr. ECCLES. I do not think that a controlled issue would be a particle different than an issue that is not controlled, because the Reserve banks are required to issue currency whenever member banks have deposits and desire to draw down those deposits in currency. It is in the determination of the volume of credit extended to member banks for the purpose of creating the deposits that the real control of the note issue lies. They cannot draw down currency unless they have established balances with the Reserve bank, and have put up acceptable assets, in which case they can drawn down their deposits in currency in the same manner that any individual depositor of a commercial bank is able to draw his deposits in currency. Whenever a bank is unable to pay out the deposits in currency, that bank must close.

Mr. WILLIAMS. They are turning out currency on what they call "acceptable assets" as security?

Mr. ECCLES. Who is?

Mr. WILLIAMS. The Federal Reserve bank? If a member bank wants to borrow money, how do they get it?

Mr. ECCLES. They put up collateral.

Mr. WILLIAMS. Who passes on that collateral?

Mr. ECCLES. The Federal Reserve banks.

Mr. WILLIAMS. And they get money for it? That is, the member banks get money for it?

Mr. ECCLES. Yes; they get credit.

Mr. WILLIAMS. And that is guaranteed by the United States Government?

Mr. ECCLES. They get deposit credit for it.

Mr. WILLIAMS. Of course, that is money?

Mr. ECCLES. Yes; that is right.

Mr. WILLIAMS. And the Government itself is back of it, and still it is simply the deposit of eligible security in the judgment of the Federal Reserve bank?

Mr. ECCLES. That is right.

Mr. WILLIAMS. And they have entire control and jurisdiction over it?

Mr. ECCLES. Over the assets which they will take, yes.

Mr. WILLIAMS. And pass on the question as to whether they are good or bad?

Mr. ECCLES. That is right.

Mr. WILLIAMS. All right.

The CHAIRMAN. Governor Eccles, do you mean that they have entire control over the kind of assets they accept? They pass upon the acceptability of assets entered as collateral as to solvency and technical eligibility, but when it comes to fixing the rules of eligibility under the present law, they are governed by the rules laid down in the act, are they not?

Mr. ECCLES. That is correct. They have discretion as to the acceptability of assets or as tc the type of paper which they will take from member banks, subject at the present time to the eligibility requirements of the Federal Reserve Act.

In the future, if the present eligibility features of the act are removed and discretion given to the Federal Reserve Board to determine the eligibility requirements, the Reserve banks would have discretion within the rules and regulations laid down by the Federal Reserve Board. However, it would not be mandatory and it is not mandatory in the present law, that the Federal Reserve banks loan to member banks. They simply have authority to loan to member banks upon what is considered eligible paper.

The proposed amendment would give the Federal Reserve banks the power to loan to member banks on paper submitted to them, provided it met the requirements laid down by the Federal Reserve Board.

Mr. WILLIAMS. Yes; I understand the only difference in the existing law and the proposed law in that respect is, as it is now it is a part of the statutory limitation, and the other is to leave it to the rules and regulations of the Board as to what is eligible?

The CHAIRMAN. Let me ask you a question right there now: This might happen, technically speaking, that under the new law the Board could make regulations defining the eligible paper which would be more restrictive than the rules fixed in the present law, or if the Board saw fit, it could liberalize those rules, but it could work either way?

Mr. ECCLES. I think so.

The CHAIRMAN. So it does not work arbitrarily in either direction?

Mr. ECCLES. That is right.

The CHAIRMAN. Under the new bill, that is correct?

Mr. ECCLES. That is correct, yes.

Mr. WILLIAMS. What, in your opinion, should be the policy in that respect, liberalized or made more restrictive?

Mr. ECCLES. I think it would depend a great deal upon the conditions that confronted the country. In 1930 and 1931 it would have been in the interests of the banking system and in the interest of the entire country if the Federal Reserve banks had been permitted to loan to member banks on any sound assets, when many of them had very little or no commercial paper. The failure of the member banks to be able to borrow from the Federal Reserve banks forced a condition of great deflation. It forced the banks to refuse to extend loans as they fell due, and forced them to sell their bonds, their securities on the market. It resulted in liquidating or extinguishing, through credit contraction, about $20,000,000,000 of our total bank deposits, including time deposits. A good deal of that, of course, was the result of tying up deposits in closed institutions; but the total volume of deposits was greatly reduced, partly because of the inability of the member banks to get relief by going to the Federal Reserve bank, until we finally liquidated our banking structure to such a point that it became entirely frozen and closed.

And in getting it open, we finally had to recognize, as an emergency matter, that the Federal Reserve banks could loan to their member banks on all sound assets and that the Federal Reserve banks could issue notes secured by any sound assets, without resort to gold, Government bonds, or eligible paper.

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The CHAIRMAN. Now, let me interrupt you with something that should be said right here. It not only went to the extent that you have pointed out, but as an emergency measure we provided that such loans might be made to nonmember banks and currency issued to nonmember banks on the same rules and regulations; is that not what happened?

Mr. ECCLES. That is correct.

The CHAIRMAN. So we were forced to do that in the hour of distress, instead of having anticipated and provided for it in advance?

Mr. ECCLES. Yes; Mr. Chairman, that is correct.

Mr. WILLIAMS. Right in that connection, to what extent has it worked?

Mr. ECCLES. When people can get their money, they do not want it. I think the law was very effective, because it stopped banks from closing. Instead of the Federal Reserve being required to make loans to meet the demand, money which had gone into hoarding to the extent of anywhere from $1,500,000,000 to $2,000,000,000 in currency that was drawn from the banks beyond what was the normal use or need of currency, tended to come back into the banks. That enabled the banks to pay off the Federal Reserve banks, so that the amount of borrowing by the member banks from the Reserve banks today is practically negligible; whereas, in 1933, it was very large.

Mr. WILLIAMS. Then instead of increasing the necessity for borrowing has actually decreased it?

Mr. ECCLES. The requirements; yes.

Mr. WILLIAMS. That has actually decreased?

Mr. ECCLES. That is right.

Mr. WILLIAMS. There has been no demand upon the Federal Reserve Board since the passage of this act, I take it, from what you say, to borrow upon these general assets, I will say, which were not heretofore eligible, such as real-estate securities, long-term bonds, and things of that kind; there have not been any of them offered as security to the Federal Reserve banks for the purpose of obtaining loans?

Mr. ECCLES. I think it is section 10 (b) of the Federal Reserve Act, as amended by the Emergency Banking Act, which says that, under exigent circumstances, member banks are permitted to borrow from Reserve banks on their time or demand note secured to the satisfaction of the boards of directors of the Reserve banks. There was some use made of that provision, but not very much, because it put a bank in a position, where it applied for credit under the terms of that provision, of admitting that it was in great distress and exigent circumstances that it required special treatment by the board of the Federal Reserve bank, which meant that a bank would only resort to that, would only use the borrowing right, as the very last resort.

Mr. WILLIAMS. To what extent are real-estate loans used for the purpose of acquiring loans from the Federal Reserve?

Mr. ECCLES. I could not say to what extent, but there has been some borrowing from Reserve banks on bills payable backed by real-estate mortgages, and other collateral put up to secure the notes of the banks.

Mr. WILLIAMS. It is the intention of this bill, as I understand it, to so amortize real-estate loans as to make them eligible for discount?

Mr. ECCLES. Not for discount.

Mr. WILLIAMS. Well, for loans?

Mr. ECCLES. Yes.

Mr. WILLIAMS. As security for loans?

Mr. ECCLES. Yes; the bill provides that the act be amended to authorize Federal Reserve banks, subject to the regulations of the board, to discount for a member bank all commercial, industrial, or agricultural paper, and to make advances to a member bank on its promissory notes secured by any sound assets.

Mr. WILLIAMS. And that includes real-estate loans, of course?

Mr. ECCLES. Collateral loans, bonds, or any other sound assets.

Mr. WILLIAMS. And the purpose of this—not of this section, but of the real-estate section—is to so liberalize real-estate loans, by amortizing them over a long period of time, as to make them eligible as a permanent policy, to encourage additional loans by national banks and member banks on real estate, in order that they can, if necessary, dispose of those in time of distress and get money from the Federal Reserve banks?

Mr. ECCLES. So long as the commercial banking system is permitted to take savings deposits, I see no reason why those savings funds cannot be loaned on amortized real-estate loans in the community of the bank.

Mr. WILLIAMS. I agree with that, myself. I absolutely agree with that, but the purpose is, as far as it can be done, to liquefy real-estate loans?

Mr. ECCLES. Yes.

Mr. WILLIAMS. I think we all agree that that cannot be done as a policy, but as far as it can be done——

Mr. ECCLES. In a depression, only the Federal Reserve can liquefy assets. Real-estate loans are no different than any other type of paper in a great deflation.

Mr. WILLIAMS. Of course, they have been, for the reason that there has been no place to discount them.

Mr. ECCLES. In a great depression there is no other place to go. And they do not have to be real-estate loans. They may be loans on collateral, or they may be investments in bonds. When the market is depressed, as it was for a period of several years, that meant bankruptcy for any bank that liquidated its assets on the existing market, and that condition tended to close many banks.

Mr. WILLIAMS. Is it the thought of the Federal Reserve Board that there should be no limitation at all, upon these amortized real-estate mortgages?

Mr. ECCLES. You mean no limitation as to the percentage——

Mr. WILLIAMS. No; I do not mean on the percentage of valuation, but on the amount of the loan on each individual property.

Mr. ECCLES. There is no limitation now, under the real-estate provision of the National Banking Act under which they have operated for 20 years, with the exception of the limitation of 10 percent of the capital and surplus on any one loan.

Mr. WILLIAMS. Real-estate loans have not heretofore been eligible for discount with the Federal Reserve bank, except as an emergency measure?

Mr. ECCLES. There is over $2,000,000,000 of real-estate loans in member banks.

Mr. WILLIAMS. Have they been able to put those loans up with the Federal Reserve bank?

Mr. ECCLES. Only when an emergency was created and then they were permitted as an emergency matter to do that.

Mr. WILLIAMS. That is exactly what I say, except as an emergency measure, they never have been eligible for loans?

Mr. ECCLES. That is right.

Mr. WILLIAMS. This act proposes to make them eligible?

Mr. ECCLES. That is right.

Mr. WILLIAMS. And it is not thought to place any limitation, at all, upon them?

Mr. ECCLES. You mean limitation as to——

Mr. WILLIAMS. As to the amount? Here is an apartment house or hotel, or some other business institution, on which they want to make a loan of $100,000,000, for example——

Mr. ECCLES. One bank is limited in the amount of a loan they can make to any one borrower to 10 percent of its capital and surplus. So it has that limitation on it.

Mr. WILLIAMS. There is to be an increase under this act?

Mr. ECCLES. No; there is no change in it, at all.

Mr. BROWN of Michigan. As a matter of fact, it is a decrease, that is, 10 percent of the time deposits?

Mr. ECCLES. No; any bank can loan any borrower up to a total of 10 percent of its capital and surplus.

The CHAIRMAN. You mean that a loan can be made on any collateral or without collateral?

Mr. ECCLES. That is right. That has always been a provision of the Banking Act.

Mr. WILLIAMS. There is a provision in here, is there not, limiting it as applied to real estate?

Mr. ECCLES. No; the limitation is 50 percent of the time deposits and 50 percent of the appraised value of the property, which is the only limitation in the present act with reference to real estate.

Mr. WILLIAMS. It is expanded to what it was, in effect?

Mr. ECCLES. It is proposed to increase it from 50 to 60 percent, but the 60 percent also includes other real estate which is not included in the 50 percent in the present law.

Mr. WILLIAMS. Then loans to each institution heretofore have been limited to 25 percent of the capital and surplus on real estate?

Mr. ECCLES. Or 50 percent of its time deposits, whichever was greater.

Mr. WILLIAMS. What I am trying to get at is, it is expanded and enlarged, or is it not?

Mr. ECCLES. Yes; from 50 to 60 percent and up to 100 percent of its capital and surplus, whichever is greater.

Mr. WILLIAMS. Instead of 25 percent, it is now extended to the full amount of its capital and surplus?

Mr. ECCLES. Yes.

Mr. WILLIAMS. Or 60 percent——

Mr. ECCLES. Of its time deposits.

Mr. WILLIAMS. Of its time deposits?

Mr. ECCLES. Right. I suggested that those limitations be taken out of the act and the Federal Reserve be charged with the responsibility of determining regulations with reference to the real-estate loans.

Mr. WILLIAMS. Do you think there ought to be no limitation in that respect in it, except the regulations and rules of the Board?

Mr. ECCLES. That is right.

Mr. WILLIAMS. Or whatever limitation they saw fit to place?

Mr. ECCLES. That is right.

Mr. WILLIAMS. It ought not to be made a statutory provision?

Mr. ECCLES. That is right.

Mr. WILLIAMS. For the reason that it would give them more flexibility in the local communities, in the different localities, and at different times, under differing conditions?

Mr. ECCLES. Many of the nonmember State banks have, at the present time, more than 60 percent of their time deposits in real-estate loans, and some of the member State banks have more than 60 percent. That would mean that those banks would be required to liquidate their real-estate loans, in order to comply with the 60-percent requirement. Many State banks are not limited in the amount of their deposits that they can loan upon real estate.

Mr. WILLIAMS. I am very much concerned about this provision regarding real-estate loans, because I have been under the impression, by reason of the fact that these loans were short-term loans, not amortized loans, the banks were not able to handle them at all in a period of depression.

Mr. ECCLES. You mean under the present bill?

Mr. WILLIAMS. Yes; under the present act, the law as it is now?

Mr. ECCLES. That is correct.

Mr. WILLIAMS. And this act proposes to amortize them over a period of years and make them eligible for discount and furnish a market, somewhat, for them when the time comes when the banks have to have their money. I think, myself, it is a very wise provision in the law.

I believe that is all I care to ask at this time.

Mr. FORD. Might I ask a question, Mr. Chairman, just a question?

The CHAIRMAN. Yes; indeed.

Mr. FORD. Suppose the Federal Reserve has taken considerable volume of real-estate loans, what provision is there for the Federal Reserve bank, itself, to dispose of them, should they want to?

Mr. ECCLES. There would be no occasion for the Federal Reserve bank to dispose of them, so long as the member bank that borrowed the money was solvent. The member bank would owe the Federal Reserve on its bills payable, secured by mortgages which it had taken.

Mr. FORD. Suppose a member bank failed?

Mr. ECCLES. The Federal Reserve bank would be required to liquidate that mortgage or collect it or sell it, just as any other asset.

Mr. FORD. It could sell it, though?

Mr. ECCLES. Yes; it could sell it.

Mr. FORD. It is not just put in there and held static?

Mr. ECCLES. No; it would liquidate any asset or loan of the member bank which it held just the same as the member bank would undertake to liquidate the loan of an individual or corporation borrower.

Mr. WILLIAMS. Governor, there is this question that I want to ask you before I finally quit: Under our present system, or under the system proposed in this bill, what do the Federal Reserve banks pay for the privilege of issuing money?

Mr. ECCLES. They do not pay anything.

Mr. WILLIAMS. Do not pay anything?

Mr. ECCLES. No.

Mr. WILLIAMS. Now, as you know, there is considerable agitation, a good deal of comment in the country, about the Government owning these institutions. What would be the difference in effect if the Government did own them?

Mr. ECCLES. The individual member banks are the owners today. However, they are limited to 6 percent dividends on their stock. The earnings of the Reserve System in excess of 6 percent are held by the Reserve banks, and at one time——

Mr. WILLIAMS. Right in that connection, do they not belong to the stockholders?

Mr. ECCLES. Not under the law, not beyond the 6-percent dividends.

Mr. WILLIAMS. Of course, I understand we had, by legislation, to take it away from them. They were claiming to own it, were they not?

Mr. ECCLES. Yes; I think that there possibly was some claim to that effect. Personally, I would see no objection to requiring that the earnings of the Federal Reserve banks, beyond the limitation of 6-percent dividends to member banks, should be turned over to the Government when the surplus of the Reserve banks has reached an amount equal to its capital.

Mr. WILLIAMS. If the Government, however, can own and operate them as successfully as private institutions have done, why not give the 6 percent to the Government rather than to the private banks, as well as the reserves and the surplus?

Mr. ECCLES. It is now provided in the law that, in case of liquidation, any surplus remaining, after the payment of all debts, dividend requirements, and the par value of the stock, shall be paid to and become the property of the United States. I see no advantage in the Government taking over the stock of the Reserve banks.

Mr. WILLIAMS. It would not cost the Government anything to do that, would it?

Mr. ECCLES. I think it would; yes. The Government could not take over the stock without paying the member banks, any more than the Government could purchase any other asset without it costing it anything.

Mr. WILLIAMS. The purchase of the stock is already in the Federal Reserve banks, the purchase price of it?

Mr. ECCLES. That is right.

Mr. WILLIAMS. And if you took it over, it would simply own it instead of the Federal Reserve System owning it; the funds then with which the stock was paid for would be in the hands of the Government, would they not?

Mr. ECCLES. No; the United States Treasury would have to make payment to each member bank for its stock in the Reserve System, and the stock would be transferred from the ownership of the individual member banks, which own stock in the respective Federal Reserve banks——

Mr. WILLIAMS. Then, in taking over the System, we would get the assets that belong to the bank, that were paid in there by the member bank, would we not, for their stock?

Mr. ECCLES. When you bought the stock held by a member bank in the Federal Reserve System, you would naturally have—that is, the Government would naturally have the assets represented by stock which it purchased. That is correct.

Mr. WILLIAMS. And that is sound, really, after all; it would not cost the Government anything?

Mr. ECCLES. It might be—it would not cost it in the sense that it would be paying out funds without getting an equivalent asset; it would be an investment, rather than an expense, but it would cost the same——

Mr. WILLIAMS. They would get the stock?

Mr. ECCLES. That is right.

Mr. WILLIAMS. The stock the member banks now own? Now, I believe I asked a question awhile ago, that if the Government can own and operate the banks and issue money, instead of private institutions, why not do that and save the 6 percent that we are now paying.

Mr. ECCLES. You would not save 6 percent. For the Government to buy the stock, it would be required to raise the money that is used to purchase the stock, and in raising that money it would borrow it. If it borrowed it or raised it as they raised funds for other purposes, it would be required to pay whatever interest the Government debt was required to bear, in order to float the funds to get the money to buy the stock.

At the present time, the last offerings of Government securities bore a rate of 2⅞ percent; so in that case, you would save 3⅛ percent, the difference between 6 percent and 2⅞ percent.

Mr. WILLIAMS. Even so, why not save it?

Mr. ECCLES. The answer is, perhaps, that there is no more reason for the Government to invest in this business so long as it controls the money supply, than in any other business.

Mr. HOLLISTER. Might I ask one question there?

Mr. WILLIAMS. Yes; go ahead.

Mr. HOLLISTER. That would be on the theory that you could necessarily buy the stock at par. There is nothing, is there, in the law which would permit the Government, unless it is some new theory of confiscation hitherto unannounced—there is nothing by which the Government could expressly pay the member bank which owns a particular amount of stock in a particular Federal Reserve bank—there is nothing by which the Government could compel that bank to sell its stock at par if it chose to put a price on it of $200 or $300 or $400, is there?

Mr. ECCLES. That is a legal question that I do not feel I am prepared to answer.

The CHAIRMAN. Let me suggest that if you answer that question you also tell us what you would do about the stock of the State bank that is a member of the Federal Reserve System.

Mr. HOLLISTER. I am assuming that the Government is trying to buy stock in a Federal Reserve bank owned by individual member banks. That would be a matter of contract between the Government and each individual stockholder bank as to what the Government would be willing to pay and what the member bank would be willing to surrender its stock for.

Mr. ECCLES. That would seem to be the situation, and that is a legal question.

Mr. HOLLISTER. If you are not prepared to answer the question, I would rather not interfere with Mr. Williams. I do not want that to remain open without some comment, but I will refer to it later.

Mr. WOLCOTT. May I ask a question, Mr. Williams?

Mr. WILLIAMS. Well, yes.

Mr. WOLCOTT. Do I understand there is about $450,000,000 in that fund which has been turned over to the Federal Treasury over and above this 6 percent that was used—or we used one-third of it, did we not, in subscribing for stock?

Mr. ECCLES. The Federal Deposit Insurance Corporation? That was $140,000,000——

Mr. WOLCOTT. Was it not one-third of that fund?

Mr. ECCLES. No; it was more than one-third. The Treasury put $150,000,000 and the Reserve System——

Mr. WOLCOTT. $149,000,000?

Mr. ECCLES. I think it was $140,000,000.

Mr. WOLCOTT. $139,000,000, I think it was.

Mr. ECCLES. It made a total of $290,000,000 that was supplied by the Reserve banks and the Treasury.

Mr. WOLCOTT. Out of this Reserve System?

Mr. ECCLES. Out of the surplus of the Federal Reserve bank.

Mr. WOLCOTT. That could be used in payment of interest on these bonds, and after that the full 6 percent and all over and above that would go to the Government?

Mr. ECCLES. You mean, then——

Mr. WOLCOTT. This reserve that is already in it——

Mr. ECCLES. Yes; but that money was paid out by the Reserve banks to the Federal Deposit Insurance Corporation, and therefore the Reserve banks no longer have those funds. Those funds are owned by the Federal Deposit Insurance Corporation and——

The CHAIRMAN. Let me correct you just a moment.

Mr. WOLCOTT. We reimbursed the Federal Reserve bank for that, did we not?

The CHAIRMAN. We did not give any money to the Federal Deposit Insurance Corporation, but we merely subscribed to its capital stock.

Mr. ECCLES. Yes.

Mr. WOLCOTT. Indirect loans——

Mr. ECCLES. You do not think that the capital stock has very much value, then, do you? The law provides that the stock of the Federal Reserve banks can receive no dividends.

The CHAIRMAN. Tim will tell that.

Mr. ECCLES. The first banking bill——

The CHAIRMAN. It has made pretty good profit up to now.

Mr. ECCLES. Title I of the banking bill provides that the Federal Deposit Insurance Corporation's capital of $290,000,000 can be reduced to a nominal amount, and the balance put to surplus, so there would not be an impairment of capital, if it became necessary to put up these funds.

Mr. WILLIAMS. I would like to remark, in that connection, that so far as I am concerned, that will not be done, because I believe the banks themselves ought to bear that burden.

Now, coming back to the original proposition, Governor, whether or not the Government, as a practical proposition, can own and operate the Federal Reserve banks on as sound a financial basis, and render the same service and save these expenses, in the long run, if you have dividends that are being paid to the banks on the stock—if that can be done, why should it not be done?

Mr. ECCLES. I believe that the ownership of the stock by the Government would not necessarily be of any particular benefit or value in the operation of the Federal Reserve System. I believe that through the adoption of the provisions of this bill, the control would be effective and the responsibility fixed, and it should be just as effective in operating the system in the public interest as it could be operated if the Government owned the stock. It gets down to a matter of human intelligence. The management of the banks or the management of the System would have to be directed in some manner by some means. I see no reason why a management selected with the Government owning the stock would insure the System being operated in the public interest anymore than would be the case with the members of the Federal Reserve Board being appointed by the President of the United States, as is now provided, and the governors and chairmen of the individual banks selected by the local directors of the bank, subject to the approval of the Federal Reserve Board. There is a great advantage in keeping regional ownership and interest in the Reserve banks.

Most of the central banks of the world are privately owned. The bank which is just being set up in Canada, after a good deal of investigation and study and consideration, is owned by the public. I understand the stockholders elect the directors, but the Governor of the bank must be approved by the finance minister, and he has very great power and responsibility.

It is not so much who owns the bank as it is the way the bank is set up and the responsibility with which it is charged.

Mr. WILLIAMS. Is it your thought that Government-owned central banks can operate as economically and as efficiently and as much in the interest of the people of the country as our present system?

Mr. ECCLES. I do not think that the fact that it may be Government-owned, in and of itself, should make any difference. It may be operated as efficiently and it may not be operated efficiently. That, as I say, gets to the human problem, after all.

Mr. WILLIAMS. The ownership of it, in that respect would make no difference?

Mr. ECCLES. I do not think so, not necessarily. If the management of the banks, the personnel of the board consisted of efficient men who would feel independent to use their best judgment and thought in carrying out the affairs of the institution, the ownership would make no difference. If, on the other hand, people were appointed to operate the system for purely political reasons, rather than with reference to their qualifications, and they were made to feel subservient to the point where their best judgment was not exercised, then of course the system, under those conditions, would be badly and inefficiently and ineffectively operated.

Mr. WILLIAMS. Of course, the central idea in this legislation here, as is stated at the very beginning, is to try to increase and centralize the power in the Federal Reserve Board over the System, and I think properly so because I think that the Government and Congress and the administration should have control of the monetary system. It is a national system, of course, and there should be some central authority and central power responsible for it. The purpose of the bill is to create centralized authority, with complete management of the corporation or system.

Mr. ECCLES. With the board, which would be charged with responsibility for the monetary policy, working with and under the advice of the Governors' committee. There are many functions that would be carried out by the individual regional reserve banks, under the direction of their boards of nine directors.

Mr. WILLIAMS. But nothing that would influence the national monetary policy, without the consent of the central board?

Mr. ECCLES. That is right, except that the Governors would influence the policies of the board, as a result of their counsel and advice.

Mr. WILLIAMS. And that would be true whether they were representing the system governmentally owned or individually owned, would it not? Right in that connection the counsel that you propose of five——

Mr. ECCLES. Representing the 12 Governors.

Mr. WILLIAMS. What function does the advisory counsel now perform? Why could it not do the work proposed by the five?

Mr. ECCLES. I think it is more proper to have the executive heads of each of the 12 banks select their committee for the purpose of advising with reference to the policies, than to have the council advise. The Governors are in much closer touch with monetary problems. The members of the council are appointed, one from each Federal Reserve bank district by the Federal Reserve banks, and I think they consist entirely of commercial bankers from the Federal Reserve districts. They are in touch with the individual problems of their particular banks and their particular communities but I do not believe would be as able or as qualified——

Mr. WILLIAMS. They perform a very valuable function; that is, do they or do they not?

Mr. ECCLES. I have not been on the Federal Reserve Board except for a few months, and I have only had occasion to meet with the advisory council on two occasions. It would, therefore, be difficult for me to judge as to just how important the functions of that body have been over the life of the System.

Mr. FORD. Might I make a comment, Mr. Williams, please?

Mr. WILLIAMS. Yes.

Mr. FORD. Mr. Eccles, does not the demand for more complete control on the part of the Government indicate that the heretofore private control has not proved satisfactory to the Congress or the country?

Mr. ECCLES. I would not say that we had had private control. I think one of the principal difficulties of the money system has been that we had not placed the responsibility definitely upon any one body and given it the power and authority to carry out the responsibility that was imposed upon it.

Mr. FORD. It is too wide-spread, and they have been forced to operate and do what the Board wanted to do——

Mr. ECCLES. We did not have a statutory open-market committee until the Banking Act of 1933 created one of 12 Governors, and charged that body with responsibility for the initiation of the open-market operations and gave to the Board the power of approving or disapproving the recommendations of the Governors. But even then if the Board approved of recommendations of the Governors, one or all of the 12 banks could refuse to participate in the operation.

Mr. WILLIAMS. Has not the Board had that open-market policy through the years?

Mr. ECCLES. The Board was not charged by law with the duty of formulating an open-market policy.

Mr. WILLIAMS. None at all? Have they not intended to control, in any way, the expansion and contraction of money through open-market operation, through their advice and instruction to the member banks, and through their own operations?

Mr. ECCLES. The Board has acted in all these matters, but without a clear mandate of law.

Mr. WILLIAMS. They made no effort—do I understand that the Board itself has never made any effort at all along that line until the open-market committee of 1933?

Mr. ECCLES. The Board has attempted to influence the money market through changes in discount rates—that is, its right to approve of the discount rates—and it has even changed discount rates on its own motion. The need of the open-market operation was recognized in 1922, and a voluntary committee of governors was organized to carry out the open-market policy or program.

Mr. WILLIAMS. They had that policy then?

Mr. ECCLES. The open-market committee of the governors had the responsibility for that program. The Board itself has not been charged specifically with the responsibility for the open-market policy.

Mr. WILLIAMS. I understand, as a matter of law, but they have actually adopted the policy, have they not?

Mr. ECCLES. To what extent I cannot say. I am not as familiar possibly as I should be with the detailed history of the operation of the Board.

Mr. CROSS. May I ask a question just on that?

Mr. WILLIAMS. Yes.

Mr. CROSS. Now, is it not a fact that the Board, in April 1923 or May 1924, brought its pressure on the open-market committee and had them to buy \$510,000,000 of Government securities and reduced the rediscount rate from 4½ percent to 3 percent, and, as a result, put the wholesale commodity price level up to 11 percent, and the agricultural products up to 20 percent, and this action was repeated a number of times, and brought about the beneficial effect when they did it?

Mr. ECCLES. I do not know to what extent the open-market purchases and reductions in the rediscount rates had an effect upon the price level. It is true, I think, that, under certain conditions, to reduce the interest rates and increase the supply of money would be effective in increasing business activity, just as to increase the interest rates and reduce the quantity of money would tend to restrict business activities, and slow up borrowing, and possibly start a process of liquidation.

I do not believe that anyone can say to what extent open-market policy can be responsible for recovery or for depression.

The Swedish money management is one of the most interesting, I think, that we have in the world today and possibly has been as successful, or looked upon as being as successful as that of any other country, and the governors of the Swedish bank, in February 1932, made this statement:

> It follows that when forming its policy in view of fluctuations in the price level the Riksbank cannot but take into account the causes of such changes in prices. For it is essential to determine whether price movements are caused, e. g., by increased tariffs, altered exchange rates, or a tendency to inflation on the domestic market which may be looked upon as primary in relation to exchange rates. In any such analysis of price conditions, naturally other price indexes besides the Riksbank's own index of consumers' prices will also be taken into consideration. Obviously, in their endeavor to create as stable economic conditions as possible, the governors are also taking into account other factors than mere changes in the price level, particularly conditions affecting productivity and stocks in various industries.

The Chairman. Gentlemen, it is evident that we cannot continue much longer, in view of the business in the House. I am going to suggest that we adjourn until tomorrow morning at 10:30, and resume with Governor Eccles.

(Thereupon a recess was taken in the hearing until 10:30 a. m., Tuesday, March 12, 1935.)

BANKING ACT OF 1935

TUESDAY, MARCH 12, 1935

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

The committee met at 10:45 a. m., pursuant to adjournment, Hon. Henry B. Steagall (chairman) presiding.

The Chairman. The committee will please come to order.

Mr. Eccles, you may proceed now. Mr. Williams, do you have further questions?

Mr. Williams. I think not, Mr. Chairman.

The Chairman. All right, Mr. Cross.

STATEMENT OF MARRINER S. ECCLES, GOVERNOR OF FEDERAL RESERVE BOARD—Continued

Mr. Cross. Governor, you agree with the proposition that it is the duty of Congress to regulate the value of money, don't you; that is, Congress, acting through its agency which it sets up, shall do it? Of course, Congress itself does not do it.

Governor Eccles. I think that is a sovereign power given to Congress.

Mr. Cross. In the Constitution.

Governor Eccles. In the Constitution.

Mr. Cross. Now if that is the duty of Congress through its agency which it sets up, which of course, is the Federal Reserve System, don't you think that that agency ought to be independent of any outside influence or interests?

Governor Eccles. The agency should represent the Nation as a whole and should not be under the domination or control of any group or groups.

Mr. Cross. Should not the agency they set up, they being responsible and having the duty to perform, which they have delegated to that agency, should not that agency be independent of any outside agencies that come in with a different purpose in view?

Governor Eccles. It is my view that the Federal Reserve Board should be as independent as it is possible to create a body of that sort, charged with the responsibility of monetary policy in the public interest.

Mr. Cross. Now, Governor, isn't it a fact that the member banks of the Federal Reserve System are constantly wanting to go out in an opposite direction to what a wise policy would dictate, and that they are constantly wanting to inflate when they should not, and constantly wanting to deflate when they should not?

Governor ECCLES. Well, of course, there are a good many thousands of member banks, and I don't believe there is any uniformity of opinion. Inflation is brought about by creating a condition of easy money, expressed in low rates and excessive reserves, in a period when there is great business activity and hence a willingness to borrow.

Mr. CROSS. Yes. But now the point I am driving at is this, isn't it a fact that the member banks, and I am asking this just to get your reaction on this, are inflating when they should not be, and are deflating when they should be inflating? Here is what Governor Harrison of the New York Federal Reserve Bank said in the hearing in 1932, page 53:

> It is almost inevitable that the Federal Reserve System, or any central bank, will always have to go contrary to what the banks are doing. When they are deflating, we have to put pressure on them, and when they are deflating we have to boost things up. I think that is what we should do.

Isn't it a fact that the member banks, when they are trying to make money for their stockholders, in times when prices are high, they want, of course, to keep extending credit, credit, credit, and inflating, and naturally their class A directors—and class B directors, who are largely under the control of class A directors—wish to keep going forward and expanding, and don't you think that is a conflicting interest contrary to what the Federal Reserve System is intended to do?

Governor ECCLES. Of course, all I have is the record. From 1926 up to 1930, there was a very small variation in the supply of money. There was no inflation in the volume or the quantity of money from 1926 to——

Mr. CROSS. You refer there to all money—credit money?

Governor ECCLES. That is right; I refer to all money. I include in that demand deposits of member banks and of nonmember banks, and the currency outside the banks, in a word the entire circulating medium.

Mr. CROSS. That is over what period?

Governor ECCLES. That covers the period from 1926 to 1930.

Mr. CROSS. Will you please answer for me this question: There was a vast difference in velocity in those years?

Governor ECCLES. Yes; that is correct.

Mr. CROSS. And the Federal Reserve System can step in and control velocity, can it not?

Governor ECCLES. I don't think that the system has as much influence or velocity as it has on volume of money. I think the velocity of money is influenced more by the tax system than by monetary policy. Velocity slows up as business activity declines, or as deflation develops.

With the national income in 1929 estimated at beyond 82 billions, with the money volume at that time 264 billions, there was a velocity of 3.12; that is, each dollar on the average turned over 3.12 times in the course of the year in the process of making up the income of the community.

Whereas, in 1933, with the national income diminished from 82 billions to 46 billions, and the volume of money reduced from 26.4

billions to 19.9 billions, income velocity had declined in that period to two and a third.

Mr. CROSS. Yes; I understand, that Governor.

Now Governor, isn't it a fact that in order to control the situation you must still have a fixed policy and step in in time? "A stitch in time is worth nine", as one of the governors explained here in his testimony.

In 1929, Governor Harrison was insisting that something be done to stop the inflation, but it delayed too long, until the crash came, and of course then when that happened it was almost impossible to do anything. But it is shown by the record before that they would go out, putting out more securities, putting out more credit, more money, when the commodity prices rose, and then when they would stop that and sell, the reverse was true, because when you sell you take from the member banks their reserves, and that of necessity causes them to rediscount which they don't like to do, and that has the effect, of course, of steadying things, and slowing matters up—keeping them from rediscounting so much.

In order that I may get your reaction on some of these things, I will quote from the testimony of Dr. Sprague who appeared before the committee, I believe, in 1923:

> There would be, I think, an advantage from the passage of the bill. I probably agree with you that the defects in the operation of the Federal Reserve System are not so much errors of judgment they have made, but rather in the hesitating manner in which at times policies have been decided upon and then executed.

Without a goal to go to, and the boards come and go, the present Board may be gone in a short while, and with no goal to go to, the individuals differ and hesitate, and don't you think that is one of the great troubles, not having any goal to go to?

Governor ECCLES. You mean without a specific provision or objective required?

Mr. CROSS. Yes.

Governor ECCLES. You mean required as a part of the law?

Mr. CROSS. Yes; for Congress to set down the purpose, and have it the purpose of Congress, rather than to just turn the Board loose and let them go ahead as they did in 1928, as my recollection of the testimony shows, or 1924, when the Presidential election was coming on and they determined they should have prosperity. So, therefore, they got out and they bought Government securities, $510,000,000, shooting the price level up 11 percent, the farm products 20 percent, and built up commodity prices. Then, after that, they reversed the process, but no election was then coming on.

Now if you have a goal to go to, so they can't just shoot things up and down for some ulterior motive, they are fastened to an anchor, and don't you think it would be wise to have such a provision in the law?

Mr. WILLIAMS. You mean a price level, do you, Mr. Cross?

Mr. CROSS. Yes.

Governor ECCLES. I don't think there should be a mandatory provision to reach a certain price level. It may be of interest in that connection to consider the preamble of the recent law creating the Bank of Canada. It is short and might be considered as a basis for our own. It doesn't definitely fix a price level, but it does fix an objective:

Whereas it is desirable to establish a central bank in Canada to regulate credit and currency in the best interests of the economic life of the nation, to control and protect the external value of the national monetary unit, and to mitigate by its influence fluctuations in the general level of production, trade, prices, and employment, so far as may be possible within the scope of monetary action, and generally to promote the economic and financial welfare of the Dominion.

Mr. CROSS. They will all say that, of course. Everybody agrees to that, but isn't it a fact that our system is such, as I suggested, we go out and do a thing when a Presidential election is coming on, without any guide as to what the purchasing power of a dollar should be, no relation to the commodity-price level, and then turn them loose? They not only hesitate, but when they do jump, they will jump because of some purpose that is actuating them like a Presidential election.

For instance, let us take Dr. Sprague, who said in his testimony, "I have reached the conclusion that a stabilization amendment might prove serviceable."

Now, that was his testimony during that same time, in 1928.

Don't you think experience has shown those people that they couldn't have a stable policy under those conditions?

Now, I want to get your reaction on some more of his testimony.

Now, Dr. Miller, in the hearings in the Senate, in 1931, said:

It was my opinion expressed several times, in discussions at Federal Reserve meetings in the opening months of the year 1929, that the Federal Reserve System was drifting, that it was in the midst of a perilous situation without a policy—

and won't that, in your opinion, continue to be the case unless you have got a goal to go to?

Governor ECCLES. I think there should be a goal, but the goal shouldn't be a fixed-price level. I think the goal should be stable business conditions because if you have a goal of——

Mr. CROSS. Who is to determine what stable business conditions are? The Board? They differ here.

Governor ECCLES. Yes; it has got to be left up to the Board, which should not be considered a political body. The law makes the Board a nonpartisan body, on which political parties as such are not represented and appointments to which are for periods of 12 years.

Mr. CROSS. That is true, but you know human nature doesn't change, and it is just like the *Dred Scott case* in the Supreme Court. People don't change. And what we want to do, it is my idea that we get something here where they are anchored to something.

For instance, now, here is the testimony of Governor Harding:

The American monetary system is a good deal like a ship at sea without adequate equipment of rudders and compass to guide it.

Don't you think they need something to guide them, something to go to?

Governor ECCLES. I don't believe that a fixed-price level is a guide that we should have. We might have a stable price level on the basis of some index, and yet have a great deal of unemployment.

Nobody would be satisfied if you reached a 1926 price level and continued to have a national income of 50 billion dollars instead of 80, and 10 million people unemployed.

Mr. CROSS. Yes, but Governor, the question of unemployment depends upon profits, doesn't it?

Governor ECCLES. Not altogether——

Mr. CROSS. I won't run my factory unless I make a profit, will I?

Governor ECCLES. That is true.

Mr. CROSS. If I make profits, I employ people.

Governor ECCLES. That is right.

Mr. CROSS. And when I employ people that increases purchasing power.

Governor ECCLES. That is right.

Mr. CROSS. And when they have that increased purchasing power they are going to buy, and I will continue to produce, but if you let matters run wide open and I keep expanding, then there is bound to be a reaction, and I throw a lot of people out of employment and I destroy purchasing power.

Don't you think it is better to have a stable purchasing power in relation to a wholesale price level?

Governor ECCLES. This is an interesting chart here that Dr. Goldenweiser gives me. It shows that the price level in England was very stable from 1931 to 1934, but the amount of their unemployment fluctuated considerably.

Mr. CROSS. Yes; I have seen some of the charts.

Governor ECCLES. But I mean——

Mr. CROSS. But, now, Governor, in reference to England, did you read the book by Sir Charles Morgan Webb, in which he in substance says that they regulated gold from 1823 on down to 1914 because they were the only creditor nation of the world and they were carrying the commerce of the world, and that it benefited them as a creditor nation? Did you read that work?

Governor ECCLES. No; I didn't. It seems to me that the Federal Reserve System can control to quite a large extent, not entirely, however, the volume of money, by its power over discount rates and its open-market policy.

Changes in the volume of money in the hands of the people, however, depend also upon the willingness of people to borrow and the willingness of banks to lend.

Mr. CROSS. Yes, Governor; but what I am trying to get at now is to try to show you how confused the Federal Reserve Board has been in the past. Now, for instance, here Dr. Miller testified in 1928, and he says:

> It is my opinion that the Federal Reserve mind at the present time is more perplexed than it has been since the troublesome period of 1920 to 1924; that it is in a state of mental confusion.

Why was that and what is there to keep it from remaining in a state of mental confusion unless you have some goal to go to?

Governor ECCLES. I think there should be a goal, but I don't think the question of prices——

Mr. CROSS. Well, name the goal you think is the proper one.

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Governor ECCLES. The goal is stable business conditions and full employment.

Mr. CROSS. All right, they had that all the time, didn't they? It is just the same as the goal in the law now, isn't it?

Governor ECCLES. In the existing law the Federal Reserve Board is not charged with the responsibility of creating a condition either of stable prices or of full employment.

As I understand it, the responsibility of the Federal Reserve System is to supply the credit needs of commerce, agriculture, and industry.

Mr. CROSS. All right, now let us go back to Congress. It is the duty of Congress under the Constitution to furnish money, adequate money, a medium of exchange, and regulate its value.

Governor ECCLES. That is right.

Mr. CROSS. How can Congress regulate that value unless it fixes the price level?

Governor ECCLES. I don't say that prices are not part of the consideration. I think that every effort should be made to maintain stable prices, but stable prices should not be the sole and paramount objective, so that the Board would be directed to maintain stable prices and not to consider total production and employment at all.

Mr. CROSS. Yes; but you take the wholesale index of prices in the market, which are arrived at by taking the mean price, where some may go way up and some way below, but you hold a mean level of prices. Now, if you don't use that, you have got no measure of value, have you? Unless you use that, what other measure of value could you figure for money?

Governor ECCLES. I am not sure that I can say. Gold, of course, hasn't proven to be a very satisfactory measure of value and the buying power of money, measured in goods and services, of course, is the value that the people are interested in.

Mr. CROSS. Governor, I want to ask you this question, You don't think we are helpless in the midst of plenty to feed and clothe, with man power to produce—that we are helpless and these things come on and then there is no help for it? Do you think that?

Governor ECCLES. I stated the other day that I don't believe that any monetary policy alone will result in stable business. Simply dealing with the volume of money, so far as it is possible to influence or affect the volume of money through the controls that the Reserve System has, cannot give you full prosperity. This is because distribution of wealth production——

Mr. CROSS. Yes.

Governor ECCLES. Is a very important element, and that gets back to the problem of the tax system. The banking system can influence the volume of money——

Mr. CROSS. Now, Governor, I understand that.

Governor ECCLES. And the tax system, it seems to me, must influence the velocity of money.

Mr. CROSS. Well, now, Governor, let me get this. Of course, I don't think the tax system is so important that we are ever going to get anywhere with it except to stop enormous fortunes by higher taxes in the upper brakets. But now suppose you have got a small community such as they had in the early days, when people would come in to the fairs and exchange their products, their things; and they followed the law of supply and demand perfectly, did they not?

Governor ECCLES. Yes.

Mr. CROSS. Now, the dollar or the monetary unit of a country is supposed to reflect as a mirror the workings in that country of the law of supply and demand for things; so if the country has plenty of everything, if that law of supply and demand were followed just like they would come together and exchange what they have, everybody would have plenty and would not be hungry and distressed and ruined and broke. Now, don't you think the monetary unit ought to perform that function?

Governor ECCLES. The monetary unit ought to; but the monetary unit can't be made to perform that function simply through monetary policy. Placing the means of payment in the hands of people who will spend is the thing that determines employment, business activity, and price levels.

The ownership of the money is an important element in the use of the means of payment. If there are corporations, owning large unused balances of funds, which cannot find a profitable place to use or invest those funds, those funds don't go into circulation.

Mr. CROSS. That is true, but if you had prices at the point where they could invest and make some profits——

Governor ECCLES. But the——

Mr. CROSS (continuing). They would invest.

Governor ECCLES. The prices would not induce them to invest. It is the profit opportunity that induces them to invest, and where you already have a great unutilized capacity because the people as a whole lack the buying power to purchase the goods produced, there is no incentive to invest in further capital goods.

Mr. CROSS. Governor, don't you think the whole theory is that we are helpless—and so far as the Federal Board is concerned we needn't look to that for relief, not for much relief—that there are all kinds of things out yonder that you can't reach and touch, and therefore we just have to follow along?

Governor ECCLES. No; I think that the monetary factor is 1 of the 3—1 of the 3 important control measures of our capitalistic system. The volume of money can largely be controlled through a banking system.

The distribution of funds which is a factor in their velocity must be controlled through the income-tax system, and employment must be regulated through a public-works system.

When the volume of money is adequate to support a certain price level for a given volume of production, and unemployment begins to develop, and as a result prices begin to decline, it is likely to be because productive facilities are out of balance with the consumers' buying power, and velocity of money is declining.

Mr. CROSS. Yes; but you don't want to let it get to where that happens. If you are going to let contractions take place, and as a result all over the country where bonds have been issued for school districts, road districts, municipalities—and you say that the dollar today or next month will double in purchasing power, so that that individual must pay twice in real value because there is no value in money so far as keeping and clothing is concerned—he must pay twice as much in real value to pay the taxes and to pay the interest on his mortgage if he has one—it becomes an impossibility. It means a general liquidation and discontent and trouble and threatened bankruptcy.

Governor ECCLES. It does, if you let the national income decline. The purpose of our tax system and the public-works system is to keep up production when private business fails to keep up full employment. The loss to the Nation, when the national income declines through unemployment, is a loss we cannot afford.

Mr. CROSS. And your idea is to do it through public works, public enterprises?

Governor ECCLES. That is right.

Mr. CROSS. Each time you do that you borrow a good many billions of dollars, don't you?

Governor ECCLES. You wouldn't have very much to do if you did it at the right time, before you allowed deflation to proceed very far. The amount that it would require at the beginning——

Mr. CROSS. That is, more or less, just a guess, isn't it? If you keep on running these billions up, who is paying that tax but the public? And if you get 50 billions and a hundred billions, the fellow who pays it has got to collect it back off the people. There are bonds which they have got to collect off the people in taxes.

Governor ECCLES. Who pays the difference between the 85 billion of national income and the less than 50 billions of national income—who pays that 35 billions?

Mr. CROSS. The fellow who has got the loans on his land. The people who have the loans foreclose the mortgages and get the land, and they keep it until they can resell it to these fellows again, those who can buy. They have to take that loss. But my idea is to get a stable purchasing power in your monetary unit, so that it can't happen that if a man goes out and puts up a factory and has to borrow money, and he borrows this money and builds the factory and expands it, and the first thing he knows the purchasing power of that dollar doubles and trebles, and he is sunk.

Governor ECCLES. You may fix a stable purchasing power as a requirement of the monetary policy of the Federal Reserve Board, or any other Board, but I don't know what methods they could use to maintain or to reach that objective.

Mr. CROSS. Don't you think it could be kept by using the rediscount rates? In other words, using the reserves—the reserves in the banks—couldn't you use the open-market operations?

Governor ECCLES. No monetary policy alone by simply attempting to regulate the volume of money will maintain a stable national income or——

Mr. CROSS. I don't say "volume" alone. I mean volume and velocity. Can't you control it through the rates, loaning of the reserves, and rediscount rates and open-market operations—wouldn't that have an effect on the velocity as well as the volume?

Governor Eccles. To the extent that a reduction of rates and an increase in the supply of money would tend to stimulate velocity; yes. But so long as there is an inequitable distribution of wealth production which results in excessive saving we will have depressions.

Only by pulling back that part of our savings that we cannot profitably use in new capital goods and using those funds to give employment to those who become unemployed can we maintain a balance.

The Government must be the compensatory agent in our economy through the money system, through the tax system, and through a public works system.

Mr. Reilly. I think the committee will have to go now. The committee will adjourn now.

(Whereupon, at 11:25 a. m., an adjournment was taken until Wednesday, Mar. 13, 1935, at 10:30 a. m.)

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(Whereupon, at 11:25 a. m., an adjournment was taken until Wednesday, Mar. 13, 1935, at 10:30 a. m.)

BANKING ACT OF 1935

WEDNESDAY, MARCH 13, 1935

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

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

The Chairman. The committee will come to order. Mr. Cross, you may continue with your examination of Governor Eccles.

STATEMENT OF MARRINER S. ECCLES, GOVERNOR FEDERAL RESERVE BOARD—Continued

Mr. Cross. Governor, you may have thought, from my questions, that I am in a critical mood. I want to say I think this bill provides for a tremendous improvement over what we have, and I think you are a big improvement over governors we have had heretofore; so do not think I am criticizing you.

Check money, for all practical purposes, performs the functions of legal tender money, does it not?

Governor Eccles. Yes; it does.

Mr. Cross. The easier credit is, the greater the volume of credit, and the greater the number of check dollars, the less the dollar will buy; is not that so? When credit is easy there are plenty of check dollars, check money, and that means prices are up, does it not, and therefore the purchasing power of the dollar is down, is it not?

Governor Eccles. That would be expected to follow. The easy money——

Mr. Cross (interposing). That is almost axiomatic, is it not?

Governor Eccles. Easy money, through the banking system, by creating low interest rates——

Mr. Cross (interposing). That is a fact, is it not, that it is axiomatic; that when credit is easy there is a large volume of credit, and that inevitably means that times are good and prices are up, and profits are up, and people are borrowing, and there is a supply of check money like there was in 1928 and 1929?

Governor Eccles. Of course, your general prices go up when means of payment in the hands of people who will spend increase faster than production.

Mr. Cross. Is the proposition I put to you true or not?

Governor Eccles. I think that is generally the case, but it certainly is not always so. Witness the present situation.

Mr. Cross. Then the tighter credit is, the less credit there is, the fewer number of check dollars there are; that is true, is it not?

Governor Eccles. Yes; I think that is true.

Mr. Cross. That being the case, then the more the dollar will buy, will it not?

In other words, as credit dries up, check money, the purchasing power of the dollar increases, does it not?

Governor Eccles. Not always.

Mr. Cross. Now, Governor, do you not think the velocity theory of money is more or less a meaningless fiction?

Governor Eccles. No.

Mr. Cross. Now, along in 1928 and 1929 we had a situation where our credit money, our check money did about 90 percent of the traffic duty of the country, did it not?

Governor Eccles. I think those were the estimated figures. I do not know how accurate they are, but that would be approximately correct.

Mr. Cross. That is what they put it at, about 90 percent?

Governor Eccles. Yes.

Mr. Cross. Now, if all of that check money had vanished or dried up, 90 percent of the money had dried up, the traffic of the country had vanished, had it not?

Governor Eccles. Unless the deposits were drawn out in currency.

Mr. Cross. If you have 5½ billion in currency, we will say, and we are talking about the check part of it, and practically 90 percent of it was gone, then you had left your legal-tender money, which was about 5 billion, we will say?

Governor Eccles. Yes.

Mr. Cross. Now, if nine-tenths of that money was check money; that is, 90 percent, and you had 45 billions in check and 5 billions in legal-tender money, and the 45 billion had vanished, it is not to be assumed that it did not all go out?

Governor Eccles. I do not know that I understand your point.

Mr. Cross. If your check money had vanished like the mist—it is a kind of phatom money, but it does the work of the country in all its functions. Say that 90 percent of the traffic was done through check money, and we will say that is nine-tenths of the total, and one-tenth of the business was done, we will say, with legal-tender money, there being nine times as much check money as legal-tender money, and the check money disappears, and you have only left your legal-tender money, of course, then 45 billion in check money would have vanished, would it not?

Governor Eccles. If it disappeared, that would be the case.

Mr. Cross. If your credit dried up like the mist, then it would disappear, would it not?

Governor Eccles. Yes.

Mr. Cross. And if you then had 5 billion in legal-tender money, and then that 5 billion had kept on performing the duty of transferring the property and the goods of the country at the same speed at which it was traveling when you had your 45 billion of credit money, it would have been doing only one-tenth of the amount of traffic duty that was being done by the whole amount of credit money plus the currency or legal-tender money, would it not?

Governor Eccles. If the total amount of money is reduced by nine-tenths, then that one-tenth or the remaining money would be doing——

Mr. CROSS (interposing). Traveling as fast as it always had been, it would have been one-tenth, would it not?

Governor ECCLES. I do not know whether it would have been traveling that fast.

Mr. CROSS. Assuming that it would be traveling as fast as it was in 1928 and 1929, with the 45 billion gone, it was doing only one-tenth of the work; if it was doing the same amount of work after the crash as before the crash, is not that true?

Governor ECCLES. If the velocity of the funds does not change, if the volume is reduced nine times, of course, your volume times your velocity would be one-tenth of what it was.

Mr. CROSS. Surely; that is simple mathematics.

Governor ECCLES. Yes.

Mr. CROSS. Now, is it not a fact that in figuring velocity you give credit to the work being done by the credit money when times are good, and the legal-tender money, in fact, is not going any faster than afterward, except that the credit money vanishes and you no longer can figure what the credit money is doing to the legal-tender money? In other words, you give credit to the legal-tender money, and when times are good you say the currency amounted to 5 billions, and it was going at such and such a speed; but you are giving credit to the legal-tender money for all that is being done by 45 billions of credit money, are you not? Is not that the way you count velocity?

Governor ECCLES. No; it is not.

Mr. CROSS. How do you count it? You cannot tell how often it swaps hands.

Governor ECCLES. The national income is the number of times that your volume of money——

Mr. CROSS. Of what money?

Governor ECCLES. All money.

Mr. CROSS. All right.

Governor ECCLES. There is no distinction so far as the working of the money is concerned between currency and checking accounts; they both perform the same function in the money system. I mentioned yesterday the difference in the velocity figures.

Mr. CROSS. Let me get this concretely, if I can, so I can understand it.

Take, for instance, the situation in 1929. At what velocity do you say money was traveling at that time?

Governor ECCLES. What would be termed as the income velocity; that is, the relationship of money to the national income——

Mr. CROSS (interposing). What was the velocity of money at that time? Say we had 50 billion, counting the credit money and the legal-tender money, what was the velocity at which all of the 50 billion was traveling?

Governor ECCLES. We had, in 1929, 26.4 billions——

Mr. CROSS (interposing). Of all money?

Governor ECCLES. Of all money.

Mr. CROSS. Checking——

Governor ECCLES (interposing). And currency; that is right. That eliminates, of course, your interbank deposits. These are the figures I got from the Federal Reserve statistical division.

Mr. GOLDSBOROUGH. That does not include savings money?

Governor ECCLES. No; you cannot include savings money any more than building and loan money.

Mr. CROSS. The checking accounts, plus the legal tender, amounted to 26 billions?

Governor ECCLES. That is right. The national income was 82 billions, according to the Department of Commerce figures, or, to be exact, 82 billion 300 million.

Mr. CROSS. What do you understand as the national income?

Governor ECCLES. It represents, as I understand it, the income received in the production of all goods and services.

Mr. CROSS. What do you count as goods?

Governor ECCLES. It would be capital goods as well as perishable goods, buildings, factories——

Mr. CROSS (interposing). And lands?

Governor ECCLES. Equipment; no land.

Mr. CROSS. Just buildings?

Governor ECCLES. Buildings—factories and equipment; all kinds of goods. The total volume of bank debits was estimated to be between 1,000 and 1,200 billion. In other words, the actual turnover of money was about 40 times a year, I think.

Mr. CROSS. Governor, now you say capital goods, and then you say the income was 80 billion. Where do you get the income at 80 billion? What do you mean by that?

Governor ECCLES. The money value.

Mr. CROSS. Of all capital goods, buildings, and so forth?

Governor ECCLES. The money value of what was produced in any particular year. If in the year 1929 the value of all foods, clothing, and capital equipment of all kinds produced in that year was a certain amount, that would be income, after the elimination of duplications—for instance, if you start to figure the value of wheat that is sold to the miller, then the miller sells to the wholesaler and the wholesaler sells to the retailer. When you take the total check transactions, they run between a thousand billion and twelve hundred billion, and it takes into account all of those relationships. But the national income only takes into account what is produced, and by considering it once, and not in the various transactions through the methods of production and distribution. That is the national income.

Mr. CROSS. I am getting at the question of velocity. You say you had 26 billion of all kinds of money. Upon what basis do you figure the velocity of the 26 billion?

Governor ECCLES. With that amount of money, with 26 billion, we had a national income of 82 billion, 300 million; or we had there what is termed an income velocity of 3.12. In other words, the total volume of our currency and checking account went into the total national income that year 3.12 times.

Now, we come down to 1933, when the national income was 46 billion, 800 million, and our money had diminished from 26 billion, 400 million to 19 billion, 900 million.

Mr. GOLDSBOROUGH. When was that, 1933?

Governor ECCLES. Yes.

Mr. GOLDSBOROUGH. The other year was 1928?

Governor ECCLES. The other year was 1929. There was very little difference between the 1928 and 1929 figures. And with the income of 46 billions, 800 millions and the deposits and currency in existence during that year of 19 billion 900 million, the income velocity was 2.35. We have not the figures for 1934, but that is expected to show a decrease. We know that the volume of deposit currency has been very substantially increased as the result of three factors—the budgetary deficit, gold imports, and the reduction of currency in circulation as the result of the dehoarding.

Mr. CROSS. Your gold is all stabilized, is it not?

Governor ECCLES. That is right. But the gold comes in from abroad to take care of the unfavorable trade balances of Europe and the rest of the world. The only way they have been able to take care of their unfavorable trade balances is to pay us in gold. There has been about 1 billion 300 million of gold coming into the country in 1934. Those three factors increase your deposits. There would have been a greater increase than that had there not been a shrinkage of loans and investments of banks, outside of Government bonds. As I recall the figure, it was around 6 or 7 hundred million dollars. The result was an increase in deposits and currency by about $4,000,000,000, as I recall the figures.

Mr. CROSS. You say an increase in currency?

Governor ECCLES. In deposits. I do not think there was any increase in currency.

Mr. CROSS. As to this billion dollars of gold that comes in here, do you mean to say that would make an increase of a billion dollars of back-bone or pocket money?

Governor ECCLES. An increase in bank deposits in that amount; yes, sir.

Mr. GOLDSBOROUGH. You said the amount in 1933 was forty-six billion, eight hundred million. Have you the amount in 1934?

Governor ECCLES. No; I have not. It is estimated as over fifty billion, but the ratio of the national income to deposit money will show up considerably less than it was in 1933, showing that with the increase in the volume of money there has been a decrease in the velocity of money; that the increased volume has not increased the national income in proportion.

Mr. CROSS. What is the increase for 1934 over 1933?

Governor ECCLES. I have not the exact figures.

Mr. CROSS. In the volume of money?

Governor ECCLES. It would just be an estimate. But I think it is around four billions. That is the increase of 1934 over 1933.

Mr. CROSS. What is the difference between the check money of 1929 and the check money of 1933?

Governor ECCLES. I do not know just what you mean. You mean in amount, the actual amount of check money in 1929 as compared with the check money in 1933?

Mr. CROSS. Yes.

Governor ECCLES. There was a difference of 7½ billion between 1929 and 1933.

The CHAIRMAN. Let me ask you a question right there, to make sure I understand it. Do you mean to give the total figures for the entire country? Are your figures predicated on calculations that embrace all of our banks?

Governor ECCLES. Oh, yes.