Mr. FLANNAGAN. Let me stop you right there. A man does not borrow money at all. What he does, when he goes to a bank and gets a note discounted, is to swap his debt for the bank's and the bank evidences its debt by placing a credit on its books. It is another operation to convert that into money. It is true that the bank gives a debt which is payable on demand, and that debt payable on demand is the thing which is substituted for coin by the people in the daily operations of the bank every day.

Senator HITCHCOCK. Well, do you think that it is possible to borrow money from the banks?

Mr. FLANNAGAN. You do not borrow money. You get it in an indirect way; but the first thing you do is to swap debts, or credits.

Senator REED. Well, you might put your note over the counter of the bank and get it in cash, but that is not an ordinary transaction.

Mr. FLANNAGAN. No; the ordinary transaction is to get your credit on the bank's books.

Senator REED. I think I can tell what is misleading Senator Hitchcock. He never borrowed any money of a bank except when he needed it right away. [Laughter.]

Mr. FLANNAGAN. He does not keep any balance?

Senator HITCHCOCK. Now, Mr. Flannagan, I wonder why there is such an insistence on treating the loan as a loan of credit, when in many cases I know, as a matter of fact, that it is a loan of actual money. I have been to the bank and borrowed money myself.

Mr. FLANNAGAN. Certainly.

Senator HITCHCOCK. And got the legal tender or the gold over the counter.

Mr. FLANNAGAN. Certainly; that can be done.

Senator POMERENE. That is the exception, however, when that is done.

Mr. FLANNAGAN. What you did, Senator Hitchcock, was to take the bank's credit that was granted to you at the time it made the loan to you and immediately convert it into money; that is all. But the operation of a discount is the bank substituting its debt, payable on demand, for its customer's debt, payable in the future.

Senator HITCHCOCK. Of course, if that is true, then it is true of an individual as well as a bank?

Mr. FLANNAGAN. Certainly.

Senator HITCHCOCK. And if I come to you now and say to you, "I want to borrow $5," and I give you my note, and you hand me the $5, I have not borrowed money from you, but have borrowed merely a credit.

Senator REED. That would not be a question of credit; but it would be a question of discretion. [Laughter.]

Senator HITCHCOCK. Now, I should like to have you distinguish between the two. Why do you distinguish them, and assume that there is some invisible or psychological loan of credit in the case of the bank?

Mr. FLANNAGAN. There is nothing invisible or psychological about it. The proposition is this: If you come and borrow $5 from me you do not borrow my note; you do not borrow my credit, because my credit, or my debt, will not circulate as money, and will not take the place of money. I am speaking now of myself as an individual.

Senator HITCHCOCK. Yes; I understand.

Mr. FLANNAGAN. But if you go to the bank and you get money—that is, get coin—that is a different proposition.

Senator HITCHCOCK. Yes; that is what I mean. Why do you always insist that it is credit in the case of the bank, when there may be no credit involved, or only a momentary credit, put on the books of the bank and taken off again immediately.

Mr. FLANNAGAN. But of course when you want to define the function of "discount" you must do it in respect to the great number of such operations. Very few cases arise when a man goes into a bank and says, "Give me the gold for my note." That is very rarely done, and even then when it is done you will probably find that the bank in addition to taking your note will take your check in order to get the gold, so as to get that book credit which was created by the discount, off its books.

The CHAIRMAN. Even if they did not do that they would credit it to "bills receivable," and charge the cash, which is a part of the available funds——

Senator HITCHCOCK (interposing). Of course there are a large number of cases——

Mr. FLANNAGAN (interposing). You generally get a cashier's check, if you have no account with the bank.

Senator HITCHCOCK. Not necessarily. But this is an inconsequental question, after all.

Senator REED. Well, now, but is not this true, as to general operations, in the great mass of banking done by merchants: The merchant goes to the bank and arranges for a credit—that they will "carry" him for a certain amount of money. He needs $10,000 in his business. He gives his note for $10,000, and that amount is put to his credit upon the books of the bank. He checks against that and continues to put money into the bank, and finally his balance runs down too low, and again he goes and borrows, and he keeps that up until he gets up perhaps to about the limit of his credit, and there stands all the time on the books of the bank a balance to him which is made up or which grows out of the fact that his notes are in there and the bank has carried over on its books an entry showing that the bank owes him a certain amount of money. That is the way is it generally done, is it not?

Mr. FLANNAGAN. Yes.

Senator REED. So you speak of it—it has been spoken of as credit here, whereas you say that in truth instead of being a credit it is a debt of the bank to him?

Mr. FLANNAGAN. Of course.

Senator REED. And a little further than that: The bank owes 1,000 people or 10,000 people for the very money that it has carried over and credited to A B upon his notes. He has borrowed money that the bank already owed to others. So it is pretty nearly all credit.

Mr. FLANNAGAN. Yes, sir; the whole banking business is swapping debts.

Senator REED. Yes.

The CHAIRMAN. I would like to call attention to the fact that when the loan of the New York banks increased $500,000 you immediately find, as an actual fact, that the deposits increase to a like amount.

Mr. FLANNAGAN. Yes.

The CHAIRMAN. And that is an almost invariable rule?

Mr. FLANNAGAN. That is right.

The CHAIRMAN. For the reason that when these loans are made they are redeposited in the same bank or in another bank or, if drawn in cash, the cash is immediately paid to liquidate debts and is then by other persons redeposited in the same way, so that they instantly reappear as an increase of deposits in almost parallel columns.

Mr. FLANNAGAN. It is almost invariably true that whenever you see an increase in deposits you will also see in the same statement a corresponding increase of loans and discounts. It means that those credits—book credits—are created by loans and discounts.

Senator HITCHCOCK. Can you tell us why it is that the European banks distinguish between deposits proper and deposits which grow out of loans, whereas American banks do not so distinguish?

Mr. FLANNAGAN. I can not tell you why it is so. They call it in the Scotch banks a "cash credit."

Senator HITCHCOCK. Generally they call it "accounts current." If I go to a bank in Europe and borrow $10,000, which is placed to my credit, that is called an "account current," but in an American bank it is called a deposit. They distinguish between the two kinds of deposits in European banks.

Mr. FLANNAGAN. I do not know why that is so; in fact, I did not know that all the European banks attempted to keep these separate.

Senator HITCHCOCK. They do.

Mr. FLANNAGAN. But we in this country do not make any distinction between the credit that is created as the result of a discount and the credit that is created as the result of a deposit of circulating notes, of checks, or of gold. In our banks we do not draw any distinction. We call them all "deposits."

Senator POMERENE. Well, should there be any distinction?

Mr. FLANNAGAN. I do not think it is practicable with us. I do not know how we could do it.

Senator HITCHCOCK. Well, it would show, then, whether a bank was merely lending its credit to excess, would it not?

Mr. FLANNAGAN. I do not know how we could draw the distinction, however, in the bookkeeping under our method. I do not know how it could be done. Nor do I see any special advantage in having it done, because each form of credit ought to be readily converted into gold.

Senator HITCHCOCK. You do not know the reason that moves the European banks to separate them?

Mr. FLANNAGAN. I can not tell you. I really do not know what you state to be the fact, of my own knowledge. I am not familiar with that.

Senator HITCHCOCK. It is done in all their statements, and it is also set forth in the report of the Monetary Commission as a fact.

Mr. FLANNAGAN. Yes. Shall I continue my statement, Mr. Chairman?

The CHAIRMAN. Yes; if you please.

Mr. FLANNAGAN. The principal change which I would urge for your earnest consideration is one which will allow all national banks to exercise all the normal functions of banking. These functions are a growth and development inherent to the business itself, and the bill restricts one function which in my opinion should be made normal. I refer to the function of note issue. Banking everywhere must consist of the three functions of discount, of deposit, and of note issue (or circulation). I do not mean that every bank must exercise all three functions, but I do maintain that the three functions must necessarily be exercised in every country where any credit system can be efficient and satisfactory.

All credits systems everywhere are but variations of the substitution of debt for coin, and in this substitution the three banking functions named are essential.

The bill before you contemplates the limitation of the function of note issue to the Federal reserve banks after 20 years.

I believe this is a mistake. You allow the temporary continuation of the present bond-secured currency, not because it is good—for our greatest financial ills can be traced to its evil influence—but because we must gradually get out of the meshes in which it has entangled us, and therefore you provide for its gradual extinction. While doing this, is it not wise to provide the gradual substitution of a more complete and perfect system, built upon our experience?

Our national bank system, with the exception of the currency provision and the counting of debts from other banks as reserves, has proved of inestimable good.

It has aided in cementing the country into one united whole, while it has given opportunity to individual initiative.

If we can strengthen this individuality and at the same time avoid the weakness which comes from excessive self-reliance I believe the present will mark an epoch in our industrial and commercial history, and that this measure will be the beginning of an era of great prosperity, and will eventually lead to our acknowledged supremacy in the financial world.

When you consider the fundamental nature of banking, which is the substitution of its own debts for other debts, and that its debts, whether in the form of deposits or circulating notes, are used by the people as a substitute for coin, it is apparent that the bank function of note issue should be exercised exclusively for the accommodation and convenience of the customer. He should be free to ask this form of debt—circulating note—if his business requirements demand it, and the bank should be equally free to give it. Or, in other words, deposits should be convertible into currency at the will of the creditor.

The only matter which should concern the legislator, as the representative of the people, is that both forms of bank debt, deposits and circulation, should be reasonably safe.

The substitution, or conversion of one form into the other, should be left to the parties in interest, or, in other words, to the requirements of trade.

Now, the individual banks come into direct daily contact with all the people—their customers; they know the people's wants and requirements, and should be put in the position to reasonably supply them. As your bill now stands, you have no method of creating a circulating note in response to trade demands except through another bank function of discount, and the intervention of two banks. These two functions are not necessarily connected. A discount, or the substitution of the bank's debt payable on demand for the customer's debt payable in the future, does not necessarily imply that the bank's debt is wanted in the form of a circulating note.

The exchange and transfer of bank debts in the form of deposits by means of the cancellation of checks, to the extent of over 500 millions of dollars daily, through the clearing houses of the country proves just the contrary.

I think the method of furnishing the member banks the circulating notes of the reserve banks most advisably thought out, and I would not change this, but hold this provision as the reserve credit of the country.

Let there be a bank for banks—one in each district—but do not have so few as to make one section of the country dependent upon another for its normal development. In addition to this, I should like to see every national bank which is a member of the Federal reserve system have the right of note issue, not exceeding its capital stock, under similar safeguards which you have provided in the way of collateral security for Federal reserve notes.

I should like to see 50 per cent gold reserve required to be held against these bank notes, not only to insure elasticity, but primarily to prevent any inducement per se as a matter of profit from such issuance. Such inducement was a cardinal defect in the original plan under which our national bank note currency was inaugurated. If you will confine this privilege of note issue to member national banks, I believe you will hear no more complaint about enforced stock subscriptions to Federal reserve banks. If you will limit the privilege to such banks as have 50 per cent of their capital stock invested in United States bonds deposited for circulation, the market will be maintained for 2 per cent bonds until you retire them at the rate of 5 per cent per annum as the bill provides. If you will allow these gold reserve bank notes to be issued pari passu with the retirement of the bond-secured notes, the aggregate volume of notes being limited to the amount of capital stock, you will provide now a true elastic bank currency as a portion of the existing circulating medium and, I believe, add largely to the flexibility of the outstanding bank currency.

At first blush it may be thought that this provision will produce inflation, because each individual bank would endeavor to get out and keep its notes in circulation to the full limit.

As a matter of fact, there can be no inflation of bank currency with gold redemption. With a requirement of 50 per cent gold reserve and redemption at the district reserve bank the profits arising from circulation could not be of sufficient inducement to prompt its issuance, and issuance would therefore come only through the legitimate demands of customers.

Under such restrictions as indicated, the total amount of national bank notes which could be issued with the present capitalization if every bank avails of the privilege to the maximum amount, would be $331,885,000, against which one-half of that amount would have to be held as a reserve in gold.

Senator Hitchcock. Will you please restate that? I did not quite catch your meaning.

Mr. Flannagan. Under such restrictions as indicated, the total amount of national-bank notes which could be issued with the present capitalization, if every bank availed of the privilege to the maximum amount, would be $331,885,000, against which one-half of that amount would have to be held as a reserve in gold.

Senator HITCHCOCK. You are speaking of the individual banks now?

Mr. FLANNAGAN. Of course, what I am arguing for is to give the individual banks the right to issue circulation within certain limitations.

Senator BRISTOW. He is contending that the individual banks ought to have the right of issue just the same as the bill gives the reserve banks.

Mr. FLANNAGAN. Yes; under the same restrictions except 50 per cent of gold reserve.

Senator HITCHCOCK. Then you would have two classes of bank notes.

Mr. FLANNAGAN. Oh, no. You might call it a gold-reserve note; but the result of it would be that it would make all the present national-bank currency be redeemed as trade required; and I believe would give them a flexibility which they do not now possess.

Senator HITCHCOCK. Let me get your idea. Your idea is to have the present national-bank currency retired gradually, as is proposed in the present bill?

Mr. FLANNAGAN. Yes.

Senator HITCHCOCK. Then you would allow the individual bank the right to issue notes to the extent of their capital stock, upon the creation of a gold reserve of 50 per cent.

Mr. FLANNAGAN. Yes.

Senator HITCHCOCK. Then you would also allow the 12 Federal reserve banks to issue up to 50 per cent of their capital?

Mr. FLANNAGAN. I do not believe there is any limitation in the bill as to the issue of notes by the Federal reserve banks; but I would have a limitation as to individual banks; I would not allow their circulation, which would include both the circulation based upon United States bonds as now and the gold-reserve notes, both combined to exceed the capital stock of the individual bank. I want to meet the ordinary daily requirements of trade. It should not be necessary, in order to get a circulating note, that a bank, desiring to oblige its customer, has got to go to the reserve bank and get a discount, except when the circumstances or general conditions of the country require it. Keep it as a reserve credit—not for the daily operations.

Senator HITCHCOCK. Of course you would be substituting for a bond-secured currency a currency which would have no security.

Mr. FLANNAGAN. I beg your pardon. I say that they have to deposit 100 per cent of discounted notes with the reserve bank before the Comptroller of the Currency would issue them these incomplete notes.

Senator HITCHCOCK. But you did not state that, I think.

Mr. FLANNAGAN. Well, I said under the restrictions that you have already made for the Federal reserve notes, which implied that. But when I read the proposed amendment to the bill you will see that is made very plain, I think, Senator Hitchcock.

In other words, the circulating bank debt, or extension of credit under this provision, might be $165,943,000, which amount, being about one-half the average amount of the daily exchange or cancellation of bank debts through the New York Clearing House, could hardly be called an unsafe extension of credit.

I firmly believe that this provision, if made, will constitute the keystone to the arch of the admirable system you have conceived, and that at the end of 20 years, when the inelastic, rigid, bond-secured currency shall have been retired, we shall have a complete and perfect system, composed of independent banks, organized on true economic principles, with an elastic currency, on a gold basis, responsive to all ordinary demands, so united under Government control by the Federal reserve act as to be a tower of commercial strength which can defy financial storm and stress, through the confidence engendered by such a combination.

Senator BRISTOW. Do you desire to take up now the amendment which you suggest?

Mr. FLANNAGAN. Now, the amendment proposed is on page 36 of the bill as reported to the House, after the word "obligation," on line 8.

These will be additional paragraphs to section 19——

Senator HITCHCOCK (interposing). Before you get to that amendment, Mr. Flannagan, Senator Bristow wanted to ask you a question.

Senator REED. Would it not be better for Mr. Flannagan to read his amendment first?

Senator BRISTOW. Yes; if his amendment relates to the subject which he has discussed.

Mr. FLANNAGAN. Certainly; that is just what it is.

Senator BRISTOW. What page of the bill?

Mr. FLANNAGAN. Page 36 of the new bill, as passed by House, at the end of line 8, after the word "obligation," I suggest to add a provision for these additional gold-secured notes.

Senator SHAFROTH. Is it a long section that you are adding?

Mr. FLANNAGAN. Yes; several paragraphs.

Senator SHAFROTH. Will you read that?

Mr. FLANNAGAN (reading):

Any national banking association being a stockholder of a Federal reserve bank—

And, mind you, I want to confine it to member banks, to give them that exclusive privilege, so as to induce all existing banks to come in under the bill.

Senator POMERENE. Do you mean by that that any State banks which might desire could come into this system as well?

Mr. FLANNAGAN. They can not issue notes unless they become national banks.

Senator POMERENE. That is just what I want to make clear, because this bill provides that the State banks might come in. I noticed in your statement that this was to be national banks, and I did not know whether you did extend it to any other banks.

Mr. FLANNAGAN. This is an additional privilege of circulating notes that you are giving the national banks which are members of the Federal reserve system, which will serve to induce them to come in, and which may also induce the State banks to become national banks.

Senator POMERENE. That is the point that I wished to make clear.

Mr. FLANNAGAN (reading):

Any national-banking association being a stockholder of a Federal reserve bank——

Senator REED (interposing). That ought to be a "member" bank. But go on.

Senator SHAFROTH. That is the definition of a "member" bank.

Mr. FLANNAGAN. That makes it one.

Senator HITCHCOCK. No; because he excludes State banks.

Mr. FLANNAGAN. I say, "Any national-banking association being a stockholder of a Federal reserve bank," because I am excluding State banks unless they do become national banks.

Senator REED. That is right.

Mr. FLANNAGAN (reading):

Any national banking association being a stockholder of a Federal reserve bank, and having on deposit with the Treasurer of the United States an amount of United States bonds as security for circulation at least equal to 50 per cent of its capital stock, may indorse and lodge as collateral security with the Federal reserve bank of its district any bills and notes discounted by it in the usual course of business and in accordance with law—

I put that "in accordance with law" in on account of that 10 per cent limitation of liability.

having a maturity not exceeding four months, and thereupon may receive from the Comptroller of the Currency incomplete circulating notes in the form now authorized to the face value of such discounted paper thus deposited.

But said circulating notes shall not be signed by the officers of the bank receiving the same, nor be issued or placed in circulation, except as and when a reserve fund in gold coin or United States gold certificates is provided by being segregated and set apart for their redemption to the extent of 50 per cent of the amount issued and outstanding.

Such gold reserve shall consist of at least one-half of the required amount, always kept intact in the vaults of the issuing bank; the remaining half may consist of balances due either from the Federal reserve bank of the district in which the issuing bank is located or from the United States Treasury.

The notes thus issued shall be redeemable on presentation at the counter of the issuing bank and also at the Federal bank of the district in which the said bank is located and at the United States Treasury.

In case of liquidation, whether voluntary or involuntary, the payment of all outstanding notes must be provided for by a deposit of lawful money with the United States Treasury from the assets of the liquidating bank before any distribution of assets to other creditors.

The amount of circulating notes of any bank delivered by the Comptroller of the Currency and outstanding at any one time, including those hereby authorized and those secured by United States bonds, shall not exceed in the aggregate the amount of the capital stock of the issuing bank and to the extent that circulating notes secured by United States bonds are retired by the redemption or funding of 2 per cent bonds under the provisions of this act other circulating notes secured as in this section provided may be issued to replace the amount thus retired.

Any member bank shall have the right of substitution at any time before maturity of an equal amount of dicounted paper for any deposited with the reserve bank as specified collateral for its circulating notes.

Now, if you consider that amendment is wise, you would have to make a change also in line 17, page 35, of the bill, which is necessary (if this amendment is adopted) in order to make the provisions conform.

Senator HITCHCOCK. What line?

Mr. FLANNAGAN. Line 17, page 35, by inserting after the word "outstanding," the words "which are secured by a deposit of United States bonds."

Senator BRISTOW. Were you through with that?

Mr. FLANNAGAN. I was through with that amendment. But there are other amendments which I would suggest.

Senator BRISTOW. Why should these individual banks—why is it necessary for a man to have anything to do with a central bank in order to get this currency? Why not make a similar provision, or provisions, for a note issue, so that it can be taken out by direct transactions with the Treasury, just as the note issues are provided for now?

Mr. FLANNAGAN. Well, I do not believe that it is wise, Senator, to undertake to issue Government circulation. If you will allow me——

Senator BRISTOW (interposing). Well, I do not mean Government circulation. You propose a bank circulation.

Mr. FLANNAGAN. Yes.

Senator BRISTOW. As we now have, except on a different principle. We have bank circulation now.

Mr. FLANNAGAN. Well, it is a sort of "bobtail" bank circulation, under restrictions which make it inefficient for commercial purposes.

Senator BRISTOW. But it is a bank circulation; and the individual banks provide for currency when they want it, according to certain legal requirements?

Mr. FLANNAGAN. Yes.

Senator BRISTOW. Now, you propose that the individual banks should still have this privilege of issuing a currency, but a different kind of currency and according to different methods. But, in order to do that, there is created this artificial, and it seems to me unnecessary, institution called a "reserve bank." Why can not the individual bank provide for this circulation by dealing directly with the Comptroller of the Currency?

Mr. FLANNAGAN. I will tell you, Senator. The Federal reserve bank offers a great many advantages. It is a combination of all the banks for times of stress. It carries out the same idea that clearing houses have found efficient in times of panic heretofore. So that it would be a mistake, in my opinion, to attempt to do away with the Federal reserve banks and attempt to have the individual banks deal direct with the Treasury in this matter.

And I think that is a good reason. I think you want to keep the Federal reserve banks as the reserve credit of the country—the reserve ability to incur a debt which will circulate as money; a place where there is such unbounded confidence that, no matter what happens, when the Federal reserve bank comes with the Government behind it (the Government being the source of all credit) there can be no question or doubt.

Senator BRISTOW. Well, of course you put the Government behind this Federal reserve bank in order to steady public confidence in it. Now, the Government is behind the present national-bank circulation—Government bonds are—and everybody has confidence in those notes now. Nobody ever hesitates to take them. A man does not look to see whether he is getting a gold certificate or a bank note. It is all the same to him.

Now, I can not see why the credit of the Government behind the individual bank is not just as effective, so far as public confidence is concerned, when it is directly behind the bank, as it would be to put it behind the individual bank through this roundabout way.

Mr. FLANNAGAN. Well, in times of panic, what would you do?

Senator BRISTOW. Let the bank deal directly with the Government.

Mr. FLANNAGAN. Would you have each bank deposit the security for its circulating notes direct with the Government?

Senator BRISTOW. Direct with the Government, according to certain stipulations and legal requirements?

Mr. FLANNAGAN. If you want the Government to go into the banking business, and be in a position to exercise direct control instead of through these regional reserve banks, we could do it that way; though I do not think the system is nearly so good as the one now suggested. I think it is much better for the Government to take direct control of 12 banks than of 7,000.

Senator BRISTOW. It would not have any more control of the 7,000 than it has now, would it, except that its facilities would be somewhat enlarged?

Mr. FLANNAGAN. Well, I do not think it is practicable; that is my thought; but I do not profess to be infallible, you know. It is my opinion that it is very much better to maintain the Federal reserve banks.

Senator BRISTOW. I desire to say that I am in sympathy with your idea that the individual bank should have this right. I do not think the individual bank ought to ask any other bank whether or not it can issue a note. I think it ought to have the same right that the Federal reserve bank has got in dealing with the Government, and should not have to go through this reserve bank in getting a favor from the Government. That is my objection. I think the individual bank ought to have a right to deal direct with the Government, and not be under any obligation to another concern.

Mr. FLANNAGAN. I think, too, the individual bank ought to have a right to deal direct with the Government and not be under obligations to any other financial concern. But do not these banks represent the other banks? Is not that a simple consolidation of the other banks?

Senator BRISTOW. That is what I object to. When you consolidate, you give control and influence and domination to a very large degree, and I think we ought to preserve the democracy of the national-bank system as it is to-day.

Mr. FLANNAGAN. I believe in maintaining the individuality of the banks. I certainly do, as I have stated; but I do believe that it is not only very desirable but necessary to have them united through the Federal reserve banks, or in some other manner.

Senator HITCHCOCK. The commercial paper which the individual bank would put up as security for notes would be deposited, not with the United States Government, but with the reserve bank.

Mr. FLANNAGAN. With the Federal reserve bank.

Senator HITCHCOCK. Would it be obligatory upon the Federal reserve bank to issue the circulation against those notes?

Mr. FLANNAGAN. The incomplete circulation comes from the Comptroller of the Currency now.

Senator HITCHCOCK. There would be no discretionary power, would there?

Mr. FLANNAGAN. No; there is none to-day, except you have to put up Government bonds.

Senator HITCHCOCK. But should that be done in the case of commercial paper?

Mr. FLANNAGAN. That is a question in your wisdom to be decided; whether you decide you will allow banks with a margin of 100 per cent discounted notes and 50 per cent gold, which they have to have in addition; whether it is not entirely safe to allow the banks to give the paper they receive in the ordinary course of business, so as to let the notes come as a matter of right to them. That would be my opinion; to let them come as a matter of right to the individual banks, so they can issue circulation upon the deposit of their regular paper, which is to be paid at maturity, and that is the reason I give the right of substitution.

Senator HITCHCOCK. You would not allow the officers of the reserve banks to say to the individual banks:

> We will refuse to loan you this currency because your notes are not good.

Mr. FLANNAGAN. The Federal reserve bank does not issue; they are mere custodians of this paper.

Senator HITCHCOCK. Well, then, refuse to deliver it.

Mr. FLANNAGAN. If you think they ought to come into more direct contact with the Government, you might specify the Federal reserve agent where the Federal reserve bank now deposits its collateral notes. If you think that is all right, it amounts to the same thing.

Senator HITCHCOCK. The idea rather appeals to me, providing it really gives to the individual bank a method by which it can secure a limited amount of an additional currency, as a matter of right.

Mr. FLANNAGAN. That is what I believe will be the case under this proposed amendment.

Senator SHAFROTH. That is permanent currency you are referring to?

Mr. FLANNAGAN. Certainly. To begin with, you will get 5 per cent of it additional every year when you retire these 2 per cent bonds, unless the banks choose now to issue an additional circulation, if the demands of trade require it. You may be sure this additional currency will not be issued unless trade demands require it. It will not be issued as a matter of profit as the old circulation was at first. As you retire 5 per cent, say, $35,000,000 a year, you can put this in place of it, so that at the end of 20 years you will have a true bank circulation.

Senator SHAFROTH. Without any contraction?

Mr. FLANNAGAN. How do you mean?

Senator SHAFROTH. The currency will take its place equal to that amount?

Mr. FLANNAGAN. Yes.

Senator REED. I want to get this in my mind. I am not sure that I have it there. I am greatly interested in your statement.

Mr. FLANNAGAN. There are several amendments here which I would like to suggest.

Senator REED. Are you anxious to get away?

Mr. FLANNAGAN. No; I want to leave at 4 o'clock this afternoon. I have plenty of time.

Senator REED. Then let me work out my proposition by way of illustration. Let us say that you are a banker in New York City and your bank has a capital of $1,000,000. You want to get $1,000,000 of this currency——

Mr. FLANNAGAN. Now, which currency are you talking about?

Senator REED. The currency that you propose under this method.

Mr. FLANNAGAN. All right; go ahead.

Senator REED. And the Government has given you the right, as you propose, to have that $1,000,000 of currency. Now, just what would be the modus operandi of your getting that money?

Mr. FLANNAGAN. You want $1,000,000 of currency and you are entitled to it under your restrictions as to capital.

Senator REED. You have $1,000,000 of capital; you want $1,000,000 of currency to use; you are a member of the regional bank.

Mr. FLANNAGAN. Yes.

Senator REED. How would you go at it under your suggestion to get this $1,000,000 in currency?

Mr. FLANNAGAN. I could not get any unless I placed on deposit with the Treasury of the United States $500,000 Government bonds.

Senator REED. Any kind of Government bonds?

Mr. FLANNAGAN. Yes, except those excluded from the circulating privilege. I need not have circulation issued against this, $500,000, but I must have that on deposit as security. So that, under the circumstance you name, I could only get $500,000 circulation.

Senator REED. You could get that on the bonds?

Mr. FLANNAGAN. No; I am talking about in addition now. If I had $500,000 of bonds, I am entitled to $500,000 of circulation, which I may have outstanding or may not have outstanding. Take, for instance, the Chemical National Bank; I think they have $50,000 bonds deposited, but they have no circulation outstanding. But, we will suppose, Senator, that the bank with $1,000,000 capital has already $500,000 of national bank notes outstanding, for unless they have the bonds deposited with the Treasury sufficient to get $500,000 notes outstanding they can not get this circulation. That is the point, is it not? You want me to follow out what you would do, do you not?

Senator REED. I would really prefer that you would start with a brand new bank that is organized to-morrow with a capital of $1,000,000 and you want $1,000,000 of circulation. How would you get it under this bill?

Senator SHAFROTH. That is under your amendment to this bill?

Senator REED. That is right, under his amendment to this bill.

Mr. FLANNAGAN. $500,000 I would have to get by the purchase of 2 per cent bonds.

Senator REED. Or any other kind of bonds you propose.

Mr. FLANNAGAN. Two per cent United States bonds, because they are the cheapest.

Senator REED. What would you do with those bonds?

Mr. FLANNAGAN. I would deposit them with the Comptroller of the Currency, and they would be transferred in trust to the Treasury of the United States and held as they are now.

Senator REED. Very well.

Mr. FLANNAGAN. I would then get $500,000 of circulation secured by United States bonds. You understand the purpose of making that restriction, do you not? It is to maintain the market price of 2 per cent bonds. I am entitled to $500,000 additional. I can not get it until I have discounted paper. I have got to go into operation. I have got to go and lend my customers $500,000 and get their paper with my capital, and when I do get among my assets $500,000 of commercial paper—discounted paper—then I can go to the Federal reserve bank and say:

> Here is $500,000 of notes I have discounted; I want you to certify to the Comptroller of the Currency that they are in your possession as collateral security for additional circulation I am going to ask for.

The Federal reserve bank will certify to the Comptroller of the Currency that fact; the Comptroller of the Currency then sends me $500,000 of notes printed like they are to-day.

Senator REED. What about the gold reserve?

Mr. FLANNAGAN. I have not got to that yet. When I get those notes from the Comptroller of the Currency they are incomplete. They are not signed by the officers of the bank; they are not ready for issuance until signed, and before I can sign and issue those notes I have to provide $250,000 of gold from somewhere. Having provided it, I can put $125,000 with the Treasury, or I can put $125,000 with the reserve bank as a deposit, and then I am entitled to issue $500,000 of notes. Of course I need not apply for all nor issue all at one time.

Senator HITCHCOCK. And you keep it in your own vaults, but segregate it?

Mr. FLANNAGAN. I may leave $125,000 in my own vaults if I issue $500,000, or one-fourth in gold of the amount I do issue.

Senator HITCHCOCK. But you do not do so.

Senator POMERENE. Let us say in the reserve bank.

Mr. FLANNAGAN. Let me see if I can not get that straight.

Senator REED. I do not think it is straight now in the record.

Mr. FLANNAGAN. It is very plain in my own mind.

Senator POMERENE. I suggest that the stenographer read Mr. Flannagan's answer in order that the record may be correct.

Senator REED. If you will let me ask these questions you will get it as straight as a string.

Senator POMERENE. Well, I think we owe it to this witness to have his answer read.

The CHAIRMAN. Very well, the stenographer will read.

(Thereupon the stenographer read the answer by Mr. Flannagan, as follows:)

> Mr. FLANNAGAN. I have not got to that yet. When I get those notes from the Comptroller of the Currency they are incomplete. They are not signed by the officers of the bank; they are not ready for issuance, and before I can sign and issue those notes I have to provide $250,000 of gold from somewhere. Having provided it, I can put $125,000 with the Treasury and——

Mr. FLANNAGAN. No; that is wrong. I did not state it right if I said "and." I can put $125,000 with the Treasury or with the reserve bank, and retain $125,000 in my own vaults.

Senator SHAFROTH. I would like to suggest to the stenographer that in order to have the record in proper form Mr. Flannagan's remarks in regard to the reserves should be stricken out.

Senator REED. Now, I would like to understand this, and I do not, and for that purpose I will ask a question or two, with the permission of the committee. Let us assume that the Government of the United States has established this regional bank system.

Mr. FLANNAGAN. Yes.

Senator REED. You desire to organize a bank and do organize one on a capital of $1,000,000. Your capital is put in and your bank is ready to do business?

Mr. FLANNAGAN. Yes.

Senator REED. You now want $1,000,000 of money. The Government has already printed the money.

Mr. FLANNAGAN. It is all in circulating notes. Of course it is not money.

Senator REED. Yes; but that is either in the Treasury or on deposit, or in the custody of the Government's agents who are representing the Government in the regional banks, so that the paper is prepared and printed. That is correct; that is a fact, is it not?

Mr. FLANNAGAN. No; there is no provision in the present law for national-bank notes to be lodged with the regional banks, but with the Comptroller of the Currency.

Senator REED. Very well. The Government has the currency already printed and in the hands of the Comptroller of the Currency.

Mr. FLANNAGAN. That it right.

Senator REED. You go out in the market and buy $500,000 of national bonds.

Mr. FLANNAGAN. United States bonds, yes.

Senator REED. Yes; and you deposit those bonds with a Government agency that is provided for by law.

Mr. FLANNAGAN. The Comptroller of the Currency, as is now provided by law.

Senator REED. Yes; and thereupon there is issued and delivered to you $500,000 of this circulating medium.

Mr. FLANNAGAN. All in incomplete bank notes, which my bank can issue.

Senator REED. Your bank can issue them when the officers of the bank sign them?

Mr. FLANNAGAN. Yes.

Senator REED. That gives you $500,000?

Mr. FLANNAGAN. Yes.

Senator REED. Now, you want $500,000 more?

Mr. FLANNAGAN. Yes; or any portion of that amount.

Senator REED. Well, let us say $500,000.

Mr. FLANNAGAN. All right.

Senator REED. You propose then, you shall take the notes of your customers and indorse those notes?

Mr. FLANNAGAN. That is right.

Senator REED. And carry them where?

Mr. FLANNAGAN. To the Federal reserve bank of my district.

Senator REED. And deposit them there with the Government's representatives?

Mr. FLANNAGAN. Right.

Senator REED. And thereupon that bank will certify to the Comptroller of the Currency that you have deposited $500,000 of this paper?

Mr. FLANNAGAN. Of this discounted paper.

Senator REED. Of this discounted paper?

Mr. FLANNAGAN. Yes, sir.

Senator REED. And it would then become the duty of the Comptroller to send to you $500,000 of currency, which is complete except that your bank officers must sign it?

Mr. FLANNAGAN. That is correct.

Senator REED (continuing). And emit it?

Mr. FLANNAGAN. Yes, sir.

Senator REED. When you have $250,000 of gold reserve piled up in your vault and segregated and set aside as a reserve for that particular $500,000 you can then sign that $500,000 of paper and pay it over your counter?

Mr. FLANNAGAN. Yes, sir.

Senator REED. Now, that is the method, but of course that could be varied by reposing in the Government agent who is representing the Government in the regional bank the right to pass upon the character of these notes you have put there if we wanted to impose that duty upon him?

Mr. FLANNAGAN. Yes; as collateral.

Senator REED. Don't you think that something in the nature of a supervision or inspection of that paper is necessary?

Mr. FLANNAGAN. Well, I will tell you why.

Senator REED. That is what I am interested in.

The CHAIRMAN. You mean to say that you do not when you shake your head?

Mr. FLANNAGAN. I do not. I think you ought to give the banks the right to issue under restrictions named, as a matter of right, without having some other person or authority to pass upon the collateral paper. To begin with, the bank itself—I am talking about my bank now, the one with $1,000,000 capital—and I issue these notes, which can not be done, unless they provide for their redemption both at the Federal reserve bank of the district and at the Treasury of the United States, and at my own counter. So it is not likely that we are going to incur that debt unless we have something behind it.

Very well. Now, in the ordinary course of business, banks do not take bad paper intentionally. It is not to their interest to do so. Why should they want to do so? I do not see that you ought to make it incumbent upon the man removed 100 miles away to pass upon local paper.

Senator REED. Let me suggest the reason and see whether I am not right?

Mr. FLANNAGAN. Yes.

Senator REED. Of course we have all been talking about honest bankers, possessed of ordinary good common sense, and some business acumen, but you have to think about another class of men. Suppose that a rascal is running a bank, or a man in desperate straits is running a bank, and suppose that he concluded that he had to have some more money, and he would just have the clerks of this bank or other people who are worthless sign up a lot of paper send it down, and get this money on it. There might be some heavy losses occasioned by that, unless there was somebody at least to exercise some kind of supervision. Is that not a danger?

Mr. FLANNAGAN. Well, if you want to provide against rascality, beyond the punishment that is provided——

Senator REED (interposing). Don't we always have to provide against rascality in every transaction we enter into?

Mr. FLANNAGAN. I am trying to meet your view, to see if there is some method of doing away with the objection of having a man far removed to pass upon it. That is what I am trying to do. How would it do to have such paper certified by the individual members of the board of directors of the member bank that they approved it? I might suggest something of that sort. There might be restrictions of that sort, but I believe that you ought to preserve the right of the individual banks to deposit collateral taken in the ordinary course of business.

Senator REED. I believe absolutely and have been arguing and hearing in a sort of a way for days that the nearer we can come to giving the individual bank certain rights which it can exercise without first submitting itself to some kind of central control the better. However, I wish you would think about some kind of a check or safeguard upon the character of the notes or discounts which are offered as collateral.

Now, I wanted to take up another thought with you and see just where we come out on that. You put $1,000,000 of cash into the vaults of the bank for the stock. You have $1,000,000. You take $500,000 of that and invest it in Government bonds, which, of course, locks up $500,000, so far as you are concerned, for which you get $500,000 in circulation, of course.

Mr. FLANNAGAN. We get currency back for it.

Senator REED. Then you have to hold the gold reserve back of the other $500,000?

Mr. FLANNAGAN. Yes.

Senator REED. Which is equal to $250,000?

Mr. FLANNAGAN. Yes.

Senator REED. This releases one-half of that money to you and you can then get 75 per cent increase over your original capital, but of course one-half of your original capital has to be invested in these low-interest-bearing bonds. You do gain 75 per cent, though, in a way. You gain an actual increase of 25 per cent, an actual doubling there; on the other you have to put the bonds up.

Mr. FLANNAGAN. Twenty-five per cent margin is all you have, Senator, over and above the actual capital invested. It seems to me that is the way it figures out. It is really 25 per cent gold reserve on your total circulation; it is 125 per cent in Government bonds and collateral notes and gold for every note that is issued. Is not that right?

Senator REED. I think you are right about that.

Senator BRISTOW. Will you not repeat that last statement?

Mr. FLANNAGAN. I said 125 per cent as security, either in Government bonds, gold, or discounted notes, for every note that is issued.

Senator BRISTOW. It would be equivalent, would it not, to a 50 per cent margin on the notes, on the deposited notes?

Mr. FLANNAGAN. Fifty per cent gold reserve on the additional notes you issue over and above the issue on your Government bonds makes 125 per cent on the whole issue, including the collateral discounted notes deposited with the reserve bank.

Senator REED. Would there be any objection to requiring the member bank which is issuing this money to deposit that 50 per cent gold reserve along with the notes that it takes for discount in the regional bank?

Mr. FLANNAGAN. Keeping it all deposited there? You have to redeem them at your own counter.

Senator REED. And therefore you want it there?

Mr. FLANNAGAN. Yes; you would not then have any there. As suggested, you have three places for redemption for all bank notes. That is to give uniformity of circulation at par everywhere.

Senator REED. What is the objection then to making the bank notes only redeemable at the regional banks and having the gold there?

Mr. FLANNAGAN. You might do that.

Senator REED. So that this gold reserve would naturally be in the hands of the Government. Would that be workable?

Mr. FLANNAGAN. I think that a margin of 25 per cent, which is a pretty good margin, is sufficient. I do not think that you want to destroy the independence of the individual bank entirely in that respect. I think you want to make them feel that you are doing the square thing. You do not want to treat them like they are all suspicious characters.

Senator REED. I do not mean that. Let us see if I have invoked there anything that is not invoked in every day's business between the banks themselves and with their customers. A bank takes a man's promissory note, not because they insist he is a rascal, but because there are occasional rascals and because it is necessary to have a record of the transaction. The bank, too, requires collateral to be deposited time and again with it, not because it is dealing with a rascal but because that is a matter of business safety. The Government of the United States now requires the banks to deposit bonds with it before it issues money, not upon the theory that the bankers are rascals, but because that is the business-like way to do it.

Now, when I say why not also deposit the gold reserve with the Government and make the notes redeemable at the regional bank where the gold is, it does not imply that the bankers are rascals and that we should treat them as rascals, but that we should simply follow the simple lines of good business and good government. Of course, it may be impracticable.

Mr. FLANNAGAN. I do not think that is desirable. You already have 100 per cent of every note that is issued represented by good assets of the bank specifically pledged as collateral security, and this 50 per cent gold reserve is in addition. That 50 per cent gold reserve, to my mind, is not required so much for security as for the purpose of preventing the unnecessary issuing of circulation. Let me illustrate: Suppose that money is worth 6 per cent and the bank is going to consider the question whether or not it is going to issue circulating notes. If it issues circulating notes it has to consider the 50 per cent gold reserves remaining idle, and hence an earning of 3 per cent on those notes, and I want that earning to be so small that there will be no inducement to get out circulating notes for the profit thereon. I prefer to make the restriction in the form of security rather than in the form of a tax, because if you make it in the form of a tax you are making the people pay it.

Senator HITCHCOCK. Let me ask you some questions right along the same lines. Do you know, Mr. Flannagan, why the redemption of these notes you propose to issue would pursue any different course from the redemption of the present national-bank notes?

Mr. FLANNAGAN. My thought is that banks when they want gold as reserve will send the notes of another bank to the reserve agent and build up their own reserve by using those notes.

Senator HITCHCOCK. That is what is done now?

Mr. FLANNAGAN. Yes. It is done through the Treasury now, is it not? My thoughts further were——

Senator HITCHCOCK (interposing). The fact is now that the Treasury every year receives 87 per cent of the national-bank notes that are outstanding.

Mr. FLANNAGAN. Oh, no. Every day?

Senator HITCHCOCK. Last year the Government received 87 per cent.

Mr. FLANNAGAN. You mean in a year?

Senator HITCHCOCK. Yes; I mean in a year.

Mr. FLANNAGAN. Oh!

Senator HITCHCOCK. That is due to this fact. That a bank out West in looking through its currency and desiring to ship currency to Chicago, is always willing to keep the gold certificates and hold the legal tender money, which can be used as a reserve. It will therefore send national bank notes to Chicago. The Chicago bankers will send them over to New York for credit, or to the Treasury for redemption to get legal tender money. Will not the same thing happen with these notes as you propose, so that the bank instead of receiving its own notes will simply give them up to the central reserve bank and they will really all be presented either to the Treasury or to the central reserve bank for redemption.

Mr. FLANNAGAN. That may be the effect of it.

Senator HITCHCOCK. If that is the case, then Senator Reed's suggestion that the gold instead of being kept in the vaults of the banks should be kept in the Treasury or in the regional reserve banks, where the real redemption will occur, is in point?

Mr. FLANNAGAN. But the bank has to preserve its reserve of 25 per cent in the Treasury or the reserve banks; and if they find they will have to keep more money there in order to get the notes redeemed they will have to send it there and get their notes back.

Senator HITCHCOCK. As I understand your suggestion, this gold reserve which you segregate against notes in the individual banks can not be counted as a reserve against deposits?

Mr. FLANNAGAN. No.

Senator HITCHCOCK. So it is no use to the banks for that purpose?

Mr. FLANNAGAN. No; it can not be of any use to the banks for that purpose.

Senator HITCHCOCK. If it is placed with the reserve bank it is available?

Mr. FLANNAGAN. That might be true. I would like to think a little more on that subject—whether or not it would be desirable to put all the note reserves in the Federal reserve banks and have exclusive redemption there.

Senator REED. Let me direct your mind to this: Whether 40 per cent or 30 per cent or, say, half of the gold reserve should be now with the Federal Treasury.

Mr. FLANNAGAN. We specify that. That is the way I have it now.

Senator REED. You specify that half of the gold reserves be deposited in the Treasury?

Mr. FLANNAGAN. Certainly; we have it specified that way now.

Senator BRISTOW. He said $125,000 of the $250,000 was to be deposited with the Treasury.

Senator REED. I had overlooked that.

Mr. FLANNAGAN. Yes; that is the way it is now. Now, let me take some of these other things.

Senator REED. Now, in regard to the examination of this paper. I take it that banks do not just on a moment's notice ordinarily want to issue this money; that they have generally a few days in advance in which to consider it?

Mr. FLANNAGAN. Oh, yes; or a few weeks.

Senator REED. Now, would there be any difficulty at all in having the bank examiner of that district called in by the bank to go over this paper?

Mr. FLANNAGAN. I think that is a good idea. I think that that is, perhaps, the solution. Let it be approved by the national-bank examiner of the district, if you want to do that.

Senator REED. If the members of the committee do not desire to ask any further questions, I would like to ask Mr. Flannagan one or two myself.

Mr. FLANNAGAN. I wanted to finish up some of the other amendments that I desire to suggest to the bill if you will allow me.

Senator HITCHCOCK. This plan of yours which you have outlined in these amendments does not interfere with the provisions of the bill which provides for the retirement of the present national currency, does it?

Mr. FLANNAGAN. Not at all. It just provides that you substitute one for the other. You allow national banks to have a circulation of 100 per cent of their capital. Those that have now 100 per cent of their capital in United States bonds can not get it, but those that have less than 100 per cent can get it.

Senator HITCHCOCK. To the extent of the difference?

Mr. FLANNAGAN. Yes, to the extent of the difference, and as the national bank note currency is retired under the provisions of the Federal reserve act, which I think is provided at the rate of 5 per cent per annum, any bank having these notes thus retired can issue other notes.

Senator HITCHCOCK. Notes under this bill may be issued to the extent of such retirement. Now then, ultimately, taking this hypothetical case of the bank with $1,000,000 capital—ultimately, after a period of 20 years, that bank will have $1,000,000 in circulating notes secured only by these deposits of discounted paper?

Mr. FLANNAGAN. Yes; discounted paper and 50 per cent gold reserves.

Senator REED. I am going to ask you to furnish the committee before you leave us, if you have the time——

Mr. FLANNAGAN. I am with you as long as you choose to have me; but I just want to finish what I have to say.

Senator REED. This is an interesting matter, and I would like to find the amount of gold this would actually gather and place in the custody of the Government, provided all of the banks were to avail themselves of the provisions of the proposed act—all the national banks I am speaking of.

Mr. FLANNAGAN. Right now it would be $335,000,000; that would be the maximum issue, of which 50 per cent would be $167,-

000,000. About $89,000,000 would be gold reserve in Federal reserve banks or treasury; but then if you continue, at the end of 20 years it would be one-fourth of the total capitalization of all national banks.

Senator Reed. Yes; and if it was in proportion to the present capitalization——

Mr. Flannagan (interposing). About $1,000,000,000.

Senator Reed (continuing). It would then accumulate $250,000,000 more in gold which would actually be in the vaults of the United States?

Mr. Flannagan. Yes; or the Federal reserve banks.

Senator Reed. Yes.

Mr. Flannagan. That is right.

Senator Reed. That is what I would like to see built up.

Mr. Flannagan. I think you will build a fine system if you will do that.

Senator Shafroth. At the end of the 20 years the notes which would be in circulation and secured by United States bonds would be retired, as I understand it.

Mr. Flannagan. Yes; that is the present provision of your bill.

Senator Bristow. Then the only circulation would be circulation secured by the 50 per cent gold and the collateral?

Mr. Flannagan. Yes; and the circulation of the national reserve banks, whatever that might be.

Senator Bristow. That is simply an emergency circulation.

Mr. Flannagan. Well, it is not right to call it an emergency circulation, because in ordinary times you can go and get it if the discount operations work as the framers think it will; it will be done constantly.

Senator Bristow. Might not that result in a contraction of the currency?

Mr. Flannagan. I do not see how it can; can you?

Senator Bristow. Well, suppose it was not profitable to the banks to keep out this circulation?

Mr. Flannagan. Circulation ought not to go out by reason of a profit to the bank. Circulation is a mere form of debt of the bank which the customer may demand; if the customer demands it, the bank will have to furnish it. The profit, on the basis of 50 per cent gold reserve and 6 per cent discount rate, is 3 per cent less whatever the tax is, which I think is about one-half of 1 per cent now.

Senator Reed. Going back to my illustration just once more. If this bill is passed and ultimately worked out so that the present bank currency is retired, and, if you wanted to organize your bank at that period, you would not take any Government bonds out at all?

Mr. Flannagan. No. That amendment that I submit to you at the end of the retirement removes that necessity.

Senator Reed. You would then simply take out $100,000 of the notes of A, B, and C, and upon them you would get issued $100,000 of unsigned currency; and then as fast as you accumulate a 50 per cent reserve you would emit currency?

Mr. Flannagan. Yes, and you would do that gradually. You would not take your whole capital. I have known of banks to be organized without a penny by the organizers simply giving their notes, having them discounted and with the proceeds purchase bonds and issue circulation.

Senator HITCHCOCK. Are you in favor of the retirement of the present national-bank-note currency?

Mr. FLANNAGAN. Most undoubtedly I am.

Senator HITCHCOCK. Your position there is not inconsistent with retaining the present bank-note currency, is it?

Mr. FLANNAGAN. Well, except the rigidity of this. My contention, Senator, is that the present bank-note currency is not the true function of bank issue. I think that before you can exercise it you have to invest your capital in Government bonds, which means that you must make a discount for the Government to the total amount of your capital.

Senator HITCHCOCK. Do you object to the present bank-note currency as a practical proposition because it is inflexible and not responsive?

Mr. FLANNAGAN. Yes, sir.

Senator HITCHCOCK. Can you give me an idea of the extent to which that bank-note currency should be restricted? What should its percentage be?

Mr. FLANNAGAN. That would be a mere guess.

Senator HITCHCOCK. You have no idea of what it should be?

Mr. FLANNAGAN. No.

Senator HITCHCOCK. You have just said to Senator Bristow you think this would result in a contraction of the currency.

Mr. FLANNAGAN. No; I asked him the question, "How can it?" If you retire 5 per cent of the present issue annually, and you are free to replace it, how can there be any contraction?

Senator HITCHCOCK. I am not talking about the provisions of this bill, which provides for retirement, because personally I am against the retirement of the national-bank-note currency.

Senator POMERENE. You are against the retirement of the national-bank-note currency?

Senator HITCHCOCK. Yes; and I would like to find out from some one, who is in a position to know, to what extent the currency really should be restricted. Some men say 10 per cent, some men say 15 per cent. Now, I ask you how about that, Mr. Flannagan?

Mr. FLANNAGAN. I can not tell you; I think that it ought to be adjusted by the requirements of trade in two ways—first as to its issuance and then as to its redemption. I have written a paper on that, which I will send you.

Senator HITCHCOCK. But there is a point where some currency must remain.

Mr. FLANNAGAN. Undoubtedly.

Senator HITCHCOCK. Can you give the committee any idea how much?

Mr. FLANNAGAN. I do not believe anybody can tell you that. I do not believe anybody knows.

Senator HITCHCOCK. If some currency must remain, why not allow the bond-secured currency to remain as the permanent feature of our currency, simply imposing on top of that an elastic cushion.

Mr. FLANNAGAN. A fringe. That is what you are doing here under this suggestion of mine.

Senator HITCHCOCK. No; we are proposing under this bill to retire all the bond-secured currency.

Mr. FLANNAGAN. Yes, in twenty years.

Senator HITCHCOCK. I put to you the question. If we must have at all times, say, 80 per cent of currency, why not allow this bond-secured currency to remain as the permanent feature of our currency system, and simply impose on top of it an elastic cushion?

Mr. FLANNAGAN. You mean for the purpose of——

Senator HITCHCOCK. I mean simply for the purpose of not having an undue disturbance in the banks of the country.

Mr. FLANNAGAN. You will not have an undue disturbance in the banking world if you retire annually at the rate of 5 per cent per annum.

Senator HITCHCOCK. I am simply asking your view in relation to that phase of the question. I would like to hear from you, and I would like to have some one state to this committee what percentage of elasticity is necessary. If it turns out to be only 10 per cent, then in a few years this country will go to a point where the present bond-secured currency can legitimately become the permanent currency of the country and without any shrinkage, and it will simply be necessary to provide for the necessary elastic currency in addition. If the bond-secured currency is safe, what objection is there to that?

Mr. FLANNAGAN. That might work. I can not say offhand what percentage it would be. You know in the case of the Bank of England they have a fixed amount—I believe it is $90,000,000—but the principle of issuing a bank currency ought not to be restricted as it is at the present time, for the Government produces an inelastic currency, and if you grant that it is inelastic, I think that that inelasticity should be corrected, and that the volume of business will adjust it. You do not want the currency to go below a certain amount.

Senator HITCHCOCK. My thought is this: That we have $700,000,000 of good currency outstanding now.

Mr. FLANNAGAN. Yes.

Senator HITCHCOCK. If that is redundant now at any time during the year, it will only be a matter of a few months before the Government will come up to it, and whatever additional elasticity we need we can have on top of that.

Mr. FLANNAGAN. Is there any guaranty that it will not be changed?

Senator HITCHCOCK. If we were only authorizing a new percentage to be deposited against it, it could remain the permanent foundation of our currency system. Every country has a permanent currency. The Bank of France always has its notes outstanding. Do you know what the shrinkage is in that country?

Mr. FLANNAGAN. No.

Senator HITCHCOCK. It is insignificant, is it not?

Mr. FLANNAGAN. I do not know. They do their business mostly with bank notes.

Senator HITCHCOCK. They have 500 millions of dollars of bank-note currency outstanding as a rule and it does not shrink, and that is true of the Reischbank in Germany. There is not a great percentage of shrinkage there. There seems to be always a need for a permanent currency. Why not retain the bond-secured currency we have now?

Mr. FLANNAGAN. If you can fix in your mind the proper amount that is true as an economic proposition. If the $700,000,000 can be retained as this fixed amount of our currency, then it is all right.

Senator HITCHCOCK. So you are unable to say what the shrinkage would be?

Mr. FLANNAGAN. I do not know how to figure it. I think it is wise to gradually provide for the redemption of any bond-secured currency. That is my thought, but I am not wedded to that particular thing.

The CHAIRMAN. I would like to call your attention, Mr. Flannagan, to the experience of the Bank of France. They have 5,800,000,000 of francs and they actually keep, though not issued at all in normal times, something over 1,000 millions of francs, but even under that condition it is being redeemed and emitted, and it therefore appears that they have over 1,000 millions of francs which they could issue in an emergency.

Senator HITCHCOCK. Have you in the reports of the Monetary Commission any statistics showing the extreme variations of issue of the banks of Europe?

The CHAIRMAN. No; I do not think there is any table showing these variations. They simply show the tables from time to time as they happened to be.

Senator HITCHCOCK. I have been told that it is not over 15 per cent of shrinkage in volume.

Mr. FLANNAGAN. In France?

Senator HITCHCOCK. No; in the average European bank. In fact I understand in Germany the effect of their system is that there is a constant tendency to expand and that contractions in a period of depression brings about an acute condition there—it does not work as well there—and that they really have their periods of depression to represent our panics and have their losses.

Senator SHAFROTH. I want to ask you a question. Would you have these notes which you propose to issue legal tender?

Mr. FLANNAGAN. Not at all.

Senator SHAFROTH. You would not have them legal tender at all?

Mr. FLANNAGAN. Not at all.

Senator SHAFROTH. What objection is there to making them legal tender?

Mr. FLANNAGAN. I would like to see all legal-tender notes retired. I have great objection to legal-tender notes.

Senator SHAFROTH. What is your objection to legal-tender notes?

Mr. FLANNAGAN. Because it is making somebody take some other debt in payment of another debt. It is wrong in principle.

Senator SHAFROTH. Every country in the world does it.

Mr. FLANNAGAN. I beg your pardon.

Senator SHAFROTH. The Bank of England does it.

Mr. FLANNAGAN. The Bank of England notes are legal tender so long as they redeem in gold, and no longer.

Senator SHAFROTH. The Government has placed itself on record as pledging itself to maintain the parity of the metals and of all forms of money. It has a gold reserve, has it not?

Mr. FLANNAGAN. The Bank of England?

Senator SHAFROTH. No; the United States Government.

Mr. FLANNAGAN. Oh, we were forced to provide a gold reserve as a result of the panic of 1893.

Senator SHAFROTH. It is there, is it not?

Mr. FLANNAGAN. Yes.

Senator SHAFROTH. And it answers the purpose, does it not?

Mr. FLANNAGAN. It does, simply because the United States Government is exercising a banking function and the commercial world has forced it to provide gold as a reserve; but it is not that way with the idea of legal tender.

Senator SHAFROTH. Every dollar of money that is out has the power of the Government behind it. That makes it circulate more readily.

Mr. FLANNAGAN. Well, I will tell you, a Government paper obligation is a debt; it is a debt whether it is issued by a bank or whether it is issued by the Government. When you say that by mandate of law that shall be received in payment by everybody for everybody else's debt, you are assuming a prerogative that the commercial world will never stand for, and you can not do it except to a limited extent.

Senator SHAFROTH. We have done that with the gold.

Mr. FLANNAGAN. But the woıld has done that as to gold.

Senatoı SHAFROTH. And we do it as to silver now, and there is no discount on it.

Mr. FLANNAGAN. Why; because there is a redemption in gold.

Senator SHAFROTH. Certainly.

Mr. FLANNAGAN. I will grant you that as soon as you provide for redemption that your paper promise to pay a debt will stand at par with gold; but there is no necessity to make the money legal tender in order to do that.

Senator SHAFROTH. Would not they be more likely to attempt to redeem the paper money in gold if it is not gold legal tender? Is not that a use that is given to the money itself; it strengthens currency, does it not?

Mr. FLANNAGAN. But it is wrong in principle; that is the point I make.

Senator SHAFROTH. Is not that a use that is given to the money itself that aids and assists and strengthens the currency?

Mr. FLANNAGAN. But it is wrong in principle.

Senator SHAFROTH. Every Government, I think, on earth had done it to a more or less extent.

The CHAIRMAN. The Reichsbank notes are made by law of the German Empire legal-tender notes and the notes of the bank of France are made by law legal tender; although those are both privately owned corporations.

Mr. FLANNAGAN. I think the experience of the commercial world is against legal tender, and I think that our own experience in 1893 shows that we had to provide a gold reserve and that ought to teach us that there is a limit beyond which we can not by mandate of law say that a paper promise is equivalent to coin.

Senator SHAFROTH. That depends upon the amount of gold reserve?

Mr. FLANNAGAN. Yes; and the amount of issue.

Senator SHAFROTH. I want to ask you this: You admit that by making this total legal-tender money issued by the Government and taking up these 2 per cent bonds would be a saving to the Government of $14,000,000 a year, do you not?

Mr. FLANNAGAN. Yes.

Senator SHAFROTH. Would not that be sufficient under any and all circumstances to maintain the gold reserve with 50 per cent back of it?

Mr. FLANNAGAN. $14,000,000?

Senator SHAFROTH. Yes; $14,000,000 a year. We have $700,000,000 of bank notes now, and 2 per cent on that. Would it not save $14,000,000 a year by the substitution of full legal-tender money instead of bank notes secured by those 2 per cent bonds?

Mr. FLANNAGAN. I think it would.

Senator SHAFROTH. Why is it that bankers are invariably insisting that their reserves should be made lower, say, 25 per cent, or down to 18 per cent; and that the country banks should be cut down from 15 to 12 per cent, so that they could issue more credit upon their assets; but when it comes to the Government it must be dollar for dollar? Why is that? Why should not the Government be permitted to have at least a little element of this and thereby effect a saving for the people?

Mr. FLANNAGAN. I believe that if the Government should issue its own notes (and not make them legal tender) to be used as a circulating medium to the extent of the outstanding 2 per cent bonds and keep gold reserves behind them of 50 per cent, that they would save the interest, and that the notes would pass at par by reason of the redemption in the Treasury.

Senator SHAFROTH. Do you not think, adding the legal-tender gold to your notes would add to it?

Mr. FLANNAGAN. No; I do not think so.

Senator SHAFROTH. Would it detract from it?

Mr. FLANNAGAN. I do not know that it would, but I think that it is wrong in principle. I think it is wrong to make a debt due by somebody else payable for another debt. You mean legal tender for private debts?

Senator SHAFROTH. Yes; for public and private debts.

Mr. FLANNAGAN. That is what I am opposed to. I think it is all wrong in principle.

Senator SHAFROTH. But do you not see that there would be such a demand for that currency that it would keep it at a parity with gold?

Mr. FLANNAGAN. Well, I will tell you, I had an experience during Confederate times in which we saw Confederate money. We had that money and we thought it was pretty good money; but it all went to pot.

Senator SHAFROTH. The very Government upon which it was founded went to pot.

Senator REED. The whole Nation went to pot.

Mr. FLANNAGAN. Yes; the whole Nation went to pot.

Senator REED. I am willing that any currency of this country shall go to pot when the Federal Republic goes to pot.

The CHAIRMAN. How long do you think that will be, Senator?

Mr. FLANNAGAN. I do not think that will ever happen.

Senator REED. I think it will be a long while yet; although if we believe the prophecies of some distinguished gentlemen I know of, we are on the verge of the precipice all the time.

Mr. FLANNAGAN. Shall I go on?

Senator BRISTOW. Just a moment, Mr. Flannagan. I got the impression from the statement that you made a while ago that you believed the present volume of our currency was redundant.

Mr. FLANNAGAN. No; I have not stated that. I do not think so.

Senator BRISTOW. Then I got the wrong impression.

Mr. FLANNAGAN. There are some other amendments to this bill which I think would be interesting, if you will allow me to suggest them to you.

If you will turn to page 3, at the end of section 2, I would suggest a paragraph for the purpose of removing some of the objections which have been made by many eminent people; that the provisions for the Federal reserve banks will produce such a violent shifting of credits as to be dangerous to the general interests of the country; and also that this amendment I have suggested would have the tendency of making the country banks decide at once whether or not they were coming into the system. It will give the organization committee some idea of how they shall exercise their power in organizing the districts. The suggestion I make is this: That you add to that paragraph on page 3, right at the bottom after the word "expenses," the following:

> Every bank indicating within 60 days after the passage of this act its purpose to comply with the provisions thereof may deposit with the organization committee its subscription to the capital stock of the Federal reserve bank to be located in the district of the subscribing bank, and thereafter at its option shall be entitled to pay one-half of said subscription in monthly installments of 10 per cent, the deferred payments after 30 days to bear interest at the rate of 5 per cent per annum, upon executing its direct obligation to said Federal reserve bank, when organized, in full payment of one-half of such subscription, which obligation shall be secured by the deposit as collateral security of bills and notes discounted, and indorsed by such subscribing bank, to the face amount of such obligation, said bank having the right of substitution before maturity of other collateral notes or bills and pro rata withdrawal of collateral as payment is made of the bank's obligation.

The effect of that would simply be that any bank that wants to pay for a subscription for stock by getting a discount can do so by putting up collateral.

Senator HITCHCOCK. Suppose, then, it should turn out that not enough banks should come into these reserve associations to put this law into effect throughout the country?

Mr. FLANNAGAN. That would not prevent it, but will encourage them to come in.

Senator HITCHCOCK. There is a pretty grave doubt, throughout the testimony which the committee has heard, and also which I have gained from outside statements, as to whether enough national banks will come in to make the law effective.

Mr. FLANNAGAN. You adopt the first amendment I suggested and you will find them all coming in. All the country banks will come in.

Senator HITCHCOCK. Suppose that even with this amendment, which I think strengthens the inducement—suppose, even with this, only a couple of thousand banks should come in?

Mr. FLANNAGAN. They could get their money back. Everybody would get his money back; that is all.

Senator REED. That leads me, Mr. Chairman, to interject this remark: There is no reason why this bill can not be so amended that when there are enough banks, wherever situated, who signify their desire or willingness to go into this plan——

Mr. FLANNAGAN (interposing). To form one?

Senator REED. To form one regional reserve bank, it shall be formed.

Mr. FLANNAGAN. There is no reason why it should not be amended in that way, that I can see. I think the arbitrary fixing of capital at $5,000,000 for many several banks before any shall be allowed to do business is not a wise provision.

Senator REED. Then it could be followed up by a provision in case of the organization of new reserves to provide one only could organize, say 5 or 6 to start on, and that then there could be stock transfers, etc., worked out.

Senator SHAFROTH. I think this bill provides for additional reserve banks.

Senator REED. But it provides first for 12; and you remember one banker here argued, and he had it figured out, how a few very large banks staying out could prevent the organization.

The CHAIRMAN. Mr. Festus J. Wade made that suggestion.

Senator REED. The discretion could be left in the board of organizers, so that they can organize a bank whenever they have got enough capital and wherever the bank is situated.

The CHAIRMAN. In reality the Federal reserves and the Federal deposits are so much more important then the question of capital, that capital is not an important factor.

Senator REED. I do not see any necessity of requiring that they must have $5,000,000 of capital subscribed before they can organize a bank.

Mr. FLANNAGAN. Do you wish to discuss that amendment at all, or shall I just pass it over? I just threw it out as a suggestion. My own opinion is that there is not a sufficient shifting of credits to amount to anything.

The CHAIRMAN. I would like to have a copy of that.

Mr. FLANNAGAN. I will give you this copy of the bill, marked in that way.

There are several other things that I would like to suggest, some minor changes, as we go along. On page 10, line 22 and line 25, the word "stock" ought to be added after the word "capital."

The CHAIRMAN. What is your suggestion?

Mr. FLANNAGAN. The adding of the word "stock," after the word "capital" in those lines.

The CHAIRMAN. You have not the last issue there, have you?

Mr. FLANNAGAN. I have the last, sir; yes.

Senator SHAFROTH. I think they have put in the word "stock."

Mr. FLANNAGAN. It is not here, Senator.

Senator SHAFROTH. I know, but in the other print they put the words "capital stock" in.

Mr. FLANNAGAN. They did in some cases, but not in this, Senator.

Senator SHAFROTH. I know they did in some cases.

Mr. FLANNAGAN. Do you see it there, Senator Owen?

The CHAIRMAN. Yes.

Mr. FLANNAGAN. In the twenty-fifth line add the word "stock" after the word "capital." And on the eleventh page and the sixth line, add the word "stock." That makes that right.

Here is a very simple amendment, but I suppose that while we are going over it, as I read this bill very carefully last night, we may as well fix it. On the fourteenth page, the sixth line, if you will read it, you will see the word "associations." As the reference has been to one association, it ought to be in the singular. If you read the context before, you will see that that is true.

Now, if you will please turn to page 15, line 3. I do not know whether you gentlemen have considered the question or not of allowing State banks with branches to come in. Of course it is very desirable for all State banks to come in, to make it to their interest to do so, but unless you allow State banks which already have established businesses and have established branches to retain those branches it is folly to expect them to come into it. They can not do it; they would not do it. None of them would entertain it at all. So my suggestion is that you allow them to retain the branches already established, if they come in, and if you determine that you are willing to do that, then that you would amend it by saying, after the word "Comptroller" in the third line, "may retain any branches existing at the time of such approval."

Senator HITCHCOCK. That gives them a great advantage over national banks.

Mr. FLANNAGAN. I am going to suggest that you give national banks the right of branches in their municipalities, so as to meet that. In one town, I mean—not branches outside of it. "Approved by the said comptroller" would make it better and clearer, because you mean the Comptroller of the Currency, as he has been named there before; and it would be well if you would amend it by inserting after the word "the" the word "said."

Then turn to page 17, line 18. This is quite immaterial, but it seems to me in order to have it conform it should be amended. Section 11 begins: "That there shall be created." If you will turn to the matter of the advisory council you will see that it reads "There is hereby created." It seems to me you ought to have them read alike.

Senator REED. The first ought to be "There is hereby created."

Mr. FLANNAGAN. It should conform to that phraseology.

Senator HITCHCOCK. Is there anything in this bill as it now stands which would prohibit the comptroller from accepting as a member a State bank which has branches?

Mr. FLANNAGAN. Yes; in the reference to the provisions of the national currency act there is a sentence here which would seem to prohibit it, but if you will make the other change so as to allow the national banks to have branches, the question will not arise at all.

Senator BRISTOW. If you allow national banks the right of branches in their municipalities, one bank could monopolize the entire banking business of New York?

Mr. FLANNAGAN. It can not do it very well. I do not see any objection to it—but, of course, you will do as you like. [Laughter.]

Senator HITCHCOCK. Can you point out where in this bill a State bank would be prohibited from becoming a member if it had branches?

Mr. FLANNAGAN. One minute, and I will do it. You know we do not have any national branch banks, do you not?

Senator HITCHCOCK. Yes; but I do not remember any provision in the bill which prevents a State bank from having branches.

Mr. FLANNAGAN. Look on page 16, line 9.

Senator HITCHCOCK. What is the paragraph? What section?

Mr. FLANNAGAN. Section 10; I can find it in this one, I suppose. Here it is; line 17 on page 16. There you will see "provided for in this and other laws relating to national banks." They have to comply with reserve requirements and submit to the inspection and regulation provided for in this and "other laws relating to national banks."

Senator HITCHCOCK. That does not prohibit it; it simply says that they must comply and conform with the reserve requirements and submit to inspection.

Mr. FLANNAGAN. And other laws relating to national banks.

Senator SHAFROTH. And that prohibits branch banks?

Mr. FLANNAGAN. Other laws relating to national banks.

Senator POMERENE. When State banks have branch banks and they take out a charter under the national banking law, they can retain branch banks.

Senator SHAFROTH. That is the substance of the amendment?

Senator POMERENE. That is the substance of the law as it exists now.

Mr. FLANNAGAN. It is?

Senator POMERENE (reading):

It shall be lawful for any bank or banking association, organized under State laws, and having branches, the capital being joint and assigned to and used by the mother bank and branches in definite proportions, to become a national banking association in conformity with existing laws, and to retain and keep in operation its branches or such one or more of them as it may elect to retain, etc.

Mr. FLANNAGAN. What section are you reading?

Senator POMERENE. I am reading the national banking act. That is where they come in under the national banking law.

The CHAIRMAN. I do not think that is in force now. I do not think they can come in now with branches.

Senator POMERENE. It is section 5155. [Reading:]

It shall be lawful for any bank or banking association organized under State laws, and having branches, etc.

Mr. FLANNAGAN. As a matter of fact, you can not find any national bank that has a branch, and there have been many State banks that have been converted into national banks. The Bank of New York, for instance, is one; and there are many others.

Senator POMERENE. Not that had other branches. This says that a State bank with branches may reincorporate under the national banking law and may retain its branches.

Mr. FLANNAGAN. Do you think that is the law now?

Senator POMERENE. That seems to be. It is the edition of 1908.

The CHAIRMAN. I think that was the law then, that banks at that time having those branches might come in, but they did not exercise that option, and since that time all these national banks are without branches, for the very reason we have in mind, that this is intended to be an individual banking system with competition preserved rather than forming a single bank to gather together powers throughout the country, having a system of branches.

Senator HITCHCOCK. I do not think section 10 bears on State banks.

Mr. FLANNAGAN. You do not think that it does? Of course if there is no law prohibiting banks with branches it does not. I just took it for granted that there was such a law, from the fact that there are no existing national banks with branches.

Senator HITCHCOCK. I understand that State banks in coming in are only required to comply with the national banking act as far as reserves and capital are concerned and submit to inspection.

Mr. FLANNAGAN. I think that those words there, "other laws relating to national banks," would include all laws.

Senator HITCHCOCK. Where do you see that?

Mr. FLANNAGAN. On the seventeenth line.

The CHAIRMAN. Page 16, line 17, requiring them to submit to inspection and regulation provided for in this and other laws relating to national banks. The regulation permits the national bank to have its branches.

Senator HITCHCOCK. It only relates to observing the requirements of inspection.

Mr. FLANNAGAN. Perhaps that is the right construction.

Senator SHAFROTH. Will you not make a copy of this act with the modifications——

Mr. FLANNAGAN. I have it right here, Senator.

Senator SHAFROTH. And give it to the chairman, so that we can have it when we take this bill up section by section?

Mr. FLANNAGAN. I have it right here; I have done that very thing.

(At this point an informal conference was had, which the stenographer was directed not to report.)

Senator REED. I move that we take a recess until half past 2.

The CHAIRMAN. We will meet at half past 2, gentlemen.

(Thereupon, at 1.05 o'clock p. m., a recess was taken until 2.30 o'clock p. m.)

AFTER RECESS.

The CHAIRMAN. Mr. Flannagan, proceed.

Mr. FLANNAGAN. We discontinued while considering amendments at page 21 of the new bill.

There has been a good deal of objection on the part of bankers to the mandatory character of the paragraph marked "(b)," page 21, section 12, requiring Federal reserve banks to rediscount prime paper of other Federal reserve banks. Of course, I do not know what you gentlemen will think of that proposition, but my thought is that it is entirely immaterial whether you insist upon the word "require" or not, for the reason that——

Senator REED. What page is that on?

Mr. FLANNAGAN. Page 21. For the reason that the Federal reserve board can actually control that matter by the question of deposits. All they will have to do would be to suggest to one bank that unless they made the desired discount that they would transfer deposits to cover, which would accomplish the same purpose, and as the banks themselves seem to think that the mandatory character of this paragraph is not Anglo-Saxon, I believe it would be wise just to erase "or require, in time of emergency," and all the balance of the paragraph after the word "banks," in the tenth line, so as to leave it as it was in the original bill, except the word "require"; the words "in time of emergency" were put in as an amendment from the original draft.

Page 22, line 11, reads:

Designate the banks therein situated as country banks at its discretion.

You remember, those of you who saw the circular of the National City Bank of New York, that they made a good deal of fun of that provision, as if the authority was given to the Federal reserve board to designate different banks in the same city as country banks. I think the expression they used was that it was a "joke." My thought is, that if you will put the word "all" in the eleventh line——

The CHAIRMAN. What page?

Mr. FLANNAGAN. Page 22—the word "all"—"designate all the banks therein situated as country banks at its discretion" it would mean that the Federal reserve board could not designate banks as country banks unless they included all of the banks in any particular reserve city.

Senator REED. Do you think that was any substantial objection? Was it not rather a play upon words?

Mr. FLANNAGAN. They did make that objection.

Senator REED. Yes.

Mr. FLANNAGAN. My thought is that I really believe this refers to cities as it stands, but to put the word "all" in it will remove any criticisms of that sort.

On page 23, line 20, after the word "resentations," being a part of the word "representations," I think it would be well to insert the words "to said board," as the contention, I suppose, is that the advisory council will not make their "representations" all over the country, but they ought to make them to the board.

On page 24, under the general title "Rediscounts," in line 20, as the section now reads, the Federal reserve bank would be prohibited from discounting any paper which was secured by Government bonds or State or municipal bonds or any other investment securities. I do not know whether that could have been the purpose of the framers, for the reason that on page 27, in the thirteenth line, the Federal reserve banks are authorized to invest in United States bonds, and any bonds issued by any State, county, district, or municipality. It would seem, therefore, that they should be authorized to loan on the same securities in which they are allowed to invest, and I therefore suggest that in the twentieth line, after the word "merchandise," you would add "or by securities in which the Federal reserve bank is authorized to invest."

Senator BRISTOW. Why not securities that the bank itself is allowed to invest in?

Mr. FLANNAGAN. That is what it suggested.

Senator BRISTOW. The member banks?

Mr. FLANNAGAN. The reason of it is that you specify what the Federal reserve bank may invest in, and I thought it would be subject to less criticism if you allowed them to loan on what they are already authorized to invest in.

Senator BRISTOW. But a national bank is authorized to invest in certain kinds of securities and other kinds of securities it must not invest in?

Mr. FLANNAGAN. Yes.

Senator O'GORMAN. In other words, the statute fixes the kind of securities a national bank shall invest in.

Senator BRISTOW. Why not let it use any kind of securities that the statute permits it to take for securing loans?

Mr. FLANNAGAN. You see, there was considerable discussion in the House on that subject, in the effort of some of the Members to get warehouse receipts used, and it was finally compromised to allow warehouse receipts for merchandise to be used as collateral security to obligations. If you want to make it so broad as to allow the reserve bank to discount any paper that the national bank is authorized to discount, there would hardly be any necessity at all for this section. The purpose of this section seems to be to limit the discounts of the reserve bank to commercial transactions as much as possible.

Senator BRISTOW. That is one other strong objection some of us have to the bill, and what reason is there that a bank should not be permitted to use its assets?

Senator O'GORMAN. Just as a national bank would?

Senator BRISTOW. Yes. Why should it not discount its loans—the loans which the Government permits it to make?

Mr. FLANNAGAN. I do not know of any reason. I am not arguing that proposition; I am simply stating that if you want to confine it to this class of securities, that in order to be consistent you ought——

Senator REED. To make the two sections harmonize?

Mr. FLANNAGAN. Yes. Now, the purpose seems to be in that connection to prohibit speculation, so that banks that are in the habit of loaning to people who buy and sell stocks on margin could not utilize the reserve banks through the member banks. I believe it would be made more emphatic and carry out that idea if you would insert in the twenty-second line—after the word "the" and before the word "purpose," the word "speculative"; and after the word "or," in the twenty-third line, insert the word "marginal"; and in the same twenty-third line substitute for the words "investment securities" the words "credit instruments." As it reads now, it says—

shall not include notes or bills issued or drawn for the purpose of carrying or trading in stocks, bonds, or other investment securities.

The CHAIRMAN. As amended, how would it read?

Mr. FLANNAGAN. As amended, it would read:

Shall not include notes or bills issued or drawn for the speculative purpose of carrying or marginal trading in stocks, bonds, or other credit instruments.

I objected to the words "investment securities" in the original reading, because it might be implied that the banks could loan on securities which are not investment securities; for instance, you might loan on mining stocks, and my opinion is that the word "investment" should come out anyhow. So that I think if you substitute for the two words "investment securities" the two words "credit instruments" that it would include everything of that nature.

There has been a good deal of discussion as to the time that this paper shall run. On the last line, the twenty-sixth, it was originally written "60 days." As amended by the House, that was changed to "90 days."

I believe that it would be wiser to retain the limit of those loans at 60 days, because if the purpose is to maintain paper of short term which is readily convertible, that 60 days would be long enough when the reserve of the bank is down to 33⅓ per cent, because in the next paragraph, on page 25, you are allowed to take paper running 120 days, if the reserve exceeds 33⅓ per cent, at an amount to be fixed by the Federal reserve board. So that my idea is to change the word "ninety" to "sixty" in the twenty-sixth line of the twenty-fourth page; and also change the word "ninety" in the third line of the twenty-fifth page to "sixty."

On the same twenty-fifth page, coming down to the twelfth line, my thought is that you can make the reading of that very much plainer and simpler, if you will make the following change: Insert after the word "discount" the word "the," and erase the letter "s" from the word "acceptances"; erase in the thirteenth line the word "such" and erase the letter "s" from the word "banks"; and substitute therefor "another member bank." Change in the same thirteenth line the word "are" into "is".

Then in the fifteenth line strike out the balance of that sentence, and to the end of the sixteenth line.

Then the paragraph will read:

> Upon the indorsement of any member bank, any Federal reserve bank may discount the acceptance of another member bank which is based on the exportation or importation of goods, and which matures in not more than six months.

The letter "s" would have to be inserted in the fourteenth line after the word "mature," because the words erased—

> and bear the signature of at least one member bank in addition to that of the acceptor,

are superfluous, as they are included in the first part of the paragraph, stating that any member bank may discount the acceptance of another member bank upon the indorsement of a member bank, so it appears useless to put that there.

In the nineteenth line, the word "such" occurs, which must have been——

Senator O'GORMAN. You propose the elimination of the seventeenth and eighteenth lines?

Mr. FLANNAGAN. No, sir.

In the nineteenth line you will find the word "such." It is not clear to what it refers. I suppose it must have been in there before the insertion of that paragraph just before it. I think it would be plainer if you would erase that word and say, "The aggregate of notes and bills bearing the signature," and so on.

On the twenty-sixth page, the seventh line, I believe, in the place of the words "face value," if you will insert the word "amount" it will be an improvement.

And in the eighth line, after the word "capital," insert the word "stock," and it will be made to read plainer. It will then read:

> One-half of the amount of its paid up and unimpaired capital stock.

Senator HITCHCOCK. And that would allow such a bank to rediscount all of that paper at the reserve bank?

Mr. FLANNAGAN. What are you referring to, Senator?

Senator HITCHCOCK. You allow a national bank to give acceptances to the extent of one-half of its capital stock?

Mr. FLANNAGAN. That is in another clause.

Senator HITCHCOCK. And you allow the reserve banks to discount the paper to the extent of one-half the capital stock of the bank?

Mr. FLANNAGAN. Yes.

Senator HITCHCOCK. Those discounts are in addition to the discounts of commercial paper of individuals?

Mr. FLANNAGAN. No. It seems to me that that refers to the whole proposition, that a member bank may not have discounted at any time more than one-half of its capital stock.

Senator HITCHCOCK. No.

Mr. FLANNAGAN. Do you think it does not?

Senator HITCHCOCK. No; there is no limit to that. The only limit seems to be on acceptances.

Mr. FLANNAGAN. Well, then, it ought to read in the nineteenth line "the aggregates of such acceptances," should it not?—No, no; that clause refers to the provision of the national-bank act, which limits the discount of the paper of any one firm or corporation to 10 per cent of its capital, so that if this says that you can not discount more paper it carries out the same limitation of the national-bank act, does it not?

Senator HITCHCOCK. I think not. It says here on page 25 that any member bank——

Mr. FLANNAGAN. Page 25; what line are you reading?

Senator HITCHCOCK. Beginning on line 11.

Any Federal reserve bank may discount acceptances of such banks.

But it can only discount them to the extent of one-half of the capital stock of the member bank.

Mr. FLANNAGAN. Yes; I think that is right.

Senator HITCHCOCK. And on the other page—the next page——

Mr. FLANNAGAN. What bill are you reading from?

Senator HITCHCOCK. The same one you are.

Mr. FLANNAGAN. On the next page?

Senator HITCHCOCK. On the next page. A member bank is permitted to give acceptances to the extent of one-half of its capital stock.

Mr. FLANNAGAN. Yes; I think that is right.

Senator HITCHCOCK. So that it is really allowed to discount at the reserve bank all of the acceptances which it gives.

Mr. FLANNAGAN. Not in excess of one-half of its capital stock?

Senator HITCHCOCK. Not "excess."

Mr. FLANNAGAN. Yes; if somebody else would rediscount an acceptance——

Senator HITCHCOCK. That is to say, it would not be that bank—another bank?

Mr. FLANNAGAN. That is right.

Senator HITCHCOCK. But the point I was making was that those discounts would be in addition to any commercial paper.

Mr. FLANNAGAN. Oh, I think so.

Senator HITCHCOCK. Discounted by that bank, of course?

Mr. FLANNAGAN. I think that is right.

If you look at the twenty-second line on the twenty-sixth page, it reads:

Liabilities to the stockholders of the association for dividends and reserve profits.

Very often in the organization of banks they contribute funds for a surplus, so that it would not be profits. I think it would be wise to change that, inserting after the word "for" and before the word "dividends" the word "unpaid," and after the word "dividends" insert the words "surplus fund," and after the word "and" insert "undivided profits" and erase the word "reserve," so that line 23 would read:

For unpaid dividends, surplus fund, and undivided profits.

On page 27, line 13, after the letter "b" in the parentheses, you have "to invest." It would naturally be supposed that the idea of investment would imply the right to sell again. It would seem, from the context, i. e., the balance of that section, that it was not thus intended, and I do not think that that could have been the real purpose of the framers; that is to say, that it should be confined to an investment in United States bonds, and bonds issued by any State, county, district, and so on, but they must have intended to mean to buy and to sell and to invest. The reason I say that is that in the fourth line of section 15, same page, they use the words "purchase and sell"; in the ninth line they use the expression "to deal in"; but when it comes to the thirteenth line they say "to invest."

Senator SHAFROTH. Why could not that just be changed by putting in the word "deal"?

Mr. FLANNAGAN. "To buy, to sell, and to invest." After the letter "b" just write "to buy and sell and."

Senator O'GORMAN. "To buy and sell" would be the best.

Mr. FLANNAGAN. The only reason I kept the word "invest" there was because of the change previously made, in which the bank was authorized to discount paper secured by securities in which it was authorized "to invest," referring to that same word "invest" here.

Senator SHAFROTH. It would not hurt to leave in that word "invest."

Senator O'GORMAN. It is wholly unnecessary and is surplusage, because it adds nothing to the authorization "to buy and sell." It might be construed to buy and immediately sell, however.

Senator SHAFROTH. That is not likely.

Senator O'GORMAN. I think it would be a strange construction, myself, but I think the word "invest" is used in other parts of the bill.

The CHAIRMAN. Evidently that word was used to make it sound better.

Mr. FLANNAGAN. On the twenty-ninth page, line 11, the last word of that line is "deposit," being a part of the word "depositing." I think it should be changed to "member."

The CHAIRMAN. Should be changed to what?

Mr. FLANNAGAN. To the word "member."

shall be confined to the Government and the member and Federal reserve banks.

Now, if you continue in that same section, on the 13th line, it says:

purchase or sale of Government or State securities or of gold coin or bullion.

It would appear to me that that would limit the Federal reserve bank to State securities only. It ought to be made to include municipal and other securities, because it is otherwise authorized, so that it appears if you make any exception there, unless you erase the whole of it (which I do not think it was necessary at all to put in), then you ought to change the word "State" into "other," and after the word "securities" insert "authorized by this act," so that the exception would be—

with the exception of the purchase or sale of Government bonds or other securities authorized by this act or of gold coin or bullion.

The CHAIRMAN. Other authorized securities?

Mr. FLANNAGAN. What would you say?

The CHAIRMAN. "Or other authorized securities," would serve the purpose.

Mr. FLANNAGAN. That would mean the same thing—"authorized securities."

And on the thirtieth page, I suggest, in the eleventh line, between the word "of" and the word "issue" the insertion of the word "all," and in the next line——

Senator O'GORMAN. Insert what word?

Senator SHAFROTH. "A-l-l."

Mr. FLANNAGAN. And in the next line, so that there can be no question as to what kind of notes are being withdrawn, that between the word "of" and "notes" you will insert "Federal reserve." You see, up above there it speaks of collateral security—"shall be notes and bills"—and while probably it would be construed to mean Federal reserve notes, I think it would be better to have it plain.

In the fourteenth line of the same page, instead of the words "shall be authorized," I should think it would be better to say "shall have authority."

On the thirty-third page, in the third line, I think it would be simply an improvement of English to change the word "reduction" to "decrease," and in the fourth line, after the word "apart," say "by said bank," and in the fifth line——

Senator SHAFROTH. Strike out "apart"?

Mr. FLANNAGAN. No; after the word "apart" and before the word "for," insert "by said bank"; and in the fifth line erase the word "corresponding" and substitute the word "similar," so that it will then read, beginning on the third line—

corresponding increase in the required reserve fund of lawful money set apart by said bank for the redemption of said notes and by the release of a similar amount of the collateral security deposited with the local Federal reserve agent.

I wish you gentlemen would read that paragraph commencing on the thirty-second page, twenty-first line, and see what it is, and then I will suggest a point that I think it does not cover.

Senator O'GORMAN. What is the point?

Mr. FLANNAGAN. The purpose of that is that a bank may reduce its liability for outstanding notes by the deposit of its own notes, other reserve bank notes, or gold and silver, but the liability, unless you cancel the particular reserve notes of the Federal reserve bank that issued them, will not be extinguished by this deposit unless the fund is used for the purpose of extinguishing them.

The CHAIRMAN. That is the objection, to earmarking these notes.

Mr. FLANNAGAN. They ought to be earmarked, or you will not get elasticity; that is my opinion. My thought is that it is incumbent on the reserve agent or the Treasurer to receive gold and silver for the reduction of the liability of the reserve bank, and to use that fund for the cancellation of a similar amount of reserve notes, when they come in, being at that time held by the public. You can not cancel liabilities by depositing the money with a third person, unless that third person uses that deposit for the purpose of canceling the liability. So, I therefore think if, on the sixth line, after the word "agent," you will add "such fund thus deposited"——

The CHAIRMAN. What page and line?

Mr. FLANNAGAN. Page 33, line 6, after the word "agent," the last word in the line, add:

Such fund thus deposited shall be used exclusively for the redemption of an equal amount of the Federal reserve notes originally issued through the bank, thus reducing its liability.

That would make it incumbent, of course, upon the reserve agent or the Treasurer to receive gold or lawful money for the purpose of reducing the liability of the reserve bank which desired to reduce its liability to see that it was applied for that purpose.

Senator HITCHCOCK. Do you think that the reserve on deposit in the Treasury is adequate to make these redemptions?

Mr. FLANNAGAN. That is 5 per cent, is it not?

Senator HITCHCOCK. Yes.

Mr. FLANNAGAN. I suppose so. I should think that 5 per cent would be adequate.

Senator HITCHCOCK. The present law provides 5 per cent?

Mr. FLANNAGAN. Yes.

Senator HITCHCOCK. For national-bank notes, and it has proved utterly inadequate.

Mr. FLANNAGAN. Yes; I believe that is true.

Senator SHAFROTH. The Treasury has got to draw money out of its general funds, all right, in order to redeem national-bank notes?

Mr. FLANNAGAN. I believe it has.

Senator HITCHCOCK. This being an elastic currency, will not the redemptions be even greater?

Mr. FLANNAGAN. They may be. You asked me this morning if I thought the redemptions would be the same, did you not, as the present national-bank currency? I am not able to tell, and I do not think anybody is. It seems to me it is a matter of experiment.

Senator HITCHCOCK. Under the present law the 5 per cent fund in the Treasury has proved utterly inadequate to redeem the national-bank notes as presented?

Mr. FLANNAGAN. Yes.

Senator HITCHCOCK. Is it not an inevitable conclusion that a reserve of the same kind will also prove inadequate for the new notes?

Mr. FLANNAGAN. I think that is a very reasonable conclusion, Senator. That might be remedied by keeping a larger amount in the reserve banks.

Senator SHAFROTH. Could it not also be accomplished by making these notes so that they could be used by national banks as reserve?

Mr. FLANNAGAN. Never in the world.

Senator SHAFROTH. If they have this power to send them down to Washington, would it not answer as reserve?

Mr. FLANNAGAN. They ought not to, because they are a Government bank and ought not to be——

Senator SHAFROTH. The question is whether if they did have this power it would not relieve the drain on the Federal Treasury.

Mr. FLANNAGAN. It is not a very material drain, because you can make the banks themselves pay it more rapidly out of their own assets if you require it. You can not assume that it is positively so, that with 12 Federal reserve banks scattered throughout the country that people are going to take the trouble to send their notes all the way to Washington to get them redeemed. It is reasonable to suppose that they will send them to the nearest Federal reserve bank.

Senator SHAFROTH. In the aggregate that would amount to the same thing.

Mr. FLANNAGAN. No; the bank would then redeem and not the Treasury.

Senator SHAFROTH. But they have got to get the gold from the Treasury.

Senator HITCHCOCK. The redemptions under the present law are not caused by people sending these notes directly to Washington for redemption?

Mr. FLANNAGAN. Of course not.

Senator HITCHCOCK. As outlined this morning, because banks throughout the country when they get bank notes are unable to use them as reserves, therefore when they send remittances to New York, Chicago, or St. Louis they send national-bank notes. Those notes give them then the full reserve credit in those three cities. When those three cities receive them, they can not count them as reserves in their vaults, and therefore they quickly send them to Washington and get legal-tender money.

Mr. FLANNAGAN. Quite right, and to that extent that constitutes elasticity, that very redemption—sending them back gain.

The CHAIRMAN. Mr. Flannagan, I ask you this question: Does the redemption of those national-bank notes really make them elastic?

Mr. FLANNAGAN. Make them elastic?

The CHAIRMAN. Yes.

Mr. FLANNAGAN. The redemption of the present national-bank notes?

The CHAIRMAN. Yes.

Mr. FLANNAGAN. No; I do not think that they do. I do not think that does make them elastic, as they should be.

The CHAIRMAN. Then, what is the purpose——

Mr. FLANNAGAN. Of having them redeemed?

The CHAIRMAN. Yes.

Mr. FLANNAGAN. Why, because it is a debt, and they ought to be paid at the instance of whoever holds them.

The CHAIRMAN. Then it is not a true money?

Mr. FLANNAGAN. No. It is not coin; and of course paper money is a debt, whether issued by the Government or issued by a bank. You can not make it anything but a debt.

The CHAIRMAN. Granted that it is a debt——

Mr. FLANNAGAN. Yes.

The CHAIRMAN. A gold certificate is a debt?

Mr. FLANNAGAN. It is a warehouse receipt.

The CHAIRMAN. Call it a warehouse receipt; nevertheless, it is a debt—a promise to pay the gold which is warehoused, is it not?

Mr. FLANNAGAN. Yes; the element of trusteeship enters.

The CHAIRMAN. That is a mere matter of synonym.

Mr. FLANNAGAN. There is quite a difference between the promise of a bank or the promise of a Government to pay from assets and when you have a particular promise to pay from a particular fund. It is the same thing as a warehouse receipt. The ownership of the gold is in the holder of the gold certificate.

The CHAIRMAN. The effect of treating these bank notes as requiring this redemption, when you do not require a redemption of the gold certificates or other moneys, is to degrade these national-bank notes and compel redemption because they are degraded. Is not that the fact?

Mr. FLANNAGAN. I do not think so at all. How could you require the redemption of a gold certificate any more than to state that it will be honored on presentation? You do the same thing with national-bank notes. It is the promise of the bank to pay, but in the latter case payment may be made with the bank's property.

The CHAIRMAN. But you impose upon this national-bank note, which is treated as currency of the country and which is secured by Government bond, the provision that it shall not be used as a reserve, although some of the State banks do use them as reserves, I think, and to quite a considerable degree. They have $107,000,000 of them as reserves. But the fact that the national-bank notes are not permitted to be used by the national banks as reserves——

Mr. FLANNAGAN. And ought not to be; that is the proposition I contend for. I beg your pardon——

The CHAIRMAN. I have not concluded my question.

Mr. FLANNAGAN. I beg your pardon.

The CHAIRMAN. It is that circumstance which compels these national-bank notes being of a less current value than the other legal-tender money of the country that causes them to come back into the Treasury and causes the Treasury to keep on hand $35,000,000 of gold or lawful money for their redemption, and in addition to that the Government is also required, because of the volume of these notes coming in, to keep a still larger sum, in that way really contracting the currency to the extent of about $60,000,000 of current funds——

Mr. FLANNAGAN. Did you ask me a question?

The CHAIRMAN. I was asking you if that was not the case—if that is not the cause of this redemption?

Mr. FLANNAGAN. I think the cause of the redemption is that they can not be counted as reserves. I think that is the cause.

The CHAIRMAN. That is the point.

Mr. FLANNAGAN. And I think it ought to be so. I do not think that any debt ought to be counted as a reserve, but that the true reserve to pay debts with is gold, and that any other payment is a swapping of one debt for another debt.

Senator SHAFROTH. Not even the United States notes now outstanding?

Mr. FLANNAGAN. Not even greenbacks. I contend that the greenbacks ought to be redeemed.

The CHAIRMAN. Ought not to be used as money?

Mr. FLANNAGAN. No.

Senator SHAFROTH. You would have nothing but gold as money, or gold certificates?

Mr. FLANNAGAN. I would have anything that could be converted into gold.

Senator SHAFROTH. You would not have that legal tender?

Mr. FLANNAGAN. No.

Senator SHAFROTH. It would not be money in the strict sense?

Mr. FLANNAGAN. It would not be money in any strict sense; legal tender does not make it money.

Senator SHAFROTH. We think it does.

Mr. FLANNAGAN. You get into the greenback idea.

Senator SHAFROTH. We get into the proposition of having the currency as does every nation on the face of the globe that bears the stamp of the Government—every single bank note of Europe is full legal tender for payment of debts.

Mr. FLANNAGAN. I can not dispute that statement, but unless you have a very good authority for it I should doubt it.

Senator SHAFROTH. I have seen it stated so.

The CHAIRMAN. There is no doubt about the notes of the Reichsbank being legal tender, there is no doubt about the notes of the Bank of France being legal tender, nor of the Bank of England.

Senator SHAFROTH. The Bank of Canada notes are legal tender?

Mr. FLANNAGAN. Are they?

Senator SHAFROTH. Not the Bank of Canada but the Dominion notes; yes, sir.

Senator HITCHCOCK. Mr. Flannagan, the operations of this bill, particularly under the amendment which you suggested this morning, are likely to result in the possibility of a considerable inflation of the currency?

Mr. FLANNAGAN. The possibility of the inflation of the currency? I think I stated that for the present the total amount of additional currency that could be issued on the hypothesis that every bank issued its maximum amount, would be some three hundred and odd million of dollars. The exact amount you will find by referring to the figures I gave.

Senator HITCHCOCK. I will change that question.

Mr. FLANNAGAN. Let me finish, please, sir. The exact amount will be found by deducting the present outstanding national-bank notes from the capital stock of the national banks.

Senator HITCHCOCK. I really intended to say that the result of the operations of this bill will be the probability of a considerable inflation of credits.

Mr. FLANNAGAN. Which is the same thing.

Senator HITCHCOCK. No; it is quite different. And I want to ask you if I am correct in this conclusion: We considered the case this morning of a bank with a million dollars capital. Let us go further and suppose that that bank has $7,000,000 of deposits and approximately $7,000,000 of loans. Under the present law it might issue $1,000,000 of currency based on bonds, and that is all?

Mr. FLANNAGAN. Yes.

Senator HITCHCOCK. It can not rediscount its notes without resorting to illegitimate banking?

Mr. FLANNAGAN. It can not rediscount what?

Senator HITCHCOCK. Under the present law?

Mr. FLANNAGAN. It can go to a correspondent bank and get a rediscount without resorting to illegitimate banking.

Senator HITCHCOCK. It is not considered good banking, and they do not do it to a considerable extent. The Treasury statement shows merely a nominal amount.

Mr. FLANNAGAN. Let me see how much that is, please. [Referring to papers.] I think it is many millions.

Senator HITCHCOCK. It is very small compared to the aggregate.

Mr. FLANNAGAN. Of course, I grant you that the matter of rediscounts ought not to be regular banking. I think that a bank that continually asks rediscounts under our present system shows an indication that it has not got sufficient capital for its business.

Senator HITCHCOCK. It is a very small amount. I will not go——

Mr. FLANNAGAN. I can tell you the exact amount.

Senator HITCHCOCK. That is immaterial as to the exact amount. Under the new law, and under your amendment, a bank with $1,000,000 capital, and, say, $7,000,000 of loans and $7,000,000 of deposits, could issue $1,000,000 of currency, could issue $500,000 of acceptances, which are nothing but the loan of its credit, and could procure easily $1,000,000 of rediscounts at the reserve bank. Would that not, in the case of that bank, mean the addition of $1,500,000 to the credit which it now extends?

Mr. FLANNAGAN. I think so.

Senator HITCHCOCK. And applying that to all the banks in the country, does that not mean a great inflation of credit?

Mr. FLANNAGAN. Under the figures that you gave me, if I followed you correctly, I believe that a bank could do it, but you can not presume that every bank is simply going to do it unless they have got some securities behind it on the other side. Banks do not go on and issue these obligations for the mere fun of the thing; they issue them as a matter of profit, having due reference to safety.

Senator HITCHCOCK. I am seeking to get from you now an answer to the question whether or not under the natural operation of this bill it will not make it possible for banks to increase the volume of credit now existing?

Mr. FLANNAGAN. I think that is true.

Senator HITCHCOCK. I think so, too. I think it will add a large per cent to the possible credit issue of every bank.

Mr. FLANNAGAN. Is that undesirable? Not a credit without a debt, mind you—as I tell you, they are relative terms. Whether credit or debt which is amply secured, does not that facilitate and encourage the business of the country?

Senator HITCHCOCK. Have you any belief as to the proper relation between gold and credit or not? This, without increasing the supply of gold, would mean a great increase in the credit based on it?

Mr. FLANNAGAN. Your question is——

Senator HITCHCOCK. Is there any proper relation, is there any per cent that the world has accepted as proper?

Mr. FLANNAGAN. I do not know of any per cent. In the various countries the experience is somewhat different. I should say that about 10 per cent for ordinary cases would be sufficient reserve for a bank to hold against its liabilities. I think experience has demonstrated that.

Senator HITCHCOCK. Do you personally favor this provision which allows banks to give acceptances to the extent of half of their capital stock?

Mr. FLANNAGAN. I think under the restrictions that it is for the importation or the exportation of merchandise that it is all right. It does not allow acceptances to be given in the ordinary sense of the word.

Senator HITCHCOCK. An acceptance is simply a loan of credit?

Mr. FLANNAGAN. Yes.

Senator HITCHCOCK. Loan of a bank's note?

Mr. FLANNAGAN. That is acceptance.

Senator HITCHCOCK. Do you think that it is right for a bank which is in the business for receiving deposits and making loans to practically indorse the paper of other people?

Mr. FLANNAGAN. If they have got satisfactory security, it is all right; there is no more objection to it than receiving a deposit. It is a form of business that is very largely adopted abroad. They are both exchange of debts.

Senator HITCHCOCK. Yes; but is it not a fact that the acceptances given abroad are largely by financial houses and not by banks of deposit?

Mr. FLANNAGAN. Nearly all banks abroad do issue letters of credit. The largest bank in England is the London City and Midland of London, with which I had at one time an account, which issues letters of credit and gives acceptances, and I think it is the common practice of banks in England to give acceptances, and it is used for facilitating the transfer of property from one place to another; and where the credit of the bank is known and the credit of the individual who wants to perform the operation is not known, that is the purpose of issuing these commercial credits.

Senator HITCHCOCK. I have the impression, and I got it from an English banker, that acceptances in England were given largely and chiefly by financial houses, and that they were not given by banks which were receiving deposits from the people.

Mr. FLANNAGAN. I think they are given by merchant bankers; I think they really call them that. I think to the largest extent—take Brown, Shipley & Co.; they are not classed in England as bankers, they are classed as merchants. We class them here as bankers. But, in addition to those houses, international houses which have correspondents or branches in various parts of the world, the incorporated banks also do issue letters of credit and do give acceptances. The giving of an acceptance is an incident to the issuance of a commercial credit and must be a part of it.

Senator HITCHCOCK. A few moments ago you said that the Federal reserve board would be able by its power to control the deposits of the United States to really compel a Federal reserve bank to loan its funds to another Federal reserve bank?

Mr. FLANNAGAN. Yes.

Senator O'GORMAN. I think the statute requires or gives express direction.

Mr. FLANNAGAN. Yes.

Senator HITCHCOCK. Do you think that is a good power to have vested in any central reserve board?

Mr. FLANNAGAN. I do not see how you are going to divest it of the power. You have got to give the power to somebody who is going to control these deposits.

Senator HITCHCOCK. I am not speaking of deposits only, but the power of the central reserve board to dictate the policy of a central reserve bank.

Mr. FLANNAGAN. But you can not presume that these men are going to dictate it for undesirable purposes. The men of the Federal reserve board are supposed to have the interests of the country at heart.

Senator HITCHCOCK. Now, one of the witnesses who preceded you, Prof. Sprague, argued as one of the benefits of this bill that the 12 Federal reserve banks would be able to control the policy of the individual banks of the country by threatening to withhold from them the privilege of rediscount. He said if a bank, for instance, was violating the ethics of banking in its remittances, or otherwise violating the standards established by the Federal reserve bank, that Federal reserve bank would refuse to discount paper for that offending bank, and thus compel it to adopt a different policy.

Mr. FLANNAGAN. I think that theory must have proceeded from a theorist.

Senator HITCHCOCK. You think that the Federal reserve board, under the terms of this bill, is compelled to discount paper for every bank?

Mr. FLANNAGAN. Do I think——

Senator HITCHCOCK. The Federal reserve bank is compelled under this bill to discount paper for any member bank?

Mr. FLANNAGAN. As a matter of practice, yes; but I think there would be some limitation to it.

Senator HITCHCOCK. Do you think it is a discretionary power that they have, or have they no power to refuse discount paper?

Mr. FLANNAGAN. I have not examined critically as to that, but my judgment would be that the Federal reserve bank should have the authority to decline or reject the discounted paper.

Senator HITCHCOCK. You are rather a friend of the idea of independent banking?

Mr. FLANNAGAN. I certainly am.

Senator HITCHCOCK. Do you think a Federal reserve bank located in Chicago, for instance, should have the privilege of saying or intimating to the Nebraska banks——

Mr. FLANNAGAN. If that was in the district?

Senator HITCHCOCK. If that was in the district—that they are extending their loans too much; that farmers are borrowing too much money for agricultural implements, that too much credit is being extended for building, and should indicate to the Nebraska banks that they must curtail their loans or, as a penalty for refusal, they would be restricted or perhaps denied the privilege of discount? Would you like that condition?

Mr. FLANNAGAN. I am inclined to think that it is necessary to have some restriction. I believe in the independence of the individual banks. I believe if you give them the power of circulation, as suggested this morning, that under all ordinary and normal conditions they can accommodate the needs of their customers and that when they go to the reserve bank it means, as a rule, that they are getting beyond the capital of their own community. I think that the restraint is desirable.

Senator HITCHCOCK. The reason that they go to the Federal reserve bank is because they have been required to give up part of the capital that they are now using in their own community, and central and reserve city banks have been compelled to give up a part of the deposits which they are now holding?

Mr. FLANNAGAN. I doubt very much if it is burdensome on the individual banks under the provisions of this law that they are giving up very much capital on which they were earning profits before. If you take into consideration the reduction of reserve which is given them, you will find that the country banks are not restricted in the amount of their earning capacity. I think Senator Reed yesterday asked a question of Mr. Frame in that connection, figuring it on that basis; so that it seems to me, Senator, that you want some restriction.

Senator HITCHCOCK. Then you favor the development in this country of a power which will be able to dictate to the individual banks how far they shall go with their loans and what class of loans they shall take, how they shall treat their customers?

Mr. FLANNAGAN. I should want that power very much restricted.

Senator HITCHCOCK. Is it restricted in this bill anywhere?

Mr. FLANNAGAN. I am inclined to think it is.

Senator HITCHCOCK. Can you point it out?

Mr. FLANNAGAN. I will examine it more critically with a view of looking into that and let you know later.

Senator HITCHCOCK. I have not found it.

Senator REED. Do you think, in the absence of a restriction, that the influence of the reserve bank might be so exercised as to be potential to any great extent over the member bank?

Mr. FLANNAGAN. In the absence of any restriction whether it could be potential; is that what you mean?

Senator REED. Yes; and whether it is likely to be?

Mr. FLANNAGAN. The answer to the question is not clear in my mind. It seems to me that if your thought, Senator——

Senator REED. I will put it in a different way.

Mr. FLANNAGAN. Yes; it would be a help if you would.

Senator REED. We organize this system; we have a regional reserve bank for four great States, embracing 650 national banks. This bank is the only medium under the bill by which the banks can get money issued by the Government in the time of necessity or need; it is the place they go to regularly for discounts, etc. Does that vest in the management of that regional bank such powers and influence as to give that management a commanding or material influence over the member banks?

Mr. FLANNAGAN. I do not think so. The thought in my mind is that these reserve banks should be used as a combination of the assets of banking interests of the particular district in which they are located; that they should be friendly, a part of the system; that if there should be a period similar to the times when the combination of banks was heretofore made in troublous times—I do not mean that assistance should be confined to panicky or commercial crises, but I mean the fact that these banks exist in itself will be a tower of strength to the balance of the banks; that there is a place where they can go and get assistance.

Senator REED. Which is the beneficent side?

Mr. FLANNAGAN. Yes.

Senator REED. A Government can not exist unless power is vested; and, assuming a perfectly beneficent and perfectly intelligent government, the more power you have centralized the better, but experience has shown us that in setting up a government we must put checks upon its power, because every time we have granted unlimited power we have had in the end unlimited abuse. That is by way of illustration. Now, while we are setting up these regional reserve banks, we must not set up a great power which might be exercised——

Mr. FLANNAGAN. To the disadvantage——

Senator REED. To the disadvantage of the member banks or of the general community.

Mr. FLANNAGAN. I agree with you exactly on that.

Senator REED. The question is not, therefore, whether these banks ought to be used for a beneficent purpose, but whether they can be used by evil-disposed people for bad purposes; that is the point. You say they ought to be used in a certain way. I grant you that, and if used in that way and only in that way they would, of course, be good thing.

Mr. FLANNAGAN. You must take into consideration the organization of these banks. You see that two-thirds of the board of directors of these banks are selected by the member banks—men who are interested in the member banks—so it is natural to be supposed that their interest will be interlocking and mutual.

Senator REED. That is all right, so far as the member bank is concerned, but how about the public—the community?

Mr. FLANNAGAN. But the reserve banks do not come in contact with the community except through the member banks.

Senator REED. What I have in mind is this—I am not trying to argue a question with you; I am trying to direct your thoughts to a question—the territory of Nebraska, Missouri, Kansas, and Oklahoma, with approximately 600 banks in it, all now separate and independent from each other, is organized into a region, and some place in it is located a regional reserve bank. There must be a human management and there must be a dominating influence and mind controlling that management. I take it that would necessarily be the president of the bank and the six members of the board selected by the banks. You are a banker in the city of Omaha, and, like all banks, you are expanding your credit as far as you ordinarily can in order to make money with safety, as you regard it. You get pretty close to the edge at times——

Mr. FLANNAGAN. Get pretty close to the edge——

Senator REED. The danger edge sometimes, and you know that there may come a catyclism of some kind which you can not anticipate, and when that time does come there has been provided one place for you to go for help. I am the president of this regional reserve bank—the only way I will ever get the presidency is in this illustration——

Mr. FLANNAGAN. You are the president.

Senator REED. Suppose I say to you, as time runs along, "Mr. Flannagan"—I am going right back to the very illustration which

Senator Hitchcock used—"you are carrying too large farm loans. Are you not carrying them at too low a rate of interest? Do you think that is good banking?" Would you not be very likely to hearken to that suggestion?

Mr. FLANNAGAN. Your question is so long I have really lost exactly what is the position you give me. I understand you are the president of the regional reserve bank. Where am I?

Senator REED. You are president of the local bank in Omaha.

Mr. FLANNAGAN. I am the president of the local bank? Now, what is the question, Senator. [Laughter.]

Senator REED. Is there anything especially amusing about that question?

Mr. FLANNAGAN. It is amusing about my getting lost.

Senator REED. The question was neither very long nor very involved. You just let it slip out of your mind, which we are all likely to do. I am the president of the regional bank in this illustration, and you are the president of the bank in Omaha, which is a member, and you are loaning large sums of money throughout the State of Nebraska, and I say to you, "Do you not think that you are putting out too many loans, and that you are loaning at too low a rate of interest." Do you not think you would be very likely to hearken to that suggestion?

Mr. FLANNAGAN. I certainly do; yes.

Senator REED. Suppose I was to say to you:

> You are paying 3 per cent interest on deposits. I think that is more than a bank ought to pay; I do not like it; I would a little rather not discount your paper so heavily that you bring in here.

What do you think you would do?

Mr. FLANNAGAN. I should probably say—I would maintain my right of action—I am the Omaha bank and you are the Federal bank saying to me that—I should probably say to you, that—

> I should prefer to maintain my independence of action; that I am managing my bank in accordance with the best judgment of my board of directors. I will tell them that you think we are paying too large interest on deposits. If they decide that it is too large, and that your opinion is of such a nature that we ought to discontinue, or you can show me wherein that that is true, then I will reduce it, but I will take your opinion under very serious consideration.

That is the way I would answer that.

Senator REED. I understand, of course, that a bank that is perfectly strong and always was well within its resources could afford to be independent. What I am really trying to find out, is whether there is a danger, through this mere organization of a condition ultimately being brought about whereby that central organization becomes the inspiration and practically the guide for the policies of the member banks.

Mr. FLANNAGAN. I do not think that that follows at all. I think the independence of individuality is preserved under the organization of the banks themselves, especially if you will give them all the normal functions of banking.

Senator REED. Do you think there would be any danger—here is a great enterprise, obliged to be carried on by large advancements from the banks—of that enterprise being wrecked by a suggestion from me, as president of the regional bank, that I did not think those securities desirable for rediscount?

Mr. FLANNAGAN. But, under the regional reserve banks, you are not allowed to take those; that is not the purpose of the regional reserve bank, to furnish capital for outside——

Senator REED. You did not understand me. Assume that there is a large institution, a heavy borrower——

Mr. FLANNAGAN. Not a bank, but an industrial?

Senator REED. An industrial, a merchant, having to carry large amounts of paper, so much so that one bank does not carry it as a member; and I was to say, as president of the regional bank, that we did not care to rediscount that paper. Would not there be great danger that that would wreck that institution, because every bank within reasonable limits, as a member of the regional bank and must all come to me finally to rediscount that paper——

Mr. FLANNAGAN. I would think that if you, the president of the reserve bank, were undertaking to regulate the industrial development in my particular section that you were going beyond your powers.

Senator O'GORMAN. Would you not be likely in that event to appeal to the reserve board in Washington and have some change made?

Mr. FLANNAGAN. I probably should.

Senator REED. Suppose I do not put this on you as an absolute demand, and say "I will not take it," but simply say, "Now, we do not just like this paper. Do you not think you had better go a little slow with it?"

Mr. FLANNAGAN. I would tell you I had respect for your opinion, and I would consider it, but that I would not let that be the final influencing cause for my action.

Senator REED. I want to get at the question as to your candid judgment whether that would not be very likely, in many instances, to close the credit of that whole region to that enterprise?

Mr. FLANNAGAN. I do not think so, Senator. I do not think such a power of an individual could be exercised to the detriment of a whole community of that sort, by the expression of an opinion, when the men in active control of the capital in the community favored it, and I do not believe as the Federal reserve president, you would attempt to put your judgment against the local judgment on a local enterprise.

Senator REED. I think, on the other hand, without any experience in banking, that if I was president of the reserve bank and saw a lot of that paper coming in, and I began to doubt as an individual, I would be very likely to suggest it to the men who came in with it to me to rediscount, and when I did do it I sort of have an idea that that institution, having no other place to go for money, because of this organization, except to the member banks, would go out of business.

Mr. FLANNAGAN. Not until the president——

Senator O'GORMAN. Could you not appeal to a board?

Senator REED. What would the credit of an institution amount to if they are compelled to come up here to Washington in an appeal?

Mr. FLANNAGAN. I think it is an abstract question.

Senator REED. I do not think it is an abstract question.

Mr. FLANNAGAN. In point of fact, do you not think that the local bank president would show to the Federal reserve president that his position was not correct? Would he not lay out his books open to him and say, "Here is what I have got; here is the statement of my condition," and the Federal reserve bank, not having any prejudice against this man, not desiring, as a matter of prejudice or feeling, to discourage his development, would naturally be open to conviction.

Senator REED. Suppose he was a different kind of a banker. Let me illustrate to you what I mean: You and I know perfectly well that without any legal organization, but simply by virtue of combinations that have grown up, powerful concentration of wealth in the hands of a few great institutions, and some kind of community of interest, that it has happened time and again that great enterprises have suddenly found their credit shut off in the chain of banks they have been doing business with, and before they could establish a credit elsewhere their doors had been closed. That certainly has happened time and again in regard to great enterprises of this country—the squeezing process—and if it has been done by men—I was going to say wicked men, and I think I will use that term—outside of any regular progress of its growth, such an influence should obtain control of a lot of these regional banks——

Mr. FLANNAGAN. Oh, but that is impossible.

Senator REED. Why is it?

Mr. FLANNAGAN. That one influence can control any number of the regional banks?

Senator REED. Yes. Let me see if I can not illustrate that: I am not trying to be chimerical, and I am not trying to fight this bill, but I am trying to find out if there is a danger in it. If there is a danger, I want to know it.

One banker the other day testified that when you came to select the board of directors of the regional bank that it was his opinion that the great banks, being largely interested and very active, would probably be active in the matter of the selection, and the smaller banks would be probably somewhat inactive or uninterested, and that the result would probably be that the directors would in the end be selected by the same important banks of the district. Do you think that is likely to obtain?

Mr. FLANNAGAN. No; it could not happen, because under this law the banks are divided into classes, according to the different capital, and each class of banks select electors which elect, so that each class of banks would necessarily be represented, the smaller banks as well as the others. It is impossible for any individual to use influence in that regard. I think that is absolutely impossible.

Senator REED. I am sticking to one reserve bank. When I get through with that——

Mr. FLANNAGAN. I understood you to say they might have several.

Senator REED. That was in a former question. I am now referring to one reserve bank. I want really to get your best judgment about this matter. I have had something to do with politics.

Mr. FLANNAGAN. I think you have.

Senator REED. And I have seen a law that gave to every voter the same right to vote and the same right to participate in a primary, and I have seen these glorious direct primaries, and I have seen the same half-dozen men running the very primary where everybody had a right to vote. They ran the thing when we had the old caucuses and the old conventions. The reason they ran them was because of their activity, their intelligence, their constant planning and work. Is it not very likely that when we come to elect the board of directors of a regional bank, that the big, strong men, the active, virile bankers will be the ones who are selected, instead of the smaller, the obscure, and the almost unknown men?

Mr. FLANNAGAN. I think those are the men who ought to be selected, the big, strong, active men.

Senator REED. When you get to that kind, is it not true to-day that the big, strong, active, virile bankers of the large cities of this country are nearly always in a direct or indirect alliance with the big, strong, bankers of New York City and other money centers?

Mr. FLANNAGAN. I think they have desirable connections; yes.

Senator REED. And there is frequently a stock ownership running through them, is there not?

Mr. FLANNAGAN. That may be. I am not posted as to that.

Senator REED. If that is true, why is it not entirely possible to work out not only a dominating control in one regional bank, but to unite that control with several regional banks; and does not that sort of control to a great extent exist to-day without any Government organization?

Mr. FLANNAGAN. I do not believe that that is a practical result to be feared. I think that that is one of the reasons why you want a number of Federal reserve banks. I do not think you want to make one section dependent upon another. I think you ought to make the association of the banks of the district uniform as much as possible, so as to have each district independent of every other district. And I think that is one of the great reasons why you want several districts. That is the great objection to the central bank, and the further you get away from it, within certain limitations, the better.

Senator REED. Then there is a danger point somewhere that you want to avoid, is there not?

Mr. FLANNAGAN. I do not believe the danger exists under this bill, Senator.

Senator REED. Let me follow that a moment. I want to illustrate how far this can go. This committee was waited on by a committee of the American Bankers Association.

Mr. FLANNAGAN. Yes; I saw the report.

Senator REED. All of them agreeing absolutely upon a program. They were very fine, elegant, intelligent gentlemen. Do you not think that there was a dominating mind down there that picked these men and sent them here with this canned argument and philosophy?

Mr. FLANNAGAN. Well, Senator, I do not believe I ought to express any opinion about that.

Senator REED. I have one which I would unhesitatingly express—not that I am criticizing them, but there must have been a dominating force. I think it was here.

Mr. FLANNAGAN. In Washington?

Senator REED. Here in Washington. I think it came here to Washington. I think it had "side-burns" when it came, and I say that respectfully. There was before us a banker from an extreme southern city wedded to this doctrine and most forcefully advocating it. I have been informed that his bank has very close and intimate connections with New York City to-day. I want to know if those forces that exist, having reached out with their ramifications in many directions, it would not be very likely that in a short time they would control and dominate every one of these regional banks so far as they can be controlled and dominated under the terms of this bill. Of course there is a governmental control above.

Mr. FLANNAGAN. I think danger from influences derogatory either to the welfare of the individual banks, or the people is covered in this bill. I do not believe that you need fear the concentration of the money power—if that is what is in your mind.

Senator REED. Would not that be lessened, if instead of giving the banks the right to select two-thirds of the members of the boards of directors, the Government, the people, selected at least half?

Mr. FLANNAGAN. No; I think that the representatives of the banks, in the Federal reserve banks, of two-thirds, is as it ought to be. They are the men that contribute the capital; they are the men that are interested in the individual banks who compose the Federal reserve banks.

Senator REED. Did you not pretty clearly demonstrate here this morning that they did not contribute the capital, that the people of the United States contributed all of the banking capital excepting a bagatelle?

Mr. FLANNAGAN. No.

Senator REED. I thought I so understood your paper. I believe you will have to revise it.

Mr. FLANNAGAN. Oh, no; I will stand by that paper.

Senator REED. It is a very elegant one.

Mr. FLANNAGAN. When I say the capital of the Federal reserve banks, I mean the capital stock which is contributed by the other banks. I am not speaking of deposits in this.

Senator REED. That is what does the banking business.

Mr. FLANNAGAN. But the Federal reserve banks are going to handle large deposits from the Government. It is going to be a means where the people are going to get the use of money that has been tied up.

Senator REED. So much the more reason, if it is the people's money, that the people should have something to say about it.

Mr. FLANNAGAN. I think the people ought to have something to say.

Senator REED. But you think they ought to have only one-third of the say. You and I know that the minority stockholder and the minority director is not anything more than an interested onlooker in the management of any corporation.

Mr. FLANNAGAN. Well, but don't you see that you have got over and above this control of the reserve banks, the Federal reserve board, which in my opinion ought to be where it is. You have got over and above that the Federal reserve board which is composed of Government officials?

Senator REED. Yes; but what right of control, after all, has that Federal reserve board? What can it do?

Mr. FLANNAGAN. What right of control?

Senator REED. Yes; what can it do?

Mr. FLANNAGAN. The powers of it are claimed to be so immense that that is what the bankers are kicking about.

Senator REED. I know they have been kicking; but it is the same men that kick the most vigorously who were the men who wanted one central bank privately controlled.

Mr. FLANNAGAN. But I have always opposed that.

Senator REED. And the right to establish branches?

Mr. FLANNAGAN. Yes.

Senator REED. So that in view of their appetite we need not be surprised if they send up their bowl like Oliver Twist did, very frequently?

Senator BRISTOW. I think, Senator, that all they asked was that we give them one-third representation on the Federal board.

Mr. FLANNAGAN. I do not think that they are entitled to any in that board.

Senator REED. I am interested in this thing from this standpoint: I mean whether they have a real control. I am questioning it now. I do not mean I am passing on the bill. This bill provides that one of these regional reserve banks shall have all the powers of a national bank. That is not the exact language, but that is what it means. A national bank has very broad powers. In addition to the powers which are expressly granted to a national bank are all of those common law property rights which every proprietor has over his property save and except as that right is expressly restricted. You give to a Federal reserve board certain limited powers of regulation. I would like to ask you if you have examined this bill with reference to just what a Federal reserve bank could do if it wanted to go to the extreme of its rights? Has it not got very broad powers?

Mr. FLANNAGAN. I have examined the bill, but not critically with that point in view. If you will turn to this report—I do not know the place. Perhaps somebody more familiar with it than I will tell me where the powers of the reserve board are recapitulated?

Senator O'GORMAN. You will find them all on pages 21 and 22; and as bearing upon the control that the Federal board has over the regional board, look at subdivision F on page 22, which confides to the Federal board the power to suspend the functions of Federal reserve banks, in substance, whenever they see fit.

Mr. FLANNAGAN. That is in the bill, but it is very much fuller in this report.

Senator SHAFROTH. On page 46 the powers of the reserve board are set forth in smaller type and they are quite elaborate.

Mr. FLANNAGAN. Senator, if you will read page 46 and page 47 of the report, No. 69, of the Banking and Currency Committee of the House, it gives you in detail what the powers of that Federal reserve board are, and if you will read them I think you will find that they have considerable authority.

Senator REED. I would rather read the bill than that comment.

Mr. FLANNAGAN. This is a summary of the various clauses in the bill, because all the powers of the Federal reserve board are not stated under that title of the bill, "Federal reserve board." They are scattered throughout the bill in various places. I think they are pretty full powers, and are summarized on pages 46 and 47.

Senator REED. I did not start this with the idea of arguing. I wanted to know if Mr. Flannagan had studied that, for my own information. I have got some opinions of my own about it. But if you have not, Mr. Flannagan, I would be glad if you would look at it, and see how far this might be of use.

Mr. FLANNAGAN. Mr. Chairman, may I continue? I would like to go away somewhere near 5 o'clock. I am just going down in Virginia.

Senator O'GORMAN. What page are you on now?

Mr. FLANNAGAN. I have forgotten.

Senator O'GORMAN. I think you were on page 33.

Mr. FLANNAGAN. If you will continue that same page, I think the intention can fully be carried out and the expression made clearer by a slight change in lines 14, 15, and 16. I would suggest that in the fourteenth line, after the word "receive," you insert the words "from any member bank," so that it will read: "Reserve bank to receive from any member bank, on deposit, at par, without charge for exchange or collection, checks, and drafts"; and after the word "draft," "payable upon presentation," because you certainly do not mean that it shall receive time drafts.

Senator HITCHCOCK. Sight drafts?

Mr. FLANNAGAN. The reason I would not use the word "sight" is that in some States "sight" gives three days' grace, and in some States demand gives grace. So if you have "payable on presentation" it gets rid of both. In Massachusetts, for instance, I think, the sight draft has three days' grace.

In the sixteenth line, from the word "or" to the word "depositor" in the seventeenth line, can be erased, because the same idea has been conveyed above. That is, you would erase the words beginning at "or," in the sixteenth line, then reading as the text reads until the last two words in the nineteenth line are reached, which may be erased.

In the twentieth line, after the word "contained," insert the word "is." After the word "patrons" in the twenty-third line, I would suggest: I regard this provision of this bill requiring Federal reserve banks to receive from other banks checks and drafts payable elsewhere at par, of the greatest importance, because it makes the deposits in all the banks at par with other deposits which can be circulated by means of checks which would then be received at par; but you do not want that privilege to be abused; and I therefore think that if you would put in some clause so that if individuals deposit checks for the purpose of procuring credit, or what is termed "kiting," they shall not have that privilege. Consequently, I propose the insertion, after the word "patrons" in the twenty-third line, the following. Under misdemeanors you will also have it covered, if you wish to make it a crime to do any regular kiting, which we will come to later, but this insertion reads as follows:

> Any person, firm, or corporation having had its check or draft returned under protest through a Federal reserve bank for nonpayment shall not thereafter be entitled to the benefits of clearing through the reserve bank, and the said reserve bank, at its discretion, may refuse from a member bank as a deposit the check or draft of such person, firm, or corporation.

The effect of that would be that protested items would be regarded with some concern, and they would not often come back through the Federal reserve banks; that they would be settled at the member banks where they came from or were presented.

In pursuance of that idea of having a parity of exchange throughout the country you will observe that on the next page, page 34, the Federal reserve board may exercise the functions of a clearing house. I believe that there is no machinery connected with this bill at all whereby a Federal reserve board could act as a clearing house, and it would be necessary to change the whole proposition if they did; that is to say, they do not keep money, and they do not keep books of account, and they do not have deposits with anybody. Nor do clearing houses have the latter. The board is not in the position to exercise the functions, and consequently I think you ought to insert, after the word "discretion" on the first line of that page, where it says "designate one Federal reserve bank to exercise the functions of a clearing house," and change the word "such" into "all Federal reserve banks," and then erase "or may designate a Federal reserve bank to exercise such function.'

Of course as it reads, you can designate a Federal reserve bank to exercise such functions, but you reserve the right of the Federal reserve board, and it seems to me it is useless, because they can not do it. The thought is that each Federal reserve bank may act as the clearing house for all of the banks in its district, and that one Federal reserve bank may be designated to act as the clearing house for the other Federal reserve banks.

On page 35, line 17, it would be necessary to insert, after the word "outstanding" the following words, "which are secured by a deposit of United States bonds," if you adopt the suggested amendment for allowing individual banks to issue circulating notes against a deposit of discounted notes and gold. In line 20, after the word "and" and the word "notes," you should insert the word "such," referring to the notes then outstanding.

We have already discussed the provision of gold-secured notes, which is added at the end of that section after the word "obligations" in the eighth line on the thirty-sixth page.

Under "Bank examinations," page 40, line 23, it is provided that the Comptroller of Currency shall so arrange the duties of national-bank examiners that no two successive examinations of any association shall be made by the same examiner. I suppose the purpose of that was to prevent any collusion between the bank examiner and the banks; but that is amply provided for under the head of misdemeanors, and it seems to me that it is unwise to deprive the comptroller of the benefit of the knowledge that one bank examiner may have by examining a bank, to be used for his benefit, for a subsequent examination. I think those words should be erased.

Senator SHAFROTH. But that does not prevent the Comptroller of the Currency the time after that to order it to be done and thereby take advantage of his experience.

Mr. FLANNAGAN. They do not examine them, ordinarily, more than twice a year. The Comptroller of the Currency can send another examiner, without taking that authority away from him. That is, you would not allow him to send the same examiner there twice. He could not to it, and why is it desirable to prevent that?

Senator SHAFROTH. In order to prevent collusion between the examiner and the bank. Of course it is not likely to occur, but we have some banks that carry assets that are not very good assets.

Mr. FLANNAGAN. But I do not think that it has ever occurred that there was any collusion between the examiners and the banks.

Senator SHAFROTH. Still, there is another provision in here against an examiner receiving any presents.

Mr. FLANNAGAN. I was going to say that I think that is covered under misdemeanors, but of course that is just a mere suggestion.

You will observe that there is a great quantity of increased examinations on page 41, line 15:

> That the Federal reserve board is required to have at least four examinations a year

In the preceding paragraph the Federal reserve bank can have any number of examinations it wants, and those are in addition to the examinations made by the comptroller. Consequently, if all of these examinations were made, you would have a useless expense, and have the banks continually being examined much more than necessary. My thought is that you might utilize the examinations made by the comptroller as a part of that minimum amount of four times, if they decided to do it, by adding after the word "cities" in the seventeenth line the words:

> but the examinations under the direction of the Comptroller of the Currency may be included in the minimum number herein required.

In section 24 there should be a heading of "Misdemeanors." There is no heading. In the eighteenth line of page 42, if you will read it carefully in regard to that paragraph beginning "no officer or director," you will find, it seems to me, that it is capable of the interpretation that an officer or director could not draw his salary or receive any benefit from the bank that employed him.

I wish Senator Hitchcock would read that carefully and see if that is not so.

Senator HITCHCOCK. It seems to me that the prohibition is just against receiving a fee or a commission or other consideration for or on account of any loan, purchase, sale, payment, exchange, or transaction with respect to stocks, bonds, or other investments.

Mr. FLANNAGAN. Yes.

Senator HITCHCOCK. It is not against receiving compensation for services to the bank.

Mr. FLANNAGAN. Ought not that to be made clear? Because it says any transactions of the bank. If you made a discount, that would be a transaction.

Senator HITCHCOCK. For any particular thing that the bank may extend to its customers.

Mr. FLANNAGAN. Would it not be better—I am just throwing this out as a suggestion—but would it not be plainer in the eighteenth line, after the word "beneficiary," if you would put in "any person, firm, or corporation other than said bank," and then let it read "either directly or indirectly."

Then we come to the question of kiting. As stated before, if we prohibit the clearing of people who have protested checks, and then in addition make it a misdemeanor for people who procure money by that means, I think you will have removed any danger of that sort.

Senator SHAFROTH. Before you leave that, let me get your interpretation of this: From the language you have inserted, after the word "beneficiary", "from any person, firm, or corporation other than the said bank," would it not relieve any officer or director of the bank from any of the prohibitions that are contained in that section?

Mr. FLANNAGAN. Would it?

Senator SHAFROTH. Would it not be an exception, and therefore they could take a fee or a gift?

Mr. FLANNAGAN. But he could not take it if it was from any firm, person, or corporation other than the bank.

Senator SHAFROTH. No, that is true; but he could take it from the bank.

Mr. FLANNAGAN. But the bank does not pay commissions for that business. What you are trying to do is to keep people from bribing bank officials.

Senator SHAFROTH. You also want to keep the bank officer, by reason of his power as a director, from doing things or receiving a commission or gift or something of that kind, in consideration for his getting the bank to do it. For instance, it is a thing that often happens. I go into a bank and I say, "I want some money." He will say, "I can not give it to you, but I can lend you it personally, and if you give me 4 per cent for the privilege I will get the money for you and pass it to your credit in the bank." That, no doubt, is intended to prevent just such a thing as that. It is not very often done, but it has occurred. I have had it occur to myself.

Mr. FLANNAGAN. I am perfectly in accord with what I consider the purpose of that section, that a bank officer should not receive any compensation of any description for the functions exercised by the bank, except his salary.

Senator SHAFROTH. Would not this exception of yours eliminate him from that punishment?

Mr. FLANNAGAN. My thought is that it would not, but I may be mistaken. You had better ask somebody who is a better lawyer than I am. I just throw it out as a suggestion.

Page 43, after the word "jurisdiction" in line 5, I think if you will insert this it will prohibit any chance for "kiting," and be a protection to all of the banks:

> Any person, with the intent to obtain credit on the books of a member bank, or the money and funds of said bank, who shall deposit or cause to be deposited in such bank any check or draft, knowing the said check or draft not to have been drawn against existing credits or to be fictitious in its nature or in its inception, shall be guilty of larceny; and any officer of a member bank who shall sign any check or draft on another member bank and deposit or cause the same to be deposited in any Federal reserve bank, knowing such check or draft not to be drawn against existing credits, or to be fictitious in its nature or its inception, shall be guilty of a misdemeanor, and shall be punished by fine or imprisonment in the discretion of the court having jurisdiction.

You might prescribe the penalty if you approve of the idea.

Senator SHAFROTH. I think that is a good suggestion.

Mr. FLANNAGAN. Before section 25 I think the heading ought to be inserted: "Stockholders' liability." I think that the idea carried out in that section is that anybody who transfers the stock of a national bank shall be liable for 60 days under the provisions of the national-bank act, which provides a double liability, and it seems to me that the prohibition in many cases would work a great hardship, and that it would have a tendency to deter people from owning national-bank stock; that the purpose to be attained is the punishment of wrongful intent, and that either on the part of the transferer, and especially on the part of the officers of the bank who would naturally be supposed to have knowledge of its failing condition. I would therefore suggest that you insert in the eighteenth line, after the word "obligations"—

with the intent to avoid any liability or presumably with the knowledge of the bank's insolvency.

On page 46, line 9, I think there is an error; that the word "upon," next to the last word in the line, ought to be changed to "under."

On page 47 the eleventh line reads:

shall be authorized to accumulate and loan the funds of its depositors.

In point of fact, no depositor has ever any funds in a bank. That is a great mistake. They have only got the debts of the bank, and the bank never loans the funds of the depositors; it loans its own funds. So I think that ought to have inserted in it the word "to" after the word "and" and before the word "loan," and the last word in the line, "of," erased, and substitute "received from." So it would read:

to accumulate and to loan the funds received from its depositors.

On the forty-eighth page, the fifth and sixth lines, the last word in the fifth line and the first word in the sixth line, I think ought to be erased, because the question of keeping separate books for individuals will hardly apply to the bank itself. I think it ought to be for its exclusive use, meaning the bank.

The CHAIRMAN. What is your suggestion on lines 5 and 6—that the word "individual" shall be stricken out?

Mr. FLANNAGAN. It is immaterial; it does not mean anything.

In the seventeenth line on the same page, after the word "country," I think it is the intention that the list therein referred to should be uniform for the district, and I think it would be well to add after the word "country," "and uniform for each Federal reserve district."

On the forty-ninth page, seventh line, the word "wilful" is wrongly spelled.

On the eleventh line of the same page the word "felony" is used. The lawyers on your committee would probably decide that it ought to be a "misdemeanor" instead of a felony; but that is for their consideration.

On the same page, if you are going to allow national banks to have branches in one municipality, in which they are located, as I previously stated, the word "foreign" of the heading should be erased, and in the seventeenth line, after the word "capital" the word "stock" should be inserted, and after the word "more" the following:

may with the approval of the Comptroller of the Currency establish one or more branches within the corporate limits of the municipality in which it is located, not exceeding two such branches for each million dollars of capital stock, and—

Those are all the suggestions I have to make.

The CHAIRMAN. We are very much obliged to you, sir.

Senator HITCHCOCK. To what extent, under the terms of that bill, would you think the Federal board of control would have the power to expand or contract the credits of the country?

Mr. FLANNAGAN. None whatever, because the initiative must come from the Federal reserve banks. You asked me their power, did you not?

Senator HITCHCOCK. Yes. Suppose the Federal reserve banks apply for currency: The Federal reserve board has the power to state at what rate of interest that currency shall be furnished. Is not that true?

Mr. FLANNAGAN. I think that is true; but my thought was, Senator, that that matter of interest was really a question of taxation. It must be very, very low.

Senator HITCHCOCK. Let me see about that. Suppose, now, the Federal reserve board establishes a rate of interest of 5 per cent. The banks would not get very much of it, would they?

Mr. FLANNAGAN. No, they would not want it.

Senator HITCHCOCK. Suppose, now, it goes to the other limits of the bill and establishes a rate of interest of one-half of 1 per cent?

Mr. FLANNAGAN. There is a limit mentioned in the bill——

Senator HITCHCOCK. Of one-half of 1 per cent.

Mr. FLANNAGAN. Is it that?

Senator HITCHCOCK. The reserve bank under that rate of interest would undoubtedly take out a great deal of currency.

Mr. FLANNAGAN. Would they, necessarily?

Senator HITCHCOCK. What is your experience as a banker? When a man can get currency at one-half per cent, will he get more than he would if he had to pay 5 per cent?

Mr. FLANNAGAN. Yes; but you must take into consideration that this currency is the debt of the reserve bank which would be turned over to the Federal reserve banks for issuance in that form when they need it; and if they could borrow that currency at one-half per cent they would probably ask for a great deal of it, if that was all it cost them.

Senator HITCHCOCK. So that the Federal reserve board has the power to expand credits of the country?

Mr. FLANNAGAN. You mean through regulation of the rate of interest, or the issue of reserve notes?

Senator HITCHCOCK. Yes.

Mr. FLANNAGAN. Yes; I suppose that is true.

Senator HITCHCOCK. That is the only system that the Bank of England uses; and even by a small change of one-half of 1 per cent it makes a tremendous difference in the volume of business.

Mr. FLANNAGAN. There is no question about that.

Senator HITCHCOCK. Then give a board the absolute extreme power to fix the rate of interest to reserve banks anywhere over one-half of 1 per cent, up to 5 or 6 per cent, and you would still say that the Federal reserve board had not the power to expand or contract credits?

Mr. FLANNAGAN. Well, perhaps in that view of the case I was wrong.

Senator HITCHCOCK. Suppose a case in which an administration is in power, and the President has appointed seven members of this body. They are his creatures. The President is up for reelection, and the question before the American people is whether the country is prosperous or not. With the Federal reserve board appointed by the President, and having the power to expand or contract credits, do you think that the Federal reserve board would have considerable effect to give an appearance of prosperity?

Mr. FLANNAGAN. The Federal reserve board have not the initiative; they can not go and issue this paper currency unless a bank applies for it. Nor can the reserve bank issue it unless a member bank applies for it.

Senator HITCHCOCK. Very true. But suppose, now, banks are always using money, or, always making loans—the national banks of the country have something like 8,000 millions of loans outstanding now, and there is a strong demand for money more or less all the time, or for credit. Suppose the Federal reserve board, in its desire to have the wheels of business turning actively, and having money cheap, fixes a rate of one-half of 1 per cent? Suppose it reduced the rate to 3 or 4 per cent before that?

Mr. FLANNAGAN. They do not regulate the rate; the Federal reserve bank regulates the rate of discount.

Senator HITCHCOCK. But the Federal reserve board regulates the rate——

Mr. FLANNAGAN. They have got supervision over it.

Senator HITCHCOCK. No; the Federal reserve board regulates the rate which the Federal reserve banks pay for currency.

Mr. FLANNAGAN. They have not the initiative.

Senator HITCHCOCK. No; I did not say they had; but the Federal reserve board has the power to regulate the rates which the Federal reserve bank pays for the 200 or 300 millions of dollars which they secure in currency, or the 700 millions, or the 1,000 millions, for there is no limit. Suppose they put it down at one-half of 1 per cent, which is almost nothing. Is it your opinion that they would give a tremendous boom to business, and might very largely influence the political organization?

Mr. FLANNAGAN. Yes; but, Senator, you have got in your mind that the Federal reserve board, for political purposes, would say: "We will fix this tax low," and then the Federal reserve banks would unite with the Federal reserve board for the purpose of advancing some particular political party, and taking out this money. That seems to be a rather strong presumption.

Senator HITCHCOCK. Let us see about this: John Smith wants to borrow money of his bank in a certain time. He applies to the bank for money——

Mr. FLANNAGAN. And that is a member bank.

Senator HITCHCOCK. To a member bank, yes; and the member bank, if it has funds with the central reserve bank, will discount notes at a very low margin, and then it can make a handsome profit by loaning to John Smith or 1,000 John Smiths, and then it will apply to the Federal reserve bank, and it will secure a discount at a low rate of interest because the Federal reserve bank has currency available at one-half of 1 per cent. Suppose the Federal reserve bank was compelled to pay 3 per cent for this currency. It would say to the member bank, "You have to pay a larger discount for John Smith's note;" and the member bank would say to John Smith, "We can not loan you money at less than 8 per cent;" and John Smith would say, "I won't use it." Is not that the direct effect of it? Is not the power to control the rate of interest the power to expand credit and the power to promote business?

Mr. FLANNAGAN. But, my dear friend, does not the Bank of England have the power to control the rate of interest? Is it not by that very means that they regulate their reserves.

Senator HITCHCOCK. Is the Bank of England interested in any particular political party?

Mr. FLANNAGAN. I think not.

Senator HITCHCOCK. Suppose a case in which the creatures of a particular President have the power to control the rate of interest?

Mr. FLANNAGAN. Well, but they can only control it through a Federal—you say the Federal reserve board. Now, that Federal reserve board can only control it through the initiative of 12 Federal reserve banks. Those Federal reserve banks are composed of banks throughout the country united together for the purpose, and that Federal reserve bank can not get out this currency unless it is applied for by the member banks. Consequently, you have got to suppose a combination and everybody being of the same mind and of the same political view in order to get this out for political purposes.

Senator HITCHCOCK. I hardly think so. I think the initiative is with John Smith who wants to borrow the money. He is willing to pay——

Mr. FLANNAGAN (interrupting). If you will just get that out of your mind. It is not.

Senator HITCHCOCK. Well, suppose it is credit. We will not quibble on terms. But he wants to borrow—the ordinary term is money—at 5 per cent. If he can get it at 5 per cent he will get it. He can get it if the bank can rediscount paper at a low rate of interest with the reserve bank. The reserve bank will take the rediscount at one-half of 1 per cent where it might not take it at 3 per cent, and the result is that you have thousands of John Smiths at these banks all over the country, borrowing money because it is cheap.

Mr. FLANNAGAN. Have you not lost sight of the fact that 33⅓ per cent gold reserve has got to be kept?

Senator HITCHCOCK. Not at all. It is a smaller reserve than any of the banks of Europe have.

Mr. FLANNAGAN. I would like to make that 50 per cent.

Senator HITCHCOCK. That is not enough of a hinderance, in my opinion.

Mr. FLANNAGAN. I would like to get away at 5 o'clock, Mr. Chairman. I should like to add that the member bank must pay the discount rate of the reserve bank before it gets a credit on the books of the reserve bank, and that this discount rate is not fixed by the Federal reserve board. The interest or tax which is fixed by the reserve board is only on the circulation the Federal reserve bank may receive—it is a tax on this form of debt and is paid by the bank. It is a tax on the change in form of debt from the deposit created by the discount into the circulating note which the member bank may want. It should not be confused with the discount rate or rate of interest paid by the member bank and charged by the Federal reserve bank.

Senator HITCHCOCK. I am through.

Mr. FLANNAGAN. I wanted to catch a train, please, sir.

The CHAIRMAN. Have you any questions, Senator Shafroth?

Senator SHAFROTH. No, no; I wanted to ask you a question, but I think it is too late now.

(The following statement was filed with the committee:)

SUMMARY OF STATEMENT SENT TO GLASS COMMITTEE.

By IRVING FISHER.

The principal points at which the present banking system of the United States seems to me to need reform are as follows:

(*a*) It needs elasticity of note issue.

(*b*) It needs a change in the requirement as to reserve which will permit the use of reserve when most needed.

(*c*) It needs the gradual substitution of banking on acceptances and for commercial paper for banking on collateral security.

(*d*) It needs interconnection of loan markets for rediscount.

In addition to these reforms (all of which are closely related, of course) and some others of less importance concerning our banking system proper, there should, it seems to me, be also the following reforms, also closely related:

(*a*) All forms of money should be made expressly redeemable in gold, including silver dollars and greenbacks.

(*b*) Our Treasury should be more easily able to deposit its funds instead of retaining them as a useless and variable and so dangerous hoard.

As to (*a*) elasticity: At present the note issue of our banks is limited by the Government debt, and, therefore, not only is rigidly fixed as its upper limit, but, so far as fluctuation is at all possible, the tendency is for the fluctuation to be the opposite of what the requirements of trade demand. It seems necessary, therefore, that a more elastic basis should be supplied, either instead of the bond basis or better, in addition thereto. The natural basis would be bank assets consisting of loans of a commercial nature based on actual transactions and consisting in acceptances or commercial paper. These would vary with the requirements of trade and would therefore tend to become the basis for currency in exact fluctuation with the requirements of trade.

As to (*b*) reserve: There are various ways of rendering reserves available. At present, when our reserve reaches the legal lower limit, which is just the time when it is most needed, the requirements of our banking law are virtually that it shall not be used at all, and while this law is administered with leniency it results in an aggravation of the very stringency for meeting which the reserve is needed. It also puts a premium on the accumulation by country banks of useless reserve withdrawn from their deposit in New York and a consequent general paralysis of trade from insufficient currency media at exactly the time when such media are most needed. One method of overcoming these difficulties is that supplied in the Aldrich bill by which a bank can deposit its reserve with the central institution, securing its deposit by rediscounting commercial paper.

Another and I think a better method is to frankly revise the laws relating to reserve, make no limit to the percentage which the reserves bear to deposits, but apply a graduated penalty when the reserves are below a specified limit.

As to (*c*) commercial paper: At present some 20 or 30 per cent of bank loans are call loans on collateral security, a form which should be discouraged since its existence tends to aggravate speculation and the evils of speculation and since there is no vital relation between the volume of such loans and the volume of business. When currency does not vary with the volume of business the necessary result must be convulsions in prices. The Aldrich bill makes under ordinary circumstances rediscount possible only for loans based on actual commercial transactions. I believe this is a good provision and ought to be made even more definite and with perhaps less exceptions than provided for in the Aldrich bill.

As to (*d*) rediscounting: A central banking institution of almost any conceivable type would act as a clearing house or reservoir for connecting the loan markets of the country and our loan markets with foreign loan markets. The Canadian system of branch banking would accomplish the same result, although not so perfectly. One objection which I have to the Aldrich plan by which the present requirements as to reserves are left unchanged and the bank is allowed to count as reserve some deposit credit on the books of the central institution, is that it perpetuates and, in fact, aggravates the present indirect and complicated system by which banks and bankers are encouraged to count as cash that which is not cash. I believe the evils of this theory permeate the thoughts of many business men, especially bankers. In banking, if anywhere, just because confusions are so easy, we should be careful to call a spade a spade, and to make a careful distinction between cash and a claim on cash. The added simplicity and directness obtained by frankly acknowledging that in the last analysis the only reserve is cash and getting away from the fictional reserve with which we now delude ourselves would itself be a safeguard against unsound methods.

Now as to the two last reforms I mentioned which are not, strictly speaking, banking reforms. I have long felt that the National Monetary Commission did not live up to what it should have done and what it was appointed to do when it entirely omitted the subject of currency reform except as it related to banking. We have two very soft spots in our currency left from the time of the Civil War and the resultant effort which followed it. These soft spots are the greenbacks and the silver dollar, neither of which is at present properly speaking redeemable in gold, our ultimate standard. The greenback is explicitly redeemable but its redeemability is coupled with the requirement that it must be reissued. It would be a great step forward if merely the word "may" could be substituted for "must." When a redeemed note must be reissued it can scarcely be said to be truly redeemed in the strict sense of that term, and this reissue requirement has consequently made trouble for us, as for instance, in the Cleveland administration, when gold was being drained from our Treasury because of the "endless chain" by which the same greenbacks could be used over and over again for withdrawing gold from the currency and without any relief from redundancy by the cancellation of the greenback. Of course the redundancy was caused by silver, not by the greenbacks themselves; but had the greenbacks been not only redeemable but retirable, the endless chain would have ceased. We may never have such a situation again, but there is no certainly that we shall not, and in fact the very existence of the anomalous situation in which the greenback is now placed, contains a suggestion of menace for the future. It is an invitation to fiat money proposals and inflationism. Moreover, I believe it contributes to the general feeling abroad that we do not have a simple and definitive gold standard, a feeling which injures our national credit abroad.

As to the silver dollar, this is likewise an anomaly due to historical conditions. I emphatically dissent from the view that the Democrats can not afford to take up this subject. Everyone knows that we have no longer bimetallism and that silver is not coordinate with gold, and I think the Democratic Party would really gain and not lose if it would now take the bull by the horns and frankly make silver redeemable in gold, instead of leaving the present ambiguous proviso which merely directs the Secretary of the Treasury to keep gold and silver at par. Of course unless some further inflation is legislated silver will stay at par without any specific redemption proviso. But the present situation creates the same kind of menace and foreign distrust, as above referred to, regarding gold. I would go further and make silver certificates into Treasury certificates, redeemable in gold directly, and gradually release all the silver now constituting the silver dollars left in our Treasury so that they could be used as needed for coining subsidiary silver. It would probably be inexpedient, at present at least, to suggest the sale of this silver although this is the businesslike procedure and has a precedent in the action of Germany many years ago. It would not be necessary to make silver dollars subsidiary coins. They could still be unlimited legal tender so far as they would really be used.

Inasmuch as the reform of our currency is distinct from banking reform it would of course be advisable that any legislation as to greenbacks, silver dollars, and silver certificates should be separate from the legislation affecting banking. But I believe these currency reforms are almost as important and in a way more fundamental than the banking reform, if we are to build a permanent structure to endure in the future.

As to Government hoarding: This of course would be obviated if a central reserve institution were created. But it could also be obviated by making suitable laws requiring or encouraging the deposits of practically all the Government's funds among national banks. This situation is not as bad as it formerly was and the problem is perhaps gradually solving itself.

If a central bank is to be created, it seems to me that it ought to deal only with other banks and not to be a rival to them, for it was this rivalry which was largely, at any rate, instrumental in causing the discontinuance of the central banks previously tried in the United States.

While I would like to see a central bank permanently established in the United States, I think there is one danger in connection with its establishment, a danger which has very generally been overlooked. This is that the establishment of a completely equipped central bank might give such a tremendous impulse to the true deposit banking as to tend to greatly inflate that currency, well called deposit currency, as well as very likely to inflate the currency in the form of bank notes. In this respect I agree with the criticism which Prof. Scott and Mr. Garrison, of Madison, Wis., have made on the Aldrich plan, and also with the criticism made by ex-Congressman Fowler, who states that the establishment of the Aldrich plan would result in driving a great deal of our gold abroad. This, in my opinion, would not be the least of the evils of a sudden inflation of our bank notes and deposit currency. The really great evil would exist in a rapid rise in prices and adding to our already excessive high cost of living.

In my opinion, one reason why American prices have risen more rapidly than the prices in European countries is the great increase in deposit banking in the United States since 1900. However excellent in itself any plan may be for giving banking facilities, one should never lose sight of the indirect effect of the system on the general level of prices. The idea that deposit currency can influence prices is not altogether familiar to those who have had to do with the problem of banking and banking legislation. Nevertheless, I agree that few propositions are more firmly established than this. I take the liberty of referring you to my own book on The Purchasing Power of Money and to the writings of others referred to therein. Ninety-three per cent of our business is now done by the check drawn on deposit subject to check. If we should suddenly eliminate all these deposits subject to check and be compelled to do all our trade on a cash basis, one can easily imagine what a tremendous contraction would result. Prices would fall disastrously. Reversely, if a country like France, which now makes little use of deposit banking, should suddenly adopt the habit and thereby equip itself with the means for effecting exchanges to the extent of four or five times its present facilities, the result would be an enormous rise in prices (partly spread over other countries, of course, through the expulsion of gold). At present the deposits subject to check in the United States are about four and a half times the actual money in circulation, and the total individual deposits are about 10 times the cash in banks. These ratios would be greatly increased if we should suddenly take off the restrictions on our banking reserve. While I firmly believe that these restrictions are injurious and should be removed, I think their sudden and complete removal would be disastrous. Mr. Farwell, I understand, has the same thought. Experience seems to show that where there is no restriction the ratio of reserves to deposits seldom tends to be much more than 5 per cent; in other words, that the deposit liabilities are likely to be some 20 times the cash in bank or twice the ratio now obtaining in the United States. Such an expansion would nearly double the available circulating media in the United States. A sudden increase of even 50 per cent would be disastrous. These possibilities ought not, of course, to stand in the way of creating a rational banking system, but they ought to cause the framers of the legislation to safeguard the introduction of the new system from letting out too much rope at a time.

While the important matter in this connection is to prevent an undue or sudden inflation of bank deposits, the same principle applies to the inflation of money in the strict sense. This is an additional reason why the introduction of a provision for more bank notes should be accompanied by the retirement of other bank notes and by the provision for a possible retirement of the greenbacks and silver certificates if rendered redundant. When Secretary McCullough in the sixties tried to redeem the greenbacks, the contraction of the currency was felt to be unfortunate, and it was at that time, as prices were falling. It was doubtless largely because of the feeling of protest against falling prices that the proviso was made in the law of 1878 preventing further contraction of the greenback. But to-day we have the opposite situation, and therefore the golden opportunity to do what McCullough could not do in the sixties without injury to the public.

I scarcely see how it would be in the public interest to maintain the present bond-secured currency, or at any rate to avoid reducing its amount. It is a necessity to get an elastic currency, and this elasticity must be secured from some other form of currency than bond-secured currency. If the present bond-secured currency is kept in circulation, then, in order to have any real elasticity in the currency as a whole, it is evident that we should need to have a very large addition to the currency in the form of new asset currency notes. Mere $50,000,000 or $100,000,000 of elastic currency added to our present system would produce very little elasticity, as it would form too small a proportion of the whole, a large mass of which, the major part, is inelastic and rigid, would not be really elastic. In other words, if we retain our present bond-secured currency we should need in order to secure elasticity to produce inflation. But to my mind inflation would be as great an evil as inelasticity. It follows, therefore, that in order to secure elasticity, and at the same time to avoid inflation, we must retire the present bank notes secured by bonds, or else entirely retire the greenback and the silver certificate, both of which are also now inelastic elements in our system.

I think our bonds should be paid as fast as they mature. One of the evils of the present system is that the Government must keep in debt in order to keep bank notes in circulation. It is true that our bonds in market value will show a very considerable shrinkage if they are no longer available as the basis for bank note currency, but the truth is that they now have an artificial value. We do not boast that our bank notes are well secured because they are based on bonds of high value, for-getting that the high value of these bonds is itself due to the fact that they are used to secure the notes. Of course, in fairness to the banks whose funds are now invested in these artificially high-priced bonds there should be some privilege or advantage accruing from the new system, whether this substitution of a new advantage for the old one lost is accomplished in the manner provided for in the Aldrich bill or in some other way.

Among the provisions of the Aldrich bill which do not appeal to me is that requiring a uniform rate of interest throughout the country. It seems to me too artificial and also of doubtful value. In this respect Mr. Farwell's plan, as in other respects, seems to me superior.

The Aldrich plan also, it seems to me, gives insufficient power to the President of the United States and to our Government generally, and also insufficient to others than bankers in the management of the bank. The Government should have power to modify the charter within proper limits. Since the Dartmouth College case, a charter has come to be regarded as an inviolable contract rather than a license. Therefore the only way to safeguard against inflexibility in the charter is to make due reservation at the outset. It will be difficult to forecast exactly how any plan will work, and the Government, which is making the plan, should reserve the right to change it in advance. The provisions in the Aldrich plan for electing the various grades of officers and electors seem to be extremely complicated. Complicated machinery of this kind generally ends in manipulation by the few who thoroughly understand it and, even when it does not do so, it is likely to create the suspicions of such manipulation in the popular mind.

I have recently been interested in a plan proposed in 1906 by Mr. Barron, now proprietor of the Wall Street Journal, and Mr. Sereno S. Pratt. This plan was aimed merely to avoid crises by providing temporary elasticity under a penalty. It resembles in principle the plan used in Germany and in some respects the plan in England of suspending the bank act at the time of an impending crisis. I attach a copy, with Mr. Barron's permission, in the thought that you may be interested.

I take this opportunity to state my conviction that the problem of banking and currency will never be satisfactorily solved nor the evils of rising and falling prices with the alternation of crises and depressions reduced to a minimum until we have gone a step further than merely regulating the operation of bankers. We can not stop short of regulating the unit of value itself. Every other unit in commerce has been standardized, but the dollar is still a mere unit of weight, although it is used in contracts extending over generations as a unit of value of purchasing power. Whether my particular plan for standardizing the dollar or some other be employed, I believe with Sir David Barbour (who was largely responsible for introducing the currency reform into India 20 years ago), that sooner or later the business world will be forced in self-defense to get a stable yardstick of purchasing power. This, however, is a matter for international action, and I have no deisre to do more than to call the attention of your committee to its importance. The President is, I think, convinced of this.

[Written Dec. 28, 1912.]

WASHINGTON, D. C., *December 14, 1906.*

The PRESIDENT,
White House, Washington, D. C.

DEAR MR. PRESIDENT: We beg leave to report that we presented to Secretary Shaw the bill we propose for strengthening the gold reserves of the Government to balance an emergency elastic currency and find the Secretary in perfect accord with our views as to dangers threatening the future, but thoroughly grounded in the belief that nothing can be done at this session of Congress, and that nothing can be done at any session of Congress, without previous strong popular agitation possibly reenforced by disastrous financial reasons.

We beg to differ from this view and to place at your service the measure inclosed and the following reasons in support of its consideration by you.

First. This plan, being for the purpose of strengthening the head of the Executive in time of grave national peril, should be drafted and proposed by the Executive, just as he would plan any measure for national defense in time to threatened war, pestilence, or famine.

Second. There is no difference of opinion as to the existence of the peril. The whole financial world feels it. The difference is over the remedy. On the one hand there are those who say there is no cure except the destruction of prosperity, the impoverishment of labor, and the return of labor's wages to the reserve centers. On the other hand is the proposal for increased bank paper currency. Nobody, however, has publicly proposed the strengthening of the gold reserves in the hands of the Executive, which should precede either remedy—panic or paper. To work the cure by destroying prosperity is suicidal. More bank paper may be temporary relief, but this would force gold out of the country whenever the rates of interest were relatively higher abroad. It should, therefore, be preceded by some plan for freeing the gold reserves in the Treasury and placing them under the control of the President and the Secretary of the Treasury.

Third. The present law, authorizing bonds to issue for gold purchases, may not be available for quick action when there is an international contest, as at present, over interest rates and gold reserves.

Fourth. The present acute international situation has existed but a short time. Until recently it was supposed that gold currency would move freely and continuously between gold standard nations and that high interest rates, especially when combined with the largest merchandise exports ever recorded, could at all times draw gold from England and Europe. Our large exports, our Treasury policy of facilitating gold imports, and our high interest rates have but served to alarm Europe in a manner and to a degree unprecedented. England is no longer able to bank the world on a gold basis, and she can not now look to France, Germany, or Russia for support. Her units in financial transactions have become outclassed by America's growth. With our immigration reaching one million a year and all our people at work, we are absorbing the life labor of the world and its life-giving currency, gold. For that gold we have been iss ing for some years only gold coin or gold certificates dollar for dollar.

Fifth. The United States Treasury has, therefore, to-day the only stock of gold capable of holding in balance the paper currency and the emergency currency which the world's activities demand. The failure to properly use it means ultimately a financial and industrial crisis and may mean sudden demands for its improper use. Freed and safeguarded, nearly 1,000 millions of dollars of gold in the United States Treasury may in the future become the financial wheel of the world, protecting industry and labor from the peril of panic, and going far toward making in the United States the monetary standard and center of the world.

Sixth. Emergency measures must be in few words and must be built upon what exists and lies close at hand. What lies closer at hand than the enormous stock of gold in the Treasury—a hoard such as no other nation possesses? Why waste this power when danger threatens? Why not make it the sure metallic basis of an unconquerable, emergency, and elastic circulation?

Seventh. We have engaged in the drawing of this plan the legal services of a firm of lawyers familiar with the national banking and currency laws, and we have given to it the results of our own study and practical experience of 25 years in the financial field as news gatherers and close observers of the financial conditions, being absolutely unattached to any interest, but serving all. We would be glad to assist you in any way in the preparation of such a plan, but have no selfish ends to serve, and we should prefer to keep strictly in the background, leaving the whole matter to your initiative, because upon you and you alone must fall the burden of maintaining the prosperity of the United States.

Yours, respectfully,

Sereno S. Pratt, *New York.*
Clarence W. Barron, *Boston.*

[Inclosure.]

AN ACT To provide a larger central gold money reserve

Section 1. The Secretary of the Treasury is hereby authorized to issue at any time United States notes in excess of the amount now permitted by law in exchange for gold or gold certificates.

Sec. 2. The Secretary of the Treasury may, upon the request of the clearing house association of the national banks of any reserve city, issue United States notes in excess of the amount now permitted by law for the purpose of serving as an emergency currency. United States notes so issued shall be deposited by the Secretary of the Treasury at his discretion in such national banks and in such amounts as the clearing house association may request. Such deposits shall constitute a first lien upon the bank's assets subject to the priority of its national-bank notes and shall bear interest for any portion of the first $200,000,000 at the rate of 7.3 per cent per annum and 1 per cent additional for each successive $100,000,000 or portion thereof.

The issue of United States notes as emergency currency shall cease when the gold reserve in the United States Treasury for the redemption of United States notes and Treasury notes is reduced to 40 per cent of the total amount of such notes outstanding.

SEC. 3. Whenever the gold reserve in the Treasury of the United States for the redemption of United States notes and Treasury notes exceeds 60 per cent of the total amount of such notes outstanding, the Secretary of the Treasury, with the approval of the President, may issue United States notes in excess of the number now permitted by law for the purpose of redeeming the bonds or other indebtedness of the United States or in lieu of the issue of bonds for public works authorized by act of Congress. The issue of such notes shall cease when the gold reserve falls below 60 per cent of the total amount of Treasury notes and United States notes outstanding.

(Thereupon, at 5 o'clock p. m., the committee adjourned until Monday, September 22, 1913, at 10 o'clock a. m.)

MONDAY, SEPTEMBER 22, 1913.

COMMITTEE ON BANKING AND CURRENCY,
UNITED STATES SENATE,
Washington, D. C.

The committee assembled at 10.25 o'clock a. m.

Present: Senators Owen (chairman), Hitchcock, O'Gorman, Reed, Pomerene, Shafroth, Nelson, Bristow, McLean, and Weeks.

The CHAIRMAN. We have arranged to hear Mr. Samuel Untermyer, of New York, this morning. Mr. Untermyer, we will be glad to hear from you this morning.

STATEMENT OF SAMUEL UNTERMYER, OF NEW YORK CITY.

Mr. UNTERMYER. Mr. Chairman, I have been asked to present such suggestions as may occur to me with respect to this bill, and in presenting them I should like to have it clearly understood that I am an unqualified champion of the fundamental principle involved in this bill; that is, an ample currency issued directly by the Government, as a Government obligation, and under the absolute control of the Government. I take it that those are the fundamental provisions of the bill.

It seems to me that the bill is overgenerous to the banks, both in freeing them from competition and in other respects; more generous than any known system of any civilized country. That we have been overgenerous in the recognition that is now given to the banks, regardless of the advisory council, and that in so far as it frees them and protects them from competition it seems to be unadvisedly overliberal, and that it is so overliberal that it is likely to destroy the ability of the reserve banks or of the Government to regulate the discount markets of the country.

Now, if you do not mind, I will take up in order the provisions of the bill which I desire to discuss.

Senator HITCHCOCK. What is that statement you made? It was so liberal that it might destroy the ability of the Government to regulate the discount markets.

Mr. UNTERMYER. Yes; because it seems to me that the discount markets should be regulated, as they are in other countries, largely by the purchase of bills and acceptances in the open market; whereas this bill provides only for the purchase of bills—that is, domestic bills through the banks. In other words, we can not do as they do in Germany and France; go into the market and buy bills and in that way regulate the discount rate of the banks.

Senator HITCHCOCK. Well, the Government does not regulate the discount market in Europe.

Mr. UNTERMYER. It does in a way. The Bank of England, for instance, does every week state what the discount rate is; but it is after all a mere statement of what the discount rate will be. It would be of very little avail if the Bank of England were confined, as under this bill the reserve banks are confined, to discounting or buying only from a bank. The Bank of Germany, the Bank of France, and the Bank of England buy in the open market; they compete with the banks, and when they fix the discount rate they have the means of enforcing that rate in the public markets by buying paper at that rate and competing with other banks.

Senator HITCHCOCK. That has not always been so of the Bank of France?

Mr. UNTERMYER. That is so of the Bank of France; it buys in the open market; it buys through 400 or 500 subagents scattered all through the country; every agent buys paper there. They buy paper in small amounts; they deal directly with the smallest tradesmen of the country. And the same thing is done in Germany.

Senator HITCHCOCK. But, of course, that is a very small percentage of their business?

Mr. UNTERMYER. No; on the contrary, in France, the statistics show that it is 55 per cent of their business.

Senator SHAFROTH. Mr. Untermyer, right there, is not the Bank of England—instead of buying paper, does it not sell paper?

Mr. UNTERMYER. No; it does both.

Senator SHAFROTH. It does both?

Mr. UNTERMYER. Yes.

Senator SHAFROTH. But, in order to raise the rate, they do not buy paper, do they?

Mr. UNTERMYER. Well, that would raise the rate. Naturally, if they make a market for paper by buying it that would raise the rate.

Senator SHAFROTH. But, when they buy the paper, that puts out that much more currency, and consequently makes competition sharper, which would lower the rates upon the other banks?

Mr. UNTERMYER. Yes; when the other banks do not want to take any paper, the Bank of England, by going into the market and taking paper, in a sense, raises the rate by creating a market for paper, when otherwise there would be no market.

Senator HITCHCOCK. But does not that reduce the rate when they go and buy the paper?

Mr. UNTERMYER. It would not necessarily do so. The more market you create for a product the more customers you get for a given article the better the rate is likely to be sustained than if there was no business.

Senator HITCHCOCK. If the Bank of England goes into the market and buys paper, that makes it easier for those who are selling the paper——

Mr. UNTERMYER. I mean by increasing the market it does reduce the rate.

Senator HITCHCOCK. It does reduce the rate, and when they want to raise the market they go and sell bonds, they sell consuls.

Mr. UNTERMYER. Not necessarily.

Senator HITCHCOCK. That is what I understand.

Mr. UNTERMYER. If they keep out of the market they raise the rate; or, if they want to keep up the rate, they say, "We will charge so much discount for paper," and everyone knows that he can not secure money for a less rate; and that has the effect of raising the rate. There are two general classes of middle men who deal in paper in London. There are recognized discount houses, great corporations like the Midland County and City of London Bank, of which Sir Edward Holden is at the head, and the Discount Bank of London, of which Mr. Nugent is the head. They have very large capital and they buy this class of paper themselves, knowing that they can rediscount it any time they want to, and that they can make money by the difference between the open rate in the markets and the bank rate.

Then there is another class of men who control the great banking houses of England. They are, some of them, discount houses, and some of them acceptance houses. A merchant who is not well known or whose acceptances are not salable on his own credit, goes to one of these banking houses and says, "I want a line of credit for my mercantile transactions of £100,000." The banking house being satisfied with the responsibility of the man, will, for a commission, accept bills that he draws on them, and those acceptances pass current and are rediscounted by the Bank of England and, in like manner, by the banks of France and Germany.

It is that system of discount and acceptances that makes it possible for England to do so much of its business on a credit basis, and require so little actual money.

Senator HITCHCOCK. Now, Mr. Untermyer, do the banks of deposit in England, like the Midland County and City of London Bank, which receive deposits from the public, give acceptances?

Mr. UNTERMYER. Yes; some of them are acceptance houses also.

Senator HITCHCOCK. But I understand that in the main——

Mr. UNTERMYER (interposing). In the main, the private bankers do a large part of the acceptance business.

Senator HITCHCOCK. Well, this bill provides that these banks, which are banks of deposit here in the United States, shall give acceptances to the extent of 50 per cent of their capital?

Mr. UNTERMYER. Yes; but only for foreign business.

Senator HITCHCOCK. Yes; I believe there is a limitation in the bill.

Mr. UNTERMYER. Yes; a limitation which is absolutely wrong and unjust to our domestic merchants, because it makes money cheaper to the foreigner than to the home merchant. If all the banks can lend their credit for foreign business, but not for home transactions, this country is made a great market for credit on foreign transactions, and excluded as a market on domestic transactions.

It seems to me that the manifest and the surest result of that policy is to aid the foreign merchant in competing with our home merchant. If the foreigner can get money cheaper than the home merchant in the form of acceptances, he is given an advantage.

Senator HITCHCOCK. It would only be the larger banks in the foreign business that would lend credit.

Mr. UNTERMYER. Not in that way. Under this bill, any national bank can lend its credit in the form of acceptances for transactions based on the importation or exportation of goods, to the extent of 50 per cent of its capital.

Senator HITCHCOCK. If it was for the exportation of goods, there would be no need for doing so. It is only for the importation.

Mr. UNTERMYER. I said based on the exportation of goods. That means that if a merchant in this country is selling to a merchant in Germany, the merchant in Germany is the one who must give the paper.

Senator HITCHCOCK. Yes.

Mr. UNTERMYER. And he can hire a New York bank to give acceptances.

Senator REED. Senator Hitchcock's question interested me, and I think it would be quite a question as to whether this, in its practical working in this country, would give to the large bankers this particular line of business and the small banker be excluded, not under the terms of the bill, but under its practical operation.

Mr. UNTERMYER. I think in its present form it would, if you are going to limit the acceptances to those based on the importation or exportation of goods. The amount of acceptances that a bank may make is unlimited in some of the other countries. The Canadian banking system has no limit in the amount of its discounting operations.

Senator HITCHCOCK. Is it not true that it is considered bad banking for a bank of deposit to give acceptances, because it has so many demand liabilities in the shape of deposits that it is considered bad banking for it to give acceptances which may come in at any time, virtually indorsing notes for others.

Mr. UNTERMYER. That has not been the result of experience in other countries, so far as I know. One would suppose that there might be some criticism made of the banks in that respect; but that apparently adjusts itself. Those who buy these acceptances get such an intimate knowledge of the extent to which a bank will lend its credit that acceptances are not given to an extent that will affect the bank's credit. That thing has always adjusted itself.

So, with the foreign banking houses. Anyone familiar with the business of the country can sit down and write out the names of the banking houses whose acceptances pass current, because it is known that they are conservative in their business dealings. The people who buy these bills are so expert that they can tell a good commercial bill from an irregular bill almost instinctively. It is amazing to see how they can pick out of their portfolio, their mass of acceptances, and tell you all about each one of them.

Senator WEEKS. Let me ask you one question, Mr. Untermyer, at this point: Are you going to advocate that the reserve banks go into the market and purchase bills and conduct a business in competition with other banks?

Mr. UNTERMYER. I do not think that would be quite fair to the banks, except where it is necessary to regulate the discount rate, if the banks are going to come into and become an integral part of this system. But if the banks are not going to come into this system, you can build up, it seems to me, quite as good a system and perhaps a stronger one in competition with the banks.

Senator WEEKS. Is that not exactly what destroyed the First and Second United States Banks?

Mr. UNTERMYER. Well, that is a long story, is it not?

Senator WEEKS. Yes.

Mr. UNTERMYER. And there are varying points of view as to what did destroy them.

Senator WEEKS. It was my recollection that that was the fundamental reason—that and politics.

Mr. UNTERMYER. Yes.

Senator WEEKS. Those were the two fundamentals that destroyed the First and Second United States Banks, and I was wondering if you were going to advocate repeating that experience.

Mr. UNTERMYER. Every other country in the civilized world which has a banking system and a central bank does buy these bills in that way.

Senator WEEKS. Yes; in both ways, that is true.

Mr. UNTERMYER. They buy mainly in the open market in competition with the banks; and not alone that, but they take deposits in competition with the banks. The Reichsbank has 70,000 deposit accounts. The Bank of France, with all its vast deposits, has only a small number of banks as depositors.

Senator WEEKS. Yes.

Mr. UNTERMYER. It does its main business directly with the business and farming community in general; almost everybody in business has a deposit in these Government banks. What we are doing here by this bill is to protect these banks against competition. We are allowing them to make an intermediate profit on every piece of business they do with the Government; and we are confining ourselves to doing business through them. My contention is that that is a very generous arrangement. Judged by the experience of other countries, it is so generous that one is disposed to marvel at the objections that the banks suggest to this bill.

Senator WEEKS. It really is not a question of generosity that we have to deal with; it is a question of public policy and of what will bring about the best results for the business interests of the country—and I did not intend to disturb your argument——

Mr. UNTERMYER. Yes.

Senator WEEKS. But I wondered if you were going to discuss that point.

Mr. UNTERMYER. Yes.

Senator WEEKS. And if you were going to take that position.

Mr. UNTERMYER. I am, and I would like to say it does not in the least interfere with my discussion to be interrupted. I think the colloquial form of discussion is the only useful form, and I shall be glad to be interrupted at any time and as often as you please by questions from members of the committee.

Senator HITCHCOCK. Mr. Untermyer, you speak of this being liberal to the banks because it does not raise up a competitor against them. But as a matter of fact the banks are to own absolutely these 12 regional banks, which is an entirely different proposition from anything existing anywhere in Europe.

Mr. UNTERMYER. Entirely different.

Senator HITCHCOCK. So that we are really creating a monopoly, as I understand it, in this country. We are binding our whole banking system into one and allowing the banks to combine what is kept separate in Europe?

Mr. UNTERMYER. I think you are dissipating a monopoly by this measure. I think you have something now which is very nearly approaching a monopoly of great credit, and that you are doing the most effective thing that can be conceived of to get rid of it.

Senator HITCHCOCK. Would not the situation that we are proposing to create be parallel to the situation which would exist if the banks of France owned the Bank of France, instead of having the ownership diffused among a large number of stockholders?

Mr. UNTERMYER. I do not think it would make any difference if the small banks of France owned the Bank of France so long as the Government controlled the bank as it does now by the naming of its governors and its vice governors and agents.

Senator HITCHCOCK. The Government does not name its directors. They are named by the stockholders.

Mr. UNTERMYER. But the Government names the governor, the head of the bank, and it names the assistant governor.

Senator HITCHCOCK. But it does not name the directors, and the directors name the rate of interest.

Mr. UNTERMYER. And there is not a banker on the board of directors.

Senator HITCHCOCK. As I understand it, the governors run the bank, but the directors fix the rate of interest.

Mr. UNTERMYER. My understanding (and I had a long talk with the governor of the Bank of France this summer on the subject, and also with the head of the Credit Lyonnaise) is that in practical effect that the Government runs that bank just as the Government runs the Reichsbank. It is a very flimsy cover, this private stock ownership, because the private stock owners have little or no real voice in the detail business management of the bank. In the first place, owners of large blocks of stock have no voice in the management at all commensurate with their interest. A man who owns over 500 shares of stock has no vote on his excess holdings, as I remember the situation at the moment. A stockholder has one vote up to 50 shares that he owns and two votes up to 100 or 200 shares, and he gets an aggregate of four votes on an ownership of 500 shares, and after that he gets no votes no matter how much stock he owns.

And then when you look at the personnel of the board of directors, we will say, of the Bank of France or of the Bank of England, you will see that they do thoroughly represent the commercial community in the best and most useful sense and that their presence on the board is of great value because of their knowledge of persons and conditions in their locality and their consequent ability to pass on paper.

Senator HITCHCOCK. You do not hold that the Bank of England is controlled by the Government in any sense, do you?

Mr. UNTERMYER. Which department—the issue department?

Senator HITCHCOCK. Either one. It is not even inspected.

Mr. UNTERMYER. Oh, I know it is not.

Senator HITCHCOCK. There is no reserve required.

Mr. UNTERMYER. But it is very subservient to Government influence.

Senator WEEKS. Well, are not all banks everywhere subservient to Government influence?

Mr. UNTERMYER. No; I would not like to say that they are. Only in so far as the Government has the power to inspect them and to control their operations. I think that if the banks of this country, the great banks, were more susceptible to Government influence and to public sentiment it would be better for them and for all of us.

Senator WEEKS. Well, we are not discussing the public sentiment phase of it. It has always seemed to me that banks everywhere were extremely anxious to cooperate with the Government.

Senator POMERENE. If the newspapers correctly reported the proceedings of the American Bankers Association it was only a few weeks ago that they wanted to have the right to veto anything that the board might do.

The CHAIRMAN. It would be more accurate to say, in some cases, that they are extremely anxious to have the Government cooperate with them.

Senator SHAFROTH. The name of the Government is a great thing to have back of them in their banking business in any way.

Senator WEEKS. That is true. But I think if you look into the inside workings of the banks generally in the United States in the last 50 years you will find that the banks have been anxious to cooperate with the Government whenever there was necessity for cooperation.

Mr. UNTERMYER. I think that in times of emergency they have shown public spirit, as you will find public spirit in any other class of the community. I think as a class they are just as patriotic and public spirited—no more and no less so—as any other part of the community.

Senator WEEKS. That is just my opinion exactly.

The CHAIRMAN. I think everybody agrees with that.

Senator REED. Well, taking that view of it, and admitting that most American citizens are willing to go out and shoulder a gun and go to war and die for their country, have you not observed a disposition of gentlemen dealing with the Government to always want to "skin" the Government? The same patriot who takes his gun and goes to war will reach his hand into the Treasury as deeply as he can and escape at the same time the penalties of the law?

Mr. UNTERMYER. That is what I meant when I said that they were just as patriotic and no more and no less than the general run of citizens.

Senator REED. I do not mean to say that the bankers do that any more than any other people. But when you come to financial transactions most gentlemen, whether they are in the banking business, or are farmers, or working men, like to get about all they can out of the Government; and I have never seen any class of citizens yet actual guardians ad litem for the Government in dealing with it. They generally want to get a good contract if they can get it.

Senator HITCHCOCK. Do you think, Mr. Untermyer, that the Government should control the rate of discount?

Mr. UNTERMYER. Do you mean this Federal board?

Senator HITCHCOCK. You made the statement in your opening remarks that the terms of this bill tend to limit the ability of the Government to regulate the discount market of the country. So I ask you whether you think the Government should control the rate of discount?

Mr. UNTERMYER. In a qualified way, in connection with the issue of currency, yes. That is to say, that when the Government is issuing currency for the relief of the community to carry on the business of the country, I think it is only just that it should see to it that people who are getting the benefit of that relief are not required to pay exorbitant rates to the banks who act as mere middlemen between the Government and the borrowers.

Senator HITCHCOCK. That is the only motive then—to protect the borrowers?

Mr. UNTERMYER. To protect the borrowers in connection with the relief you are furnishing the borrowers. It is hardly just for the Government to say, on the one hand, to the national banks, "We will help you relieve the financial stringency," and, on the other hand, permit them to exact just as much as they please from the borrower in granting that relief with Government funds.

Senator HITCHCOCK. Yes. Now, I want to suppose a case to you and see whether you think this would be desirable. Under the terms of this bill the board of control has the right to fix the rate of interest at which currency shall be advanced to the reserve banks.

Mr. UNTERMYER. Yes.

Senator HITCHCOCK. Suppose an administration was drawing to its close. Seven men, chosen by the President, compose the board of control. They are the creatures of the President. He is a candidate for reelection. The question before the people is whether the administration has brought prosperity to the country. Do you think there would be any danger that those seven men might make such easy money for the country as to start the wheels of industry and create a boom by advancing currency to the reserve banks at one-half of 1 per cent, so that they might, in turn, let it out liberally to the individual banks, and the individual banks having a redundant currency would let it out liberally to their customers on loans that might not ordinarily be desired, and the country would have a period of inflation of credit?

Mr. UNTERMYER. My answer to that would be that one can, of course, with the aid of a vivid imagination, conceive almost any given state of things, but that I do not believe it is within the range of possibility.

I am not in sympathy with this talk about political boards. I believe that we should get as able, useful, and public-spirited a body of governors for this Federal reserve board as could be selected from the ranks of any country, or as could be selected by the bankers themselves—and perhaps a better board than could be selected by the bankers. I have no fear of the political control aspect.

Senator HITCHCOCK. Well, do you think——

The CHAIRMAN (interposing). You have not let him finish his answer, Senator Hitchcock.

Mr. UNTERMYER. Yes, if I may go on. I think, Senator Hitchcock, that the brakes that are put upon the issue of currency here are sufficient to keep it within bounds. In the first place, the Federal reserve bank can not disburse any more currency than that which will keep up its gold ratio, to start with——

Senator HITCHCOCK (interposing). Well, that is very small.

Mr. UNTERMYER. That is as much as necessary.

Senator HITCHCOCK. No; it is smaller than any country in Europe.

Mr. UNTERMYER. That is a question of the way you figure it.

Senator HITCHCOCK. Can you name a single bank of Europe that keeps as low a reserve as 33⅓ per cent? That is under——

The CHAIRMAN. There is Belgium.

Mr. UNTERMYER. If we carry out the recommendations of the bill which Senator Owen has introduced with respect to the gold certificates that are outstanding, it will be very much easier for us to get as large a gold reserve as is required. Thirty-three and one-third per cent has always been regarded as safe. I do not think——

Senator HITCHCOCK. The Bank of England has 50 per cent. The Bank of France has 85 per cent. Germany has about 60 per cent—between 50 and 60 per cent.

Mr. UNTERMYER. It has 60 per cent now, but it did not have it six months ago.

Senator SHAFROTH. There is no limitation upon it. They could run it down lower if they wanted to. They can run it up to 50 or 60 per cent.

Mr. UNTERMYER. They have had it as low as 20 per cent in Germany and their currency and credit have not suffered in consequence. I discussed that question very fully with one of the chiefs of the Reichsbank a few weeks ago. It is a question of confidence in the ability of the country to redeem its promise to pay in gold rather than a question of the precise proportion actually in hand.

Senator HITCHCOCK. Can you recall my original question now?

The CHAIRMAN. You have not permitted him to answer you question.

Senator HITCHCOCK. No. I will get you to indicate whether, with your vivid oriental imagination, you can conceive of a condition such as I have suggested relating to the board of control producing, in a sense, a condition of prosperity?

Mr. UNTERMYER. Yes; by assuming at the outset that these men upon the board of control are going to be recreant to their trust and are going to deliberately bring on a cataclysm in the affairs of the country.

Senator HITCHCOCK. No; I am not picturing a cataclysm at all. I am picturing a condition of prosperity.

Mr. UNTERMYER. No; that is not a condition of prosperity.

Senator HITCHCOCK. Well, I will say of activity.

Mr. UNTERMYER. You are assuming that they will let out money for practically nothing except for the purpose of unduly stimulating enterprise and creating an unhealthy inflation and an undue credit in the business world. I think you have presented a set of premises that are almost inconceivable.

Senator HITCHCOCK. Well, it is possible under the law for them to let out currency for one-half of 1 per cent, which is practically a nominal rate.

Mr. UNTERMYER. Yes; it is possible.

Senator HITCHCOCK. And it is possible, on the other hand, for them to charge 5 per cent.

Mr. UNTERMYER. But that always assumes that they are going to act contrary to the needs of the country and contrary to sound business and to their consciences.

Senator HITCHCOCK. But suppose they think that the needs of the country are the reelection of the President who appointed them?

Mr. UNTERMYER. That belief would not be consistent with their sworn duty under the bill. The needs which will govern them in their action under the bill are the financial needs of the country—and the law under which they are acting; and I can not conceive that they will lose sight of that fact. No other assumption is permissible.

Senator POMERENE. It would be just as fair to assume that the Supreme Court of the United States would be recreant to its trust as to propose that the members of this Federal reserve board would.

Senator HITCHCOCK. Well, is it not a fact that nearly every Cabinet officer, when the time comes for the President to be reelected, goes out to assist in his reelection?

Mr. UNTERMYER. It is perfectly consistent for them to defend their policies, and the country is entitled to have them do so, and is benefited by such a custom. It is a pity they are not given seats in Congress and required to answer every day for their official acts; but if, instead of going out, they should sit in their private chambers and deliberately violate their official oaths, that would be an analogous case to the one you are assuming.

Senator HITCHCOCK. I am not assuming the case——

Mr. UNTERMYER (interposing). Oh, but those are your premises.

Senator HITCHCOCK. The law gives them the right to let out currency at as low a rate as one-half of 1 per cent.

Mr. UNTERMYER. But the law assumes that they are going to exercise a judicial discretion.

Senator HITCHCOCK. And you do not conceive that it will be possible for them to let out currency as low as one-half of 1 per cent legitimately?

Mr. UNTERMYER. No.

Senator HITCHCOCK. I think it is entirely too cheap. But the bill provides for it.

Mr. UNTERMYER. Yes. But when money is as cheap as that it is not needed. There is a surplus of it.

Senator HITCHCOCK. You would not say that that is an objection to the bill?

Mr. UNTERMYER. I should say that the rate is too low.

Senator HITCHCOCK. I should think so.

Senator BRISTOW. Mr. Untermyer, you made one suggestion that interested me. You said that if the banks will not come in under the bill, why we would do so-and-so with these banks. What do you mean by that?

Mr. UNTERMYER. I mean, in the first place, that the attractions of this bill to the banks are so great that it does not seem conceivable that they can stay out, either national banks or State banks; and, secondly, that if, for the purpose of getting better terms, they should decline to come in, there is a system which seems to me quite as sound, quite as feasible, and perhaps as much in the public interest as the one outlined in this bill, if not more so. Now, I believe the banks will come in. I do not believe any State bank or national bank can live outside of this system with all its attractions.

In the first place, the 10 per cent which the country bank pays in, and about which there has been so much protest, it can get back——

Senator BRISTOW (interposing). It borrows it back. Why should a country bank be compelled to put in 20 per cent instead of 10 per cent of its money, and then borrow it back as a favor?

Mr. UNTERMYER. Let us see if it is a favor. I think it is a money-making arrangement for the bank. It buys this stock, in the reserve bank, and then if there is an equitable arrangement of rediscounts, it gets it back in the form of a loan; and certainly it will not have to pay 5 or 6 per cent; while it will be getting 5 or 6 per cent on the stock it subscribes for. Suppose it pays 2 or 3 per cent to borrow back the money; it is making the difference between that 2 or 3 per cent and the 5 per cent dividend which it is getting as a dividend on its stock. So, I think there is a good deal of humbug about this talk of the hardship on country banks under the bill.

Senator BRISTOW. Then, do you think that these country banks do not know what they are talking about?

Mr. UNTERMYER. I did not say that.

Senator BRISTOW. But you seem to think there is a good deal of humbug on their part?

Mr. UNTERMYER. I have not quite been able to believe, when they look at all the attractiveness to them under the bill, that the outcry is made by the country bankers.

The CHAIRMAN. The outcry of the country banks comes from the gentlemen who hold the country bank deposits.

Senator BRISTOW. I challenge that statement as being a fact. It comes from the men who do not want to dissipate the resources of the community and send them to a foreign city, and then have to borrow it back as a matter of favor. Do you think that these country bankers are a lot of chumps that are willing to be managed by men in New York and Chicago?

The CHAIRMAN. I think the argument as to the hardship on country banks comes mainly from the banks which have these country banks' deposits.

Senator BRISTOW. I think there is a doubt about that, and it is not true in any sense——

The CHAIRMAN (interposing). I think some of the country banks have put up the argument——

Mr. UNTERMYER. Let us look at the figures. It has seemed to me, from the point of view of the logic of the situation, as though it were very strange that the country bankers should object to this feature: First, because, as I say, they get their distributive part of the money back by way of loan, and they make money by the operation. Second, it is preeminently to their interests to strengthen their reserve bank as much as they can and with a 10 per cent subscription to the stock, it will cost them nothing, and they can make something. A 5 per cent subscription makes a comparatively weak bank. The next privilege the country banker gets is with regard to the use of its reserves——

Senator WEEKS (interposing). Would a 5 per cent subscription make a weak bank, if the number of banks were reduced?

Mr. UNTERMYER. I am assuming, Senator Weeks, that the subscription will not stand in the way of any bank going into this system. That is, that they will recognize that they will get back that money by borrowing it back and making money from the operation.

Aside from that, you take the reserves now that they are required to put into a city reserve bank, or a central reserve bank. They would get back the use of two-thirds of those reserves of which they do not now get the use. But, under this arrangement, they are going to get back two-thirds of those reserves, and they are going to be able to use their capital and their deposits and resources over and over again.

A bank should, if properly conducted, be as well off as if it had twice the capital it has under the present system.

On the question of where it is possible that the opposition to this measure may originate. There are 10 banks in New York——

The CHAIRMAN (interposing). In New York City?

Mr. UNTERMYER. In New York City all practically under the domination of one little set of men that have 15,483 deposits of the out-of-town banks of the country. They have 60 per cent of all the deposits of all State and National banks of the country. Here is a list of them, with the number of bank depositors.

The CHAIRMAN. Will you give that to the stenographer, so that it may go into the record?

Mr. UNTERMYER. Yes. The Bankers' Trust Co. has 237 of these out-of-town bank depositors. It is governed under a voting trust, of which Messrs. Morgan and Baker, or their firms, constitute the voting trustees. They control the election of directors of that bank through a voting trust. The National Bank of Commerce has 1,671 bank depositors. That is largely controlled by the Morgan and Baker people.

(The list referred to follows:)

Out-of-town bank depositors.

Bankers Trust Co	237
National Bank of Commerce	1,671
Chase National Bank	3,103
First National Bank	579
Guaranty Trust Co	182
Hanover National Bank	4,074
Liberty National Bank	312
Mechanics & Metals National Bank	1,010
National City Bank	1,889
National Park Bank	2,426
Total	15,483

Senator WEEKS. The Bank of Commerce?

Mr. UNTERMYER. The National Bank of Commerce in New York.

Senator WEEKS. How much stock do J. P. Morgan & Co. own in that bank?

Mr. UNTERMYER. I think I can give you the exact amount from the report of the Pujo committee.

Senator WEEKS. The capital is $25,000,000, is it not?

Mr. UNTERMYER. Yes. You know they bought in very largely lately, within a few years.

Senator WEEKS. I do not know anything about it.

Mr. UNTERMYER. When the Mutual Life and the Equitable Life sold their Bank of Commerce stock, they sold one-half of their holdings in that bank, and that was bought by a group that was gotten together by these gentlemen. You may remember that in 1906 the Legislature of New York passed a new insurance law requiring the insurance companies to dispose of their bank and other stocks; and under that arrangement they disposed of half of the stock they held in the Bank of Commerce. Those two companies had practically controlled that bank.

Senator WEEKS. How much stock do Morgan & Co. control in the Bank of Commerce?

Mr. UNTERMYER. I will have to look that up for you; it is quite considerable.

Senator WEEKS. You stated that Messrs. Morgan and Baker controlled the $25,000,000?

Mr. UNTERMYER. If you will let me look at that during recess, I will give you the exact figures. I did not say they owned the control.

Senator WEEKS. You said they controlled it.

Mr. UNTERMYER. I said they controlled it, and I will show you that by the list of their board of directors.

Senator WEEKS. You mean that they control the policy of the bank, but do not control the stock?

Mr. UNTERMYER. I do not mean that they own one-half of $25,000,000 of that stock any more than I mean that the men who control a railroad to-day own a majority of the capital stock of that railroad. They control a railroad by the ownership of 2 or 3 per cent of the stock sometimes.

Senator WEEKS. They control it because the stockholders wish them to control it.

Mr. UNTERMYER. But the control of the capital of the Bank of Commerce, as evidenced by the constitution of its board of directors and in many other ways, is under these gentlemen. That subject has been fully exploited, and I do not care to inject it here.

Senator WEEKS. That is to say, the stockholders think that these gentlemen are fit people to manage the bank?

Mr. UNTERMYER. Well, I do not think that is quite a fair way of putting it, Senator Weeks.

Senator WEEKS. I think that is absolutely fair, Mr. Untermyer.

Mr. UNTERMYER. I do not think so. I think that when we know how impossible it has been in the history of this country to change the control of any corporation because of the inertia of stockholders. I do not think it is fair to say that a bank or a railroad is controlled by a few men because most of the people of the country—most of the stockholders—think that they are the best people to control it. I do not think that is true of the New Haven road to-day; but you have heard of no movement to take the control of the New Haven road away from the men who now control it.

Senator WEEKS. But the inertia of the stockholders simply means that the stockholders are satisfied.

Mr. UNTERMYER. No; it means that there is no known way by which the stockholders can assert themselves as they do in other countries. They simply do not do it.

Senator WEEKS. You know that that is not so.

Mr. UNTERMYER. I know that the stockholders do not assert themselves in this country. They submit to all sorts of abuses and mismanagement and often worse, rather than get together and make a change in the control.

Senator WEEKS. They do when they are satisfied.

Mr. UNTERMYER. Then you must not forget this: What may be good for the stockholders of a bank is not always good for the public that is dealing with the bank. For instance, it may be a very good thing for the stockholders of the Bank of Commerce that these gentlemen control that bank. It is a good thing for them. They make a great deal of money through the control by these gentlemen that they could not otherwise make, because these interests control the accounts and other patronage of railroads and great industrial companies; and their ability to throw business to these banks and to make them great is in itself a sufficient incentive to stockholders to leave the control with them.

Senator WEEKS. Then we will admit that the stockholders of the Bank of Commerce are satisfied with Morgan & Co., and Mr. Baker and others controlling the bank because they make the bank successful.

Mr. UNTERMYER. Yes; I think they——

Senator WEEKS (interposing). Then, as far as the stockholder is concerned, they control the bank because the stockholders want them to do so.

Mr. UNTEMYER. It is not material to our present discussion and so if you care to have such an admission for the purpose of discussion, we will assume it for that purpose.

Senator WEEKS. I do not want any admission. I simply want to get at the facts.

Mr. UNTERMYER. We none of us know the facts as to what are the wishes of the stockholders.

Senator SHAFROTH. Mr. Untermyer, before you leave the question as to the amount which is to be kept in its vault by the country bank, I have made a little calculation, and I want you to tell me whether I am wrong or right. Let us suppose a country bank with $100,000 capital?

Mr. UNTERMYER. Yes.

Senator SHAFROTH. And that it has $1,000,000 of deposits?

Mr. UNTERMYER. Yes.

Senator SHAFROTH. And under the present law it has got to keep 6 per cent of that in its own vault?

Mr. UNTERMYER. Yes.

Senator SHAFROTH. And 9 per cent in other banks?

Mr. UNTERMYER. Yes.

Senator SHAFROTH. Now, this bill changes the amount of the reserves that are required from 15 to 12 per cent?

Mr. UNTERMYER. Yes.

Senator SHAFROTH. And requires it to keep in its vault 5 per cent, and in other banks 5 per cent, with a leeway as to the remaining 2 per cent. Now, on one $100,000, the 10 per cent that would have to be paid to the capital of the reserve bank under this bill would be $10,000, and the 5 per cent which it would deposit with the reserve bank would be 5 per cent of $1,000,000, which would be $50,000, or which added together makes $60,000. That is the amount which the country bank with a capital of $100,000 and $1,000,000 of deposits has to put up and part with?

Mr. UNTERMYER. Yes.

Senator SHAFROTH. And it must part now with 9 per cent of $1,000,000 which would be $90,000. Is not the country banker better off by $30,000 under this now policy than under the law as it exists to-day?

Mr. UNTERMYER. I think he is better off by a great deal more than that difference because——

Senator SHAFROTH (interposing). Well, is he not better off at least to that extent?

Mr. UNTERMYER. Certainly.

Senator SHAFROTH. Now, then, what other advantages would he have under the bill?

Mr. UNTERMYER. If he is equitably dealt with and he is dealing in commercial paper, he can borrow back the $10,000 of capital that he invests——

Senator SHAFROTH. Yes.

Mr. UNTERMYER. In the stock, because there is no reserve required of the reserve bank except as against its demand liabilities. Then, if he is fairly dealt with, he ought also to be able to borrow back two-thirds of the $50,000. That is $33,000, and the $10,000 makes $43,000, in addition to the advantages of which you speak.

Senator SHAFROTH. Now, does not the reduction of the amount required to be placed in the reserve banks as part of the reserves of these various banks, whether city banks or country banks, inure to their advantage to the extent of probably 5 per cent on their deposits?

Mr. UNTERMYER. I have not figured that.

Senator SHAFROTH. Well, you take a city bank——

Mr. UNTERMYER. Yes.

Senator SHAFROTH. It is required now to keep in cash in its own vaults 25 per cent?

Mr. UNTERMYER. Yes.

Senator WEEKS. That is a central reserve city?

Mr. UNTERMYER. Yes; a central reserve city.

Senator SHAFROTH. A central reserve city. Now, that 25 per cent in its own vault is locked up so that it can not use it. Now it is required to put in—it reduces it to 18 per cent.

Mr. UNTERMYER. Yes.

Senator SHAFROTH. And 9 per cent in its own vaults, and 9 per cent in the central reserve, or the reserve banks. That difference between 25 and 18 per cent, calculated on its enormous deposits, will make a greater difference than the difference of requiring the full 25 per cent to be kept in its vaults?

Mr. UNTERMYER. Certainly; I have always argued that the purpose should be to reduce the reserves, as far as it was safe to do so.

Senator SHAFROTH. And that inures to the financial benefit of the banks?

Mr. UNTERMYER. It appears so.

Senator BRISTOW. So far as the country bank is concerned—I am not considering this from the standpoint of the central reserve city bank—the reduction from 6 to 5 per cent is of no consequence whatever to the country banks, because they have to carry more than 6 per cent anyhow in their business, and they always do carry more than 6 per cent, unless they are in a failing condition.

Senator SHAFROTH. The point I am referring to is the amount they have to put in other banks being reduced from 9 to 5 per cent.

Senator BRISTOW. They will carry more than 5 per cent anyway, because it is necessary for them to do it. And as to the reduction in the amount required to be carried in their own vaults, that is not of advantage to them, because they have to carry more anyhow and always do carry more.

Senator SHAFROTH. Well, why are they protesting, then, and trying to get the reserves to be deposited in the country banks still lower?

The country banks are trying to do that now. If it is of no benefit to them to have it lower, why should they do that?

Senator BRISTOW. I do not know what protests are being made. But you know you can examine any country bank in your State; and it carries more money than it is legally compelled to carry. It has to, in its business.

Senator SHAFROTH. It is carried very largely because it can not go to one of these central reserve banks and discount its paper and cash practically every obligation that it has outstanding, under the present law.

Mr. UNTERMYER. That is the reason they do not carry any reserves in the European banks, because of these central reservoirs. They know they can get all the money they want.

Senator BRISTOW. I am not objecting to these central reservoirs, if you put it in the control of the banks themselves. You started out to say that 10 men have control over I do not know how many banks.

Mr. UNTERMYER. 15,483.

Senator BRISTOW. Well, 15,483 banks——

Mr. UNTERMYER. I did not say 10 men control these banks. I say that those 15,483 banks are depositors with those 10 institutions.

Senator BRISTOW. But it has been asserted by the chairman and yourself that these influences that center in New York are controlling these country banks and causing them to protest here to us against this legislation?

Mr. UNTERMYER. If anything I said conveyed the impression that I believed that, because these 15,483 country banks had deposits in the New York banks, the New York banks controlled those country banks, I want to disabuse your mind of it, because that would be perfectly absurd.

The CHAIRMAN. I said nothing that justified that conclusion.

Senator BRISTOW. I certainly so understood the chairman. I think the record will show that the chairman said that this protest came from this central source.

The CHAIRMAN. Let the record speak for itself.

Senator WEEKS. What the chairman intimated, and what Mr. Untermyer more remotely intimated, and what you read every day in the press, is that there are certain great money devils who are controlling this suggestion, and that they are influencing the country banks to protest against this bill in the hope of getting better terms.

Mr. UNTERMYER. Now, on that subject, if I may be permitted, I will say this: What I meant to say is that these New York City banks, 30 of which have 19,015 of these banks' deposits, that it is not to their interest to lose these deposits if they can keep them. Under the present system they have those depositors and they want to keep as much of this money as possible.

Senator HITCHCOCK. How many country depositors, 19,000?

Mr UNTERMYER. There are 30 banks in New York City, out of 111 banks and trust companies there, which together have the deposits of 19,015 banks throughout the country. Now, of those 30 banks, 10 banks which I have referred to, and which I am about to name and which will go into the record, have 15,483 of those deposits.

Senator WEEKS. You know that those deposits are not an unmixed blessing, do you not?

Mr. UNTERMYER. They seem to be pretty lucrative business. The banks do not seem anxious to let them go. Let me show you, in that connection, how much of that money is used in Wall Street.

Senator HITCHCOCK. Before you pass to that will you not allow me to bring up the question of the country banker from the standpoint of the country bank? I have got a letter here which I received from a country banker yesterday, which is right in point, I think, and I will lead up to that by one or two questions. Mr. Untermyer, you say there are 30 banks in New York City having deposits from 19,015 banks throughout the country?

Mr. UNTERMYER. Yes; there may be a few hundred duplications in that where a bank has a number of bank correspondents.

Senator HITCHCOCK. Every one of those 19,000 country banks in selecting the New York depository has the choice of at least 30 banks?

Mr. UNTERMYER. Yes.

Senator HITCHCOCK. Suppose this bill passed, how much of a choice would those country banks have?

Mr. UNTERMYER. The money does not go back to the banks then; it goes to the reserve bank.

Senator HITCHCOCK. They would be required to put it in the reserves of New York City, would they not?

Mr. UNTERMYER. But they would get two-thirds back instead of none.

Senator HITCHCOCK. I am asking you where they will be required to put it? They would be required to put it there. Suppose that reserve bank refuses to rediscount their paper?

Mr. UNTERMYER. Yes.

Senator HITCHCOCK. Where would the country bank be?

Mr. UNTERMYER. Do you mean, unjustly refused?

Senator HITCHCOCK. Suppose it refused, regardless of any reason, what would the country bank do?

Mr. UNTERMYER. Do you mean as to borrowing?

Senator HITCHCOCK. Yes.

Mr. UNTERMYER. I do not know. I suppose it would do what it would do now if its correspondent in New York refused to discount.

Senator HITCHCOCK. Now, if the National Bank of Commerce refused to discount the paper of the country bank, it can go to the First National Bank, or any other national bank that is a reserve agent in New York City, where it may keep its reserves?

Mr. UNTERMYER. In theory it might do so, but in practice I do not think—if one of the New York banks refused, I do not think you would find any other bank would take up the business.

Senator HITCHCOCK. I think the fact is that the country banks are changing their accounts all the time, shifting accounts. And, moreover, if it failed to get its credit and proper treatment from the reserve agent in New York City, it might take the reserve agent in Philadelphia, or St. Louis, or Boston, or Chicago, or Omaha, or St. Paul.

Mr. UNTERMYER. Yes; but, Senator Hitchcock, these banks will all have accounts with other banks anyway to do their regular business.

Senator HITCHCOCK. Then, under the terms of the bill, they are not permitted to do so after three years?

Mr. UNTERMYER. Yes; they are, except as to their reserves. You do not suppose that they will not have accounts in New York? They will have.

Senator HITCHCOCK. They will have accounts in New York only by increasing the balance that they carry over the requirements of the bill.

Mr. UNTERMYER. Which they are doing all the time.

Senator HITCHCOCK. And the bill has placed the reserve requirement low for the purpose of giving them a capital to operate on.

Mr. UNTERMYER. Let me illustrate. On the 1st of November, 1912, in the height of this last panic, the country banks had in 30 of the New York City banks $240,000,000, which the city banks were lending for them on the New York Stock Exchange, over and above the reserves of those banks—money that they had sent to New York to be loaned on the stock exchange by those 30 banks, in their own names; and of that amount 10 banks, to which I have referred, had $172,193,000 on that day belonging to their country correspondents loaned on the stock exchange, of moneys that did not form part of the reserves. This was independently of moneys that formed a part of the deposits of these country banks with the New York City banks; it was just money sent right on to be put into Wall Street, because of the high rates being paid for money then.

Senator WEEKS. When was that?

Mr. UNTERMYER. On the 1st of November, 1912; it was twice as much as these banks were lending in that way any 1st of November in any preceding year, yet the money was never more urgently needed at home.

Senator WEEKS. What were the rates?

Mr. UNTERMYER. Pretty high, I think, as high as 20 per cent.

Senator WEEKS. Not last November?

Mr. UNTERMYER. Yes; that was a terrible time of stringency.

Senator HITCHCOCK. Let me ask you if there is anything in the pending bill to prevent that situation?

Mr. UNTERMYER. Yes; I think that the whole theory of the pending bill will prevent it, for this reason——

Senator HITCHCOCK (interposing). What provisions in the pending bill will prevent it? I do not care anything about the theory.

Mr. UNTERMYER. The provision that makes commercial paper liquid, instead of being a dead asset, as it is now, until the day of maturity; the provision that makes that kind of paper desirable because of its rediscount privileges. That will turn, to my mind, the money of the country that has been employed in Wall Street, in stock-exchange operations, into commercial paper, because it will then be a liquid asset.

Senator HITCHCOCK. I understand that this $240,000,000 sent to New York City by country banks was not sent as a part of their reserves?

Mr. UNTERMYER. It was not sent as as part of their reserves. It was in addition to their reserves.

Senator HITCHCOCK. And it was not sent as a part of their deposits?

Mr. UNTERMYER. Of course, it was a part of their deposits; it must have been.

Senator HITCHCOCK. Not reserve deposits?

Mr. UNTERMYER. No; not part of their reserve deposits.

Senator HITCHCOCK. It was sent there because a good rate of interest would be paid for it.

Mr. UNTERMYER. And because it was liquid. Because of the fact that the only liquid asset a bank can get nowadays is a stock-exchange loan. The banks are right in putting their money in that form, because they can get it overnight. But when you arrange it in the United States as they do in other countries, so that commercial paper is quite as liquid as a stock-exchange loan, you will divert your loans to commercial paper.

Senator HITCHCOCK. Now, Mr. Untermyer, is it not the fact——

Senator WEEKS (interposing). May I ask Mr. Untermyer a question right along that line? You do not know of anyone who is opposed to making that change, do you?

Mr. UNTERMYER. I hope not.

Senator WEEKS. I do not think there is anyone.

Senator HITCHCOCK. This letter is written from O'Neill, Nebr., under date of September 6, on the letterhead of the First National Bank, capital $50,000, surplus $70,000—a very respectable bank. It reads as follows:

Senator G. M. HITCHCOCK,
Washington, D. C.

DEAR SENATOR: I admire the stand you are taking on the pending currency and banking bill. I can see no inducement for banks located as I am to longer remain in the national system if this bill becomes a law. I very much despise the present Nebraska guarantee law, but believe it to be much better than to be forced into a measure that gives the contributors no voice in the management.

This bill may do for the city banker. I can not see where it in any way will be of any benefit to the bank dealing with the farmers and located as I am.

I hope you may be able to so modify it as to give us the right to go in or stay out; and, from my present understanding of the bill, we will dead sure stay out.

With kindest personal regards, I am, yours, truly,

E. P. GALLAGHER.

Now, there is a country banker. He has been in the banking business——

Mr. UNTERMYER (interposing). Is he characteristic of many of the 26,000 bankers?

Senator HITCHCOCK. It is characteristic of all the letters that I have received from country bankers in Nebraska.

Mr. UNTERMYER. Very often a certain amount of misunderstanding about any complicated measure will exist among those affected by it.

Senator HITCHCOCK. I do not think this is a misunderstanding. This man has built up a very successful bank, and he has on the bottom of this statement, on this card, these words: "This bank carries no indebtedness of its officers and stockholders." It is a model.

Senator SHAFROTH. What is its capital?

Senator HITCHCOCK. Its capital is $50,000; its surplus, $70,000; deposits, $487,000; cash and due from banks, $146,000. Its loans are $400,000. That is what I consider a model country bank.

Mr. UNTERMYER. Yes.

Senator HITCHCOCK. And as I have said, his statement shows that his bank has no indebtedness of officers or stockholders—which I know that Mr. Untermyer would approve of.

Mr. UNTERMYER. That ought to be posted in every New York City institution.

Senator HITCHCOCK. I knew that you would approve that. Now, here is a man who will not come in and who believes that others will not come in.

Senator SHAFROTH. Will he not get a benefit directly from the reduction from 15 to 12 per cent which will operate just as I have stated in my illustration of $100,000?

Senator HITCHCOCK. I want to ask Mr. Untermyer some questions on that head. This man is located at O'Neill, Nebr. If he should get into this system and keep all his reserves, either in his own bank or the reserve bank of his district, and he should go to his reserve bank for a discount and that reserve bank should say to him: "Mr. Gallagher, we do not care to discount any of your paper," what is he going to do?

Mr. UNTERMYER. Why, his paper is so good that it will have a market all over the country under this bill.

Senator HITCHCOCK. I am asking you what he is going to do?

Mr. UNTERMYER. Simply sell it through discount associations, acceptance houses, and other institutions that are bound to spring up under this bill. It will be as liquid as stock exchange collateral. Suppose you have an account with a broker, and you have got collateral, and you go to that broker and he will not give you a loan on that collateral. What are you going to do? Your collateral is good. You must go somewhere else.

Senator HITCHCOCK. I say that he is bound to keep his reserve in the reserve bank, but the reserve bank is not bound to discount his paper. As it is now, he can keep his reserves at Omaha, or St. Paul, or Chicago, or Minneapolis, or South Omaha, or St. Louis, and if the bank he is dealing with does not give him good treatment he can go to another. He is independent; but under the system proposed in this bill he is absolutely dependent upon one source that can practically ruin him by refusing to discount his paper.

Mr. UNTERMYER. I do not agree with you.

Senator HITCHCOCK. Can you explain how he can get relief under the bill?

Mr. UNTERMYER. If the bill carries out its purpose, this commercial paper is going to be as liquid as stock exchange loans, and he can get a loan anywhere.

Senator HITCHCOCK. I know that is a stock phrase, but how is he to get more collateral security when he goes to the reserve bank at Chicago and presents his paper at a discount and the reserve bank refuses to discount it? What is Gallagher going to do? His money is tied up in the Federal reserve bank.

Mr. UNTERMYER. Of course you are assuming that he is entitled to this discount. If his paper is turned down at the Federal reserve bank, he will take it to any discounting house or to any of the many people who are going to spring up to take care of that paper. He will sell it just as if that paper were secured by stock-exchange collateral.

Senator HITCHCOCK. Then he does not need it now?

Mr. UNTERMYER. What I mean is that he is not limited to that reserve bank. You need it now, because you can not build up an open market for bills of exchange, unless you have some such system as this. We have such markets everywhere else in the world.

Senator HITCHCOCK. You admit that at the present time Mr. Gallagher is very well situated. He can get half a dozen banks in Omaha to do business with.

Mr. UNTERMYER. That depends upon what he wants.

Senator HITCHCOCK. Undoubtedly. He keeps a part of his reserve in Omaha.

Mr. UNTERMYER. We have no right to assume that he will not get the credit from the reserve bank to which he is entitled. He and his associates will control the bank.

Senator HITCHCOCK. I would like to have you point out in the bill any way he can demand that as a matter of right—demand rediscount of his paper.

Mr. UNTERMYER. You must know that to be impossible to put in.

Senator HITCHCOCK. I think it ought to be put in somewhere.

Mr. UNTERMYER. It is not possible.

Senator HITCHCOCK. I think otherwise. You are going to destroy the independence of these country banks and make them absolutely dependent upon the yes or no of some man.

Mr. UNTERMYER. On the contrary they are dependent on the yes and no of their own shareholders. The shareholders direct these banks; they have six out of nine votes and it is fair to assume that their own representatives are not going to treat them unfairly. They have two-thirds of the representation on this board.

Senator SHAFROTH. The bill is drawn for the purpose of advancing money and they are given the right of representation in the institution that is created by the bill.

Mr. UNTERMYER. Yes.

Senator POMERENE. And under this bill they have the same right to go elsewhere to get their accommodations that they now have under the present law. They have the right to go to places other than the reserve bank.

Mr. UNTERMYER. Yes; in addition to which they will build up a market for this sort of commercial paper.

Senator REED. But they will not have the same right. It could more properly be said to be the same practical right—not the same legal right. There is nothing which says in terms that if they do not get money from the Federal reserve bank they can not go to another place to get money. If such a law were enacted, it would, of course, be unconstitutional; but under this law when it is in full operation the reserves carried by the member banks must all be put with the central reserve bank. Of course, that means that their reserves will be withdrawn from the banks where they now keep those reserves.

The CHAIRMAN. Not their balances.

Senator REED. I am speaking of reserves. It is true, as Senator Owen suggests, that they could keep balances in the other banks.

The CHAIRMAN. They are now doing it; 9 per cent in excess of the legal reserves.

Senator REED. Now, looking at it from a practical point of view, suppose that a banker with what ought to be regarded as acceptable security comes to this Federal reserve bank, presents his security, and is turned down. About how much chance would he have afterwards to have that paper rediscounted, unless there was a tremendous cut made in it, by any other member bank, or with any of the reserve banks?

Mr. UNTERMYER. My contention is that there will be such a general and open market for paper of this kind that the reserve bank will not be the sole resort of the member banks at all. It is not true in any other case. There are dozens and dozens in every one of these countries of other institutions that buy this paper, and they take it to the bank when they need the money.

Senator REED. There is no other country that has a system like this we are proposing to inaugurate.

Mr. UNTERMYER. No; there is no other country that has the large bank representation in the system that is given to the banks by this bill.

Senator REED. That is right where I think the danger lies. You seem to think that large representation is an element of safety.

Mr. UNTERMYER. You mean the bank representation?

Senator REED. The bank representation is just where I think the danger lies. A perfectly disinterested management of that kind might do one thing; an interested management would do quite a different thing.

Mr. UNTERMYER. But, in considering the character of our country and its diversified interests and climates and industries, you have to have a number of these banks. You can not have one bank any more than you can have one reserve bank for all Europe.

Senator REED. I am not speaking of one bank.

Mr. UNTERMYER. For these different banks you have two alternatives. One is to align the bank with the member banks of the country and the other is to have its capital issued to and bought by the general public, as it is in Europe. Everybody owns bank stock there. That is true of the Bank of England, with the Bank of France, and with the Bank of Germany. They have vast numbers of shareholders in very small holdings.

If you take the second course and issue this stock to the public—which I believe they will gladly take—then we have to do as the European banks do, open the doors and accept deposits from the general public and buy paper in the open market in competition with the banks. Those are the two alternatives. You have either to have one system or the other.

Senator REED. You are getting away from the thought I was trying to suggest to your mnid and upon which I wish to get your opinion. I am not going to undertake to express my own opinion now. I am trying to get your help this morning and I do not know any better way to get it than by a mere statement of what you think about it. In the banking world to-day there are some institutions so large and so powerful that they necessarily exercise a very considerable controlling influence over many other banks and generally over the whole financial world. They have their connections, direct or indirect. There are lines in many places. I said the other day to another witness, or rather advised him, that I have understood that there are a number of banks in my own State—splendid institutions; very strong—that have relations of some kind with the great financial institutions in New York City, and what is true of my State I take it is true of others. Now, just at this point I want to ask you whether or not you think that is the case.

Mr. UNTERMYER. It is undoubtedly the case. The ramifications are far greater than is generally realized.

Senator WEEKS. May I ask a question right there? I want to ask Mr. Untermyer what he means by "relations," if you will allow me.

Mr. UNTERMYER. I do not mean by "relations" that they control these institutions. What I mean is that they are the correspondents for these banks; that they sometimes hold stock in the bank.

Senator WEEKS. Frequently?

Mr. UNTERMYER. Infrequently. That they sell securities to these banks, because some of our banks in New York are sellers of securities as you know; and they frequently load them up with a great many securities; that these banks throughout the country or their officers are underwriters in a great many of the financial enterprises that are floated from New York; and that in one way or the other the ramifications of the great New York banks are very diversified.

Senator REED. In other words, and in a word, no matter what the relationship springs from, there is an intimate, close working arrangement between many of the banks of the country and large financial institutions of the East, so that they make up in a way a chain of banks which may run across the country, or partially across the country?

Mr. UNTERMYER. I would not put it quite so broadly as that—that they make up a chain. They certainly have relations and at times they have certain spasmodic relations. They have various relations.

Senator REED. I intended to go into another matter, but since the Senator has raised this question——

Senator NELSON. Senator Reed, may I ask a question or two in this connection? I do not deisre to interrupt you.

Senator REED. I will come to a sort of a stopping point in a moment. I want to speak of this kind of relation. Take a man of immense capital, and there are a few in this country, interested in a bank or two in New York City, interested in a bank or two in Chicago, interested in some other banks in other towns, having a controlling interest or having a potential interest. Does not that condition exist?

Mr. UNTERMYER. Not in that form to any extent, Senator Reed. I do not think that any of the men who have very large interests in the great banks of New York have very large interests—stock interests—in the banks of other cities; not to any appreciable extent. Of course they have very great interests in a number of banks in New York City, and they have relations more or less close with great institutions throughout the country, such as being their correspondents, such as having participated in large syndicate transactions, and in a variety of other ways; but the stock interests of the few great men who control things in New York in banks outside of New York are not appreciable.

Senator REED. Aside from the stock holding, what is the tie?

Mr. UNTERMYER. The tie is a very close one.

Senator REED. I will say to you frankly that I know of many banks out West generally regarded by the business world as Morgan banks, and they seem to be able to get money in greater quantities and have better facilities through some means for handling large enterprises than other banks of the same capital.

Mr. UNTERMYER. The tie is a recognized tie. It is a tie largely of mutual participation in great financial enterprises. For instance, you take the banks in Senator Weeks's city, in Boston. In two of the three great banks there there is largely represented interests of Kidder, Peabody & Co. and Lee, Higginson & Co. Lee, Higginson & Co. have very close relations with Morgan & Co., in New York. They make vast sums of money together. Lee, Higginson & Co. are a very potent factor in two of those three big banks there, not only because they own a considerable amount of stock, but mainly because they are a large part of the support and prosperity of those banks. They are identified with so many great institutions, railroad and industrial, whose deposits go into those banks, that they would be a most important factor, even though they did not own any of the stock. Stock ownership is not the criterion of control or influence over a bank. The true criterion is the capacity to bring business and otherwise aid in the upbuilding of the institution.

Senator WEEKS. Let me suggest to you in that connection that Lee Higginson & Co. do not any more control those banks than you do.

Mr. UNTERMYER. I said two of the three, you will remember.

Senator WEEKS. I am speaking of the two of the three that you are. They do not any more control the banks than you do.

Mr. UNTERMYER. Senator Weeks, I have not said they controlled the banks. What I have said is that they have substantial stock holdings in both of those banks.

Senator WEEKS. They have.

Mr. UNTERMYER. That was proven by the testimony before the Pujo committee, and I refer you to the testimony taken there for detailed information on the subject, but that is the least part of the control they exercise. The mere stock interest is the least part of the control they exercise. The real source of the power they have in those banks, and justly so, is their ability to build up and add to the success of those banks, because of the great enterprises in which they are engaged, whose deposits are directed to those banks.

Senator WEEKS. Now to what extent does that interest control the policy of the bank? I know something about the case of Lee Higginson & Co. I would like to have you explain what that interest amounts to.

Mr. UNTERMYER. In what direction? Nobody has assumed any malign influence in this discussion.

Senator WEEKS. If there is not any malign influence, what kind of influence do Lee Higginson & Co. have over these banks?

Mr. UNTERMYER. Well, in the first place, they buy and sell securities, do they not?

Senator WEEKS. Occasionally.

Mr. UNTERMYER. Very much more frequently, if you will pardon me, Senator Weeks, than you seem to think. If you will look over their lists of securities.

Senator WEEKS. I know what their lists of securities are. They probably own a couple of millions, but they are both $75,000,000 banks.

Mr. UNTERMYER. I think you will be surprised to find that they have a good deal more than that.

Senator WEEKS. I am not going to be surprised, because I know better.

Mr. UNTERMYER. That is my recollection.

Senator WEEKS. You are trying to recollect a lot of things and I think your recollection is at fault in that instance.

Mr. UNTERMYER. Perhaps so, but I think not. At any rate, even though they do not hold securities issued by these financial houses to the extent stated they participate in underwritings and are otherwise identified with them.

Senator WEEKS. Very seldom.

Mr. UNTERMYER. But they do participate even though it may be seldom.

Senator WEEKS. They undoubtedly do, but it is very seldom.

Mr. UNTERMYER. And Lee Higginson & Co. are a very great aid to those banks.

Senator WEEKS. Undoubtedly they divert business to those banks whenever they can, because they are stockholders and they want to make those banks prosperous.

Mr. UNTERMYER. It is right that they should.

Senator WEEKS. Yes, it is right that they should.

Mr. UNTERMYER. There is that tie.

Senator WEEKS. Yes, there is that tie.

Mr. UNTERMYER. And then there is that tie between Lee Higginson & Co. and J. P. Morgan & Co.

Senator WEEKS. That is true; but J. P. Morgan & Co. do not own stock in those banks.

Mr. UNTERMYER. I understand; it is not necessary so long as they have Lee Higginson & Co. as their partners.

Senator WEEKS. What I am trying to get at is what influence J. P. Morgan & Co. or Lee Higginson & Co.—what that influence amounts to, if it is not a malign influence. What is it?

Mr. UNTERMYER. It is the ability to influence the making of loans on great financial projects.

Senator WEEKS. You refer to good loans?

Mr. UNTERMYER. Well, generally speaking, yes; but everybody can not get money on good security, and it has an influence in preventing or refusing loans to enterprises that are not favored by these people and which may be in competition with them. That is the point.

Senator WEEKS. Do you think that has ever happened in the case of those banks?

Mr. UNTERMYER. I would rather not say anything on that subject. I do not care to express an opinion at this time. It is not germane to our present discussion. The subject is fully discussed with complete data in the report of the Pujo committee.

Senator WEEKS. Do you know anything about it?

Mr. UNTERMYER. I do not know the inner workings of those banks.

Senator WEEKS. Let me say for the public record, as far as that is concerned, that Lee Higginson & Co., in my judgment, have never attempted to influence the making of loans to anybody else, or buying any other securities than those which they control themselves if the notes and securities offered were good.

Mr. UNTERMYER. I have not assumed that they have.

Senator WEEKS. But when we talk about influences in the tone in which that is being discussed, the impression is given that malign influences or some improper influences are being used. Of course, a bank aids its customers—its good customers—whenever it can. If

Lee Higginson or anyone else keeps a good account with the National Shawmut Bank, of Boston, the National Shawmut Bank is going to try to aid Lee Higginson & Co. in their business enterprises whenever it can properly do so.

Mr. UNTERMYER. Do you believe that if a body of men wanted to start competition with the United States Steel Corporation to-morrow or at any other time that they could borrow money from any of those banks?

Senator WEEKS. They could from one of them.

Mr. UNTERMYER. I am not speaking of the three banks.

Senator WEEKS. If the loan was good they could get the money; if it was not good, if it was a hazardous loan, they could not get it.

Senator REED. Well, we are getting away from what I was talking about. I do not care whether it is stock ownership; I do not care whether it is the simple power of great capital, but the point is that here are these great monopolistic enterprises and there is a tie, one tie or another, which you state, in your opinion, exists, and which spreads out in many directions.

Mr. UNTERMYER. Yes; in the way I have stated. It is a nebulous, intangible sort of thing.

Senator REED. But like the nebula it may be very powerful if it gets together. A nebula may make worlds and planetary systems.

Mr. UNTERMYER. I have always contended that it had a great deal of power.

Senator REED. What I am getting at is this, and this is the next step that I want to take: Is it not, in your opinion, very likely to happen that these same powerful influences which now exist in an unorganized condition will be potent in the organization when once created? I mean by that—I will put it again in the form of a statement.

Mr. UNTERMYER. I understand.

Senator REED. I will take my section of the country. There will be a regional bank in which we will be incorporated. There are a lot of little banks out there and there are a few large banks. The large banker is active, looking at the broad field; the small banker is active, but he is looking generally after his particular institution. Here are these large banks that have these influences of which we have been speaking, ramifying out from a central point. We are going to elect three directors for a regional bank. Whom do you think is going to exercise the most potent interest in that election?

Mr. UNTERMYER. That is a mere matter of conjecture.

Senator REED. Is it a matter, really, of conjecture? Is it not a matter of just prudent forethought?

Mr. UNTERMYER. My point, however, is this: That we are in such a perilous condition in the situation in which we now find ourselves that this proposed bill can do only good in the direction you are seeking.

Senator REED. I am not talking about a choice between two evils.

Mr. UNTERMYER. I believe it will dissipate a lot of that.

Senator REED. We are about to create a system.

Mr. UNTERMYER. I believe it will scatter it.

Senator REED. It is our business to try and create a law, or rather a system, no part of which will be at fault, and to try to completely overcome any present evil conditions.

Mr. UNTERMYER. I think this bill will aid largely, and for this reason: Every bank has representation in the directors regardless of its size—equal representation and the naming of an elector. The small bank has as much to say about the election of those three directors as the large banks.

Senator REED. That far it is good.

Mr. UNTERMYER. That tends to overcome the power of the big banks in the first place.

In the second place, when you take the second class, class B of the directors, the Government has supervisory power over the operation of those gentlemen and can remove them if they do not truthfully represent the agricultural, industrial, and commercial interests they were formed to protect.

Senator SHAFROTH. They can do that for cause.

Senator WEEKS. How is that cause to be determined—whether they are representing those interests properly or not?

Mr. UNTERMYER. I understand as the bill stands the Government simply has the power of removal. It does not need to give them a trial.

Senator O'GORMAN. The reserve board in Washington can remove them for cause and the reserve board is the judge of the cause.

Mr. UNTERMYER. I think so, as I read the bill. If it is not so it ought to be so. That being so, I think there is nothing to fear in the domination of these reserve banks; and that is one reason for having a number of them rather than a few. The danger of the domination of those reserve banks by the great financial interests is so trifling as compared with the control they now exercise over the finances of the country that we should fly to this measure for protection because I have not seen anything better suggested.

Senator O'GORMAN. For protection against what, Mr. Untermyer?

Mr. UNTERMYER. For protection against the concentration of the credits of the country and the control of those credits in a few hands—to promote the dissipating of the control of the credits.

Senator O'GORMAN. You are familiar with the banking conditions in Europe, are you not?

Mr. UNTERMYER. Yes; fairly.

Senator O'GORMAN. You think the banking conditions in Great Britain are quite satisfactory?

Mr. UNTERMYER. Very; and vastly superior to ours for this reason——

Senator O'GORMAN. I do not ask for your reasons just now. Would the same be true of the conditions in Germany and France?

Mr. UNTERMYER. Yes; they have less banks, but they are real competitors.

Senator O'GORMAN. In Germany the great banking center is Berlin, is it not?

Mr. UNTERMYER. Berlin is one of the great banking centers; yes.

Senator O'GORMAN. What is the next?

Mr. UNTERMYER. Frankfort.

Senator O'GORMAN. And Paris is the great banking center of France?

Mr. UNTERMYER. Yes.

Senator O'GORMAN. And London of Great Britain?

Mr. UNTERMYER. Yes; London; but there are other big centers in England where you can get large sums of money without going to London.

Senator O'GORMAN. Is there any difference between the influence exercised by the great London bank in Great Britain and the great bank in Paris, through France, and the great banks in Frankfort and Berlin, through Germany? Is there any difference between these influences and the influences that you think prevail in this country with respect to the New York banks?

Mr. UNTERMYER. Yes; a vast and fundamental difference.

Senator O'GORMAN. In what respect?

Mr. UNTERMYER. You can go with a venture to London and if it is a meritorious venture and you are turned down in any one of seven of the great banking houses you can go to the eighth place and they will take it up without regard to what the other men have done and without consulting them. In other words, there are separate and distinct groups in London; there are less numbers of banks, but there are more separate groups and they operate independently of one another; they do not operate in concert with one another; and the result is that there is competition for the best kind of financial business, which does not exist in New York. You could not carry out a great venture in New York requiring a large sum of money against the opposition of some one, two, or three individuals or institutions there. They would consult one another before acting.

Senator O'GORMAN. You do not think the London bankers consult one another in respect to large enterprises?

Mr. UNTERMYER. They do not in that sense. There are different groups of bankers, different sets of underwriters. I have had considerable experience in that direction for the past 25 years, and I know that to be a fact. They operate in absolute independence of one another, which is in striking contrast with our unfortunate conditions, as you will find demonstrated in the report of the Pujo committee. There is no custom of interlocking directorates, either. That is practically unknown abroad.

Senator O'GORMAN. You say that is also true of the banks of Frankfort and Berlin.

Mr. UNTERMYER. It is true in Berlin to a somewhat less extent. There are less independent units there.

Senator O'GORMAN. How about Paris?

Mr. UNTERMYER. There are less independent units in Paris than in London, but more than in Germany.

Senator O'GORMAN. What are the leading banks in Paris?

Mr. UNTERMYER. There are five or six, as I recall, including the Credit Lyonnais, the Bank of Discount, and the Bank et des Paris de Pays.

Senator O'GORMAN. The Credit Lyonnais is the powerful bank of France, is it not?

Mr. UNTERMYER. Not the only one. There are one or two others that are almost equally powerful.

Senator O'GORMAN. It has connections and branches in every department of France, has it not?

Mr. UNTERMYER. Yes, sir; as have one or two other concerns their branches in other parts of France.

Senator O'GORMAN. Then, among the great banking interests of France there are but two or three or possibly four units?

Mr. UNTERMYER. Well, not more than a half dozen, we will say.

Senator O'GORMAN. You say there are not that many in New York City?

Mr. UNTERMYER. What I said was that in New York City there were far more units, but they operate together and they are interwoven and intertwined and they have places where their interests all come together in given institutions, so that they may be regarded as, in fact, constituting very few units, so far as concerns genuine competition. They share in one another's enterprises. The smaller men live to some extent on the patronage of a few big men and their enterprises, and when it comes to the attempt to do any business or to finance a new enterprise that would compete with any one of them or with any business that is under the protection of any of the big men the others rise as one man in the defense of that one's privileges. It is the most hopelessly despotic system in the world.

Senator NELSON. Mr. Untermyer, does the system which exists in New York of making call loans on stock collateral exist either in France, Germany, or England?

Mr. UNTERMYER. Not exactly in that way. They make loans.

Senator NELSON. Call loans?

Mr. UNTERMYER. They make loans for the fortnightly settlements, you know.

Senator NELSON. Do they make call loans, demand loans, secured by stock collateral, as they do in this country?

Mr. UNTERMYER. In a somewhat modified form in England they do.

Senator NELSON. I am speaking of demand loans.

Mr. UNTERMYER. Demand loans in the sense that they are payable at the fortnightly settlements. They do not settle every day on the London Stock Exchange as they do here.

Senator NELSON. A moment ago you spoke of these stock collateral call loans as liquid loans.

Mr. UNTERMYER. Yes.

Senator NELSON. The panic of 1907, as well as the panic of 1893, and the panic of 1873, disclosed this fact: That in the assets of a bank these stock collateral demand loans were indicated as liquid but they were the poorest of all loans.

Mr. UNTERMYER. I do not think so, Senator. I think it is only fair to say that they proved to be the best way in which a man could get his money.

Senator NELSON. In the panic of 1907 when the Treasury Department dumped so much money into New York to stop the panic there, was not most of that money used by the leading banks to check the panic on the stock exchange?

Mr. UNTERMYER. Yes——

Senator NELSON. And not for the purpose of moving the crops out West?

Mr. UNTERMYER. I think there was over $25,000,000 used, most of it disbursed by J. P. Morgan & Co., to stop the panic on the stock exchange. All the figures on that subject are collated in the testimony taken by the Pujo committee.

Senator NELSON. Is not this a fact: That in the midst of a panic these stock collateral loans, demand loans, when the banks which took the loan makes a call on the borrower and wants the money, the borrower has not got the money. He tries to get it from another bank, and all the banks are in the same condition; they are all holding back their money. How can you call that loan liquid then?

Mr. UNTERMYER. It is liquid because it is always covered by an excess of about 20 per cent collateral readily salable, and all the man does when he can not get his money is to sell the security on the stock exchange and get his money.

Senator NELSON. But in times of panic he can not get his cash. He has to take clearing-house certificates.

Mr. UNTERMYER. The man who has the loan gets the money, and I do not think anybody during panic conditions did not get money on that sort of loans.

Senator NELSON. Did not the clearing house settle their balances with clearing-house certificates?

Mr. UNTERMYER. The banks in the clearing house, yes; but the individual lender or creditor who had a loan, amply secured by active stock-exchange collateral, got his money.

Senator NELSON. How did it come that actual cash was at a premium at that time?

Mr. UNTERMYER. Because, I suppose, the banks would not give up the money they had and people could not get the money out of the banks, and because they did settle their differences between their members by clearing-house certificates. It was the very wise thing to do.

Senator NELSON. Out West, in our agricultural country, where we live, we find that mortgages on real estate, on improved farms, are the very best security.

Mr. UNTERMYER. That may be well secured, but they are not liquid.

Senator NELSON. They can be sold, just like your call collaterals, can they not?

Mr. UNTERMYER. They are not due. You can not go to the borrower and get the money.

Senator BRISTOW. How can you go to the borrower and get the money on a short-time note if he has not got the money?

Senator REED. Mr. Chairman, the Senate meets at 12 o'clock today, and I wish we might take a short recess.

The CHAIRMAN. Very well, we will meet 30 minutes after the Senate adjourns.

(Thereupon, at 12 o'clock m., the committee took a recess.)

AFTER RECESS.

The CHAIRMAN. The committee will come to order. Mr. Untermyer was examined in such a way that he was rather deflected from the proposition he started on.

Senator SHAFROTH. I would like to state to Mr. Hitchcock, with relation to his First National Bank of O'Neil, that if you should calculate what they have to pay under the present bill and what they have to pay under the present law, you will find that they have to pay on 10 per cent, which would be $5,000——

Senator HITCHCOCK. Pay what?

Senator SHAFROTH. To the capital stock of the reserve bank, $5,000; and then they would have to pay 5 per cent upon their deposits—deposits of about $500,000, which would make $25,000—the total amount which would be required to be paid in cash to the Federal reserve bank would be $35,000. They have to keep as reserve now $45,000, whereas the amount which they have to keep as reserve and payment on their capital stock is only $30,000 and consequently it is $15,000 less in cash that they have to put up under this new bill than under the old law. If you take the amount which they now hold in their banks as recited by you, $146,000, and deduct from it $30,000, which they have to put up under this new bill, it would leave them $115,000 which they could put in their bank; and therefore they could get a competing bank to figure on rates of interest or loans for that on the market which they have, according to the amount which they have now in their bank, and for that reason it does seem to me that this new bill would be of advantage to that very bank, according to its own figures.

Senator HITCHCOCK. I do not think you and I had better discuss that now. I think we had better take Mr. Untermyer's views.

Mr. UNTERMYER. Now, taking up the discussion of this bill that is before us, I have these suggestions to make:

First, as to the conditions on which State banks shall be permitted to become members. As I remember the provisions of the bill the State bank in order to become a member is only required to conform to certain conditions of the bill. It is not bound to restrict its charter powers to the powers that would be possessed by a national bank. If the theory of the bill is to be carried out with the subscription of the national bank made compulsory, as I think it should be, State banks ought not to be permitted, to my mind, to get the benefit of membership in this system, unless their charter powers are restricted to the charter powers of the national bank. Unless those powers are so restricted there is very little incentive left to the national bank to stay in the system, because by becoming a State bank it can widen its powers. The powers of national banks should be somewhat amplified and made more liberal.

Senator POMERENE. In what respect?

Mr. UNTERMYER. They ought to be permitted to be trustees of mortgages, as State banks and trust companies can now be trustees of mortgages.

Senator HITCHCOCK. Of course, you realize that in many States there is no system of that kind. In the West we have no trustees for mortgages.

Mr. UNTERMYER. We have in this way: Trust companies in a great many Western States have the right to become trustees of mortgages made to secure an issue of bonds. It is a lucrative business. In my practice in almost every State in the Union I have had such trust companies act as trustee.

Senator HITCHCOCK. I thought you referred to a deed of trust, such as is given by individuals as security for loans.

Mr. UNTERMYER. I mean trustee under a deed of trust to secure an issue of bonds. A trust company now performs that function, and there is no reason why a national bank should not have the right to perform the same function. Many trust companies now act as executors and trustees of estates, and it is a question whether national banks should not be given that power.

Senator WEEKS. Do you think they ought to be given that power?

Mr. UNTERMYER. I do not see why not. If a trust company can safely exercise that power, which involves the investment of no capital of the bank and simply involves investing and holding the fund in compliance with fixed rules of law, I see no reason why a national bank should not have that same privilege. On the other hand, there are trust companies in many of the States, like New York, that have powers that are such that I think render it rather precarious to permit them to become members of this system, and would give them an undue advantage. They can invest money in stocks. I know some of them that buy and sell stocks very liberally.

National banks have no right to buy or deal in stocks. The Comptroller of the Currency says they have the right to buy and hold bonds for investment, but that is very doubtful. They do, in fact, hold bonds, but I do not think the phraseology of the national-bank act permits them to hold them nor to invest their money in that way. It was never contemplated, to my mind, that a national bank should act as an investment company. Its assets ought to be liquid; but if you are going to allow State banks and trust companies to buy and sell stocks while national banks can not do so, national banks in the large cities may go into the State banking system. But if you will say that a State bank which wants to become a member of a reserve bank must conform in its charter to the powers given to national banks there will be very little incentive for the national banks to change.

Senator POMERENE. And there will be less incentive for the State bank to go in.

Mr. UNTERMYER. To go into the national system.

Senator POMERENE. Yes; thereby curtailing their powers?

Mr. UNTERMYER. Except on the assumption upon which I have been proceeding that no bank can afford to stay out; that it can not stand the competition of the banks in the system. In other words, the ability to use its capital through the process of rediscount and the other rights given by this bill are so attractive that I do not believe the banks outside can compete—certainly not in the larger cities.

Senator WEEKS. Mr. Untermyer, do not you think this bill should be so framed, if possible, that it would draw in—not drive out—all banks not in the national system, so that we would have one banking system in the country?

Mr. UNTERMYER. Yes; that is the one thing to be hoped for if this plan is to be a success—that you will have all the banks in. The only question is how to get them in. I say the best way is not to furnish an inducement for them to go out. If State banks have powers not possessed by national banks and can go into the system with those powers why should not the national bank convert itself into a State bank and go in with these added powers?

For the purpose of preventing that situation I should unify the powers of national and State banks that become members, broaden the national-bank powers wherever possible, so they will conform to the reasonable powers of the State institutions.

Senator WEEKS. How can you unify the powers? We have no control over the powers of the State banks.

Mr. UNTERMYER. No; except that you can say that a State bank shall not be permitted to go into the system unless its powers conform to the powers of the national bank. Either I am right or I am wrong about the attractiveness of this plan. If I am right, they will go in; if I am wrong, they will not go in. It is not required that they shall narrow their powers very much. It simply requires that they shall step out of the speculative purchasing of stocks.

Senator SHAFROTH. Mr. Untermyer, here is a provision of this bill and I wish you would say whether it covers the objection, and if not, whether you could add something which will cover it. It is on page 16, and I will read it.

It shall be the duty of the Federal reserve board to establish by-laws for the general government of its conduct in acting upon applications made by the State banks and banking associations and trust companies hereinbefore referred to for stock ownership in Federal reserve banks. Such by-laws shall require applying banks not organized under Federal law to comply with the reserve requirements and submit to the inspection and regulation provided for in this and other laws relating to national banks. No such applying bank shall be admitted to stock ownership in a Federal reserve bank unless it possesses a paid-up unimpaired capital sufficient to entitle it to become a national banking association in the place where it is situated under the provisions of the national banking act, and conforms to the provisions herein prescribed for national banking associations of similar capitalization and to the regulations of the Federal reserve board.

Will you state what in addition to that will cover the point you make?

Mr. UNTERMYER. I have considered that provision very carefully and it is in the light of that provision that this suggestion is made.

Senator SHAFROTH. What suggestion has been made?

Mr. UNTERMYER. All the State bank is required by this bill to do is to comply with the reserve requirement, submit to inspection and regulation, and to conform to the provisions of this act. That does not involve any curtailment in its powers, whatever they may be. If, for instance, it has the power to buy and sell stocks on the market, it could still buy and sell stock and be a member of this reserve association.

Senator SHAFROTH. I think your suggestion is a good one. What I want to do is to have you formulate something to put in there to make an addition to the bill.

Mr. UNTERMYER. I will be very glad to do so.

Senator HITCHCOCK. Suppose, Mr. Untermyer, the Corn Exchange Bank in New York City, a State bank, having a large number of branches, as I understand, should desire to come into this association, under this bill; could it come in with all those branches?

Mr. UNTERMYER. It could under this bill, yes; but it ought not to be permitted.

Senator HITCHCOCK. You do not believe in branch banks?

Mr. UNTERMYER. I am very much opposed to branch banks. If national banks could have branches we would have mighty few banks in this country now. The great institutions would have established branches which would have driven the smaller concerns out of business. I do not think our institutions are adapted to the branch-bank system.

Senator SHAFROTH. Can you formulate an amendment to the bill to-night?

Mr. UNTERMYER. I will draft it now, if you do not mind.

Nor unless its charter powers are restricted to those that may be possessed by a national-banking association.

Senator SHAFROTH. Where would you put that—after the word "board"?

Mr. UNTERMYER. After the word "board," at the end of line 25:

Nor unless its charter powers are restricted to those that may be possessed by a national-banking association.

Senator HITCHCOCK. How would the bank go to work to restrict its charter powers?

Mr. UNTERMYER. By filing an amended charter.

Senator REED. Would not you reach that, Mr. Untermyer, much better by providing:

Provided, however, That when such bank comes into this system its powers shall thereupon become restricted to those permitted under this act.

In other words, you would not compel them to go through the form of having their charter changed, which might be very difficult. Indeed, many of them are not chartered at all. In one sense of the word they exist under a general law which they are powerless to change. But if you were to provide as I suggest it seems to me, then, by virtue of the act of coming in their powers would thereby become limited.

Mr. UNTERMYER. As a legal proposition, I would say they would not. They would go out of the system.

Senator REED. If they violated or exercised any of the forbidden powers, they would have to be disciplined.

Mr. UNTERMYER. They would go out of the system. An act done by them under that provision would not be ultra vires of the corporation.

Senator REED. No; it would not be ultra vires of the corporation, but the difficulty is the one I suggest. You take a bank in my State. It does not get a charter from the legislature. There is a general banking law, and when a bank is organized under that act it possesses all of the powers prescribed in the act.

Mr. UNTERMYER. Of course, it can by its certificate limits its powers.

Senator REED. Well, I doubt that.

Senator SHAFROTH. It seems to me that is a very good suggestion and I think you ought to dictate it now, so we will not overlook it.

Senator REED. I will do so.

Senator HITCHCOCK. That is true of all the Western States; it is only in the Eastern States where special charters are granted.

Mr. UNTERMYER. We do not grant them in our State. Nearly all of the Eastern States now operate under a general banking law.

Senator HITCHCOCK. But take a corporation existing in a State which empowers its corporations to exercise certain functions. They exercise those functions by virtue of the law and not by the virtue of incorporation papers.

Mr. UNTERMYER. But it has the right under that certificate to take as much or as little of that power as it chooses. It need not take it out unless it desires.

Senator REED. As I stated, I will dictate the provision I suggest:

Provided, however, That when such bank comes into this system, its powers shall thereupon become restricted to those permitted under this act.

What I have stated would not be the phraseology which should go into the bill, but it embodies the idea.

Mr. UNTERMYER. I think that entirely answers the purpose.

Senator REED. I want to say that is a very radical departure from the suggestion made here by some bankers who thought that trust companies and State banks would not come in at all if their powers were restricted and then some one asked the question whether that would not give them the advantage, and they seemed to admit it would. What is your idea about that?

Mr. UNTERMYER. Why, my idea would be to broaden somewhat the powers of a national bank.

Senator REED. If I am not cutting in on somebody else's examination—I do not want to do that—I would like to ask Mr. Untermyer one or two questions. Would you permit a national bank to loan upon real estate securities; and if so, to what extent?

Mr. UNTERMYER. I am rather opposed to that. I think there should be a separate system of land credits. I do not think it is the function of a bank whose assets should be liquid to loan upon real estate, except very short-time loans, and that is of no consequence, and that is not useful.

Senator REED. Mr. Untermyer, I want to direct your thought right on that question of liquid securities. It is in connection with an idea that has occurred to me. I again prefer making a statement to asking a question. I understand that the objection which bankers have to investments in State bonds or county bonds, municipal securities or farm mortgages, is founded in the fact that all of these securities have a long time to run, and, therefore, you say they are not liquid. That is they do not mature rapidly so that the money can be speedily obtained by virtue of the maturement. Now, if that is true, suppose there was a system provided by which those securities could immediately be cashed. Would they not then become absolutely liquid?

Mr. UNTERMYER. If we grant your premises, they would; but they have not found any method to do that abroad.

Senator REED. I am not speaking about what is done abroad. You know we do not find very many principles of government abroad that we think fit this Government, and it might be that statement could be extended to principles of finance.

Mr. UNTERMYER. I do not think it extends to finance. I think we are children in finance.

Senator REED. But they would be liquid; that is the point I am trying to get at.

Mr. UNTERMYER. If you made them liquid they would be liquid.

Senator REED. Now, they are safer, as an actual matter of safety, than ordinary notes of hand, are they not? Speaking largely now, assuming in both instances reasonable care, they are a safer line of security, are they not?

Mr. UNTERMYER. I would not like to answer that categorically. I should like to enter into an explanation of other provisions that come into this bill.

Senator REED. I am going to assume it, because the world assumes it.

Mr. UNTERMYER. The world assumes that genuine commercial credits are the safest basis.

Senator REED. I know they do in the banking world.

Mr. UNTERMYER. And they are, too.

Senator REED. Well, personally, I would rather have a farm mortgage on a good piece of agricultural land, so far as safety is concerned, than I would to have the note of John D. Rockefeller, because the land is there and nothing can take it away. However, I do not care to argue the question with you. If they can be made liquid, there would be no reason for not accepting them, would there?

Mr. UNTERMYER. You mean made realizable over night?

Senator REED. Yes, sir.

Mr. UNTERMYER. No; there would be no reason.

Senator REED. We are proposing to create a system here in which you can take a note of hand unsecured——

Mr. UNTERMYER (interposing). Not unsecured.

Senator REED. Putting an unsecured note—I mean it is not secured by collateral—and it is unsecured except that the name may be good or the names of two makers?

Mr. UNTERMYER. And the bank.

Senator REED. And you put that into a member bank, and you can indorse that paper and take it to a reserve bank and transform it into money at once. That is this system.

Mr. UNTERMYER. Yes, sir.

Senator REED. Suppose that instead of my taking my note of hand, as a purchaser I take my note of hand with a good farm mortgage back of it, and I put that into the member bank.

Mr. UNTERMYER. With what maturity?

Senator REED. I do not care if it is 10 years. That member bank takes it to the reserve bank and gets the money. The bank has got the money, has it not? It has relieved the member bank instantly?

Mr. UNTERMYER. Yes.

Senator REED. Now we come to the question of the reserve bank's condition. The reserve bank has issued a currency which is heavily taxed in order that it may not stay out too long. The member bank takes that money that it got back and puts it in its vaults and proceeds to use it and loan it out, so that the money has now gone into circulation; and in 30 or 60 or 90 days it wants to retire and take out this currency. What is too hinder it taking the money it got, putting it into the currency trade, and coming over and taking that note out? Why is it not a perfectly feasible thing, provided the class of long-time security is limited so that the amount could be limited?

Mr. UNTERMYER. If you make it an infinitesimal amount, it only weakens the system to an infinitesimal degree.

Senator REED. I do not mean to make it an infinitesimal amount, but I mean to make it substantial; not altogether long-time security.

Mr. UNTERMYER. To the extent to which you clog up the marketability and the liquid character of the flow of the currency between the member banks, the reserve bank, and the Government, to that extent you weaken the system.

Senator REED. Really, now, Mr. Untermyer, I am not trying to argue this; I am trying to elicit from you an absolutely unbiased judgment, and I want you really to consider this.

Mr. UNTERMYER. I have considered it.

Senator REED. I am not speaking about a condition whereby a bank would deal in nothing but farm mortgages and, suddenly being pressed, would come up with nothing but long-time paper; but assuming that a bank is doing a considerable business in short-time paper, could it not with perfect safety carry some long-time paper, because it can instantly convert it into cash, and thus get 30, 60, 90, or 120 days in which to gather in this money and utilize this short-time security by simply calling it in?

Mr. UNTERMYER. All I can say in answer to that is that I do not think that the class of security is a legitimate basis of a currency issue at all, whether it is a small amount in proportion to the bank's assets or whether it is a large amount in proportion to the bank's assets.

Senator REED. Do you think a Government bond is?

Mr. UNTERMYER. I do not think a Government bond is, either; and in Europe they do not, and they do not issue currency except to a very limited extent upon Government bonds For instance, you take the Bank of Russia; it will issue currency upon grain in the warehouse; and the Bank of Germany and the Bank of France will issue currency upon merchandise that is unsold, to a limited extent, whilst they will not issue currency upon municipal or Government bonds.

That brings me to the discussion of what is commercial paper, and in that respect I think that is the most important part of this subject of reserves.

Senator REED. Yes; but I take it that your fundamental reason for answering my suggestion rather in the negative lies in the fact that you would not take any long-time security, even if it were a county bond, a municipal bond, a State bond, or a Government bond?

Mr. UNTERMYER. I think not. I think it is absolutely unsound and unscientific finance.

Senator REED. And if a farm mortgage were bad, a Government bond would be bad, except that the Government bond is a higher class of security?

Mr. UNTERMYER. Relatively, that is about the proposition; and if you will allow me I hope to develop that a little later, because that is really the most important consideration, to my mind, in this bill; that is, as to what is commercial paper. Unless we are to have a great inflation resulting from this bill, if you are going to allow currency to be issued except upon paper that automatically retires itself in the current course of business, according to human experience, paper that represents an actual transaction, in the purchase and sale of merchandise, if you are going to depart from that to any extent, I think you run into the danger of great inflation.

The next suggestion I have to make in that line is that the reserve banks should have broader rediscounting power as to the character of paper that they may take than to rediscounting paper that is the basis of a currency issue. As the bill now stands, the reserve bank can only rediscount classes of paper that it may turn over to the Government, and for which it may get currency. It is limited to that. It ought not, in my judgment, to be so limited. I do not think it can get enough paper of that kind, according to our methods of doing business, for a long time to come; and even if it could, there is no reason to my mind why the reserve bank should not be able to rediscount for the member banks a certain proportion of paper that would not be the legitimate subject of currency issues.

Senator REED. In other words, you would want to enlarge their power of investment, but do not want to enlarge the power of inflation—I will use that term?

Mr. UNTERMYER. Yes. I want to distinguish between the two. I want to curtail the power of currency issue to define more clearly and more narrowly and correctly commercial paper and what is commercial paper for which currency can be issued so as to prevent the clogging up of the source of issue by paper that does not automatically retire itself.

I want first to call your attention to the definition in this bill of what paper is eligible to rediscount—what the framers of this bill have regarded as commercial paper, which I do not think is commercial paper.

Senator SHAFROTH. What section?

Mr. UNTERMYER. Section 14.

> Upon the indorsement of any member bank any Federal reserve bank may discount notes and bills of exchange arising out of commercial transactions——

Senator REED. What issue have you there?

Mr. UNTERMYER. I have got the last copy of the bill.

Senator SHAFROTH. There is a change in the language there. This is the act as it passed the House. It says:

> Upon the indorsement of any member bank any Federal reserve bank may discount acceptances of such banks which are based——

Mr. UNTERMYER. That is another provision. This is up here [indicating]. That has not been changed.

Senator SHAFROTH. Had you not better use the act itself?

Mr. UNTERMYER. Yes. That has not been changed. I have this one marked. [Reading:]

> Upon the indorsement of any member bank any Federal reserve bank may discount notes and bills of exchange arising out of a commercial transaction; that is, notes and bills of exchange issued or drawn for agricultural, industrial, or commercial purposes, or the proceeds of which have been used, or may be used, for such purposes.

That is not commercial paper at all, according to any known rule of commercial usage. In the first place, a note may be drawn to buy a farm. That would be for agricultural purposes. Or it may be drawn to buy a factory, and that would be a note drawn for commercial purposes, but that is not commercial paper:

> The proceeds of which have been used, or may be used, for such purposes.

In other words, you do not know what may happen to the proceeds after it has been acquired. That is hopelessly loose and impossible as a basis for currency issue. You will observe further on the bill provides that the character of paper that shall be the basis of currency issue shall be the character of paper that is subject to rediscount. In other words, when you define what is the subject of rediscount you define under this bill what is the basis of a currency issue. Commercial paper, according to European usage, is only that kind of paper that represents an actual transaction in the purchase and sale of merchandise. In other words, if A sells a bill of goods to B and draws on B for the price of that bill of goods and B accepts that draft, that is a commercial transaction, a legitimate commercial transaction, and presumably in the common course of business that merchandise goes into consumption and the money is paid with which to discharge that bill at maturity.

Senator SHAFROTH. Is that called prime commercial paper?

Mr. UNTERMYER. That is the only kind of commercial paper I know of. I do not know why the bill refers to "prime." I do not know what the difference would be between prime commercial paper and secondary commercial paper. But that is commercial paper, and it is commercial paper because the transaction automatically cancels itself. If currency is issued for that bill, in the common course of business experience the merchandise represented by that bill has gone into consumption, and the acceptor of that bill has gotten back the money with which to pay that bill, and the currency is retired.

The CHAIRMAN. It would take the money out of the pockets of the people and put it back?

Mr. UNTERMYER. So that automatically the currency will retire itself.

Senator REED. That is an acceptance.

Mr. UNTERMYER. You may take it in the form of a note, although we are the only people in the civilized world who do so. That form of obligation is too likely to cover up and confuse the difference between commercial transactions and other transactions. But suppose it is done, and the purchaser gives his note to the seller and the seller cashes it. That represents a commercial transaction. That note, after it goes into the bank in the ordinary course of business, is discharged at maturity out of the proceeds of the sale of the goods for which it was given. That is the reason why commercial paper is considered the highest order of security for currency issue.

We will say that I am a cotton manufacturer and I want to enlarge my factory or to buy a diamond necklace for my wife, or an automobile, or to buy fixed plant, or something that does not go into consumption, and I give my note for it. That is not commercial paper. That note is not going to discharge itself. It does not represent a transaction in merchandise that is intended to go into consumption. It may take me a lifetime to get the money back out of my factory if I use the money for extensions, or if I use it to buy something for my wife there will be no way of automatically discharging that obligation. That is where they have differentiated, in the countries that have used commercial paper as a basis for currency issue, between what is commercial paper and what is not; and that is the reason the use of an acceptance is rather better form than the use of a note. With the use of an acceptance the paper better explains itself. It almost tells its own story as to its character.

Senator HITCHCOCK. You are not speaking now of acceptances given by banks, necessarily, are you?

Mr. UNTERMYER. Acceptances given by banks do not rank as high in other countries as acceptances given by merchants, except for foreign transactions. In a foreign transaction they do not know the merchant so well or the purchaser does not want an obligation that must be enforced in a foreign country, and therefore they take the name of a banking house which is better known or more accessible for purposes of enforcing the obligation as an acceptor. But when you come to home transactions, a strictly commercial acceptance is on a higher plane than the acceptance of the most reliable banking house.

Senator BRISTOW. How much of the business of our country is done in this form of acceptance that you speak of where a bill of lading is attached to the goods?

Mr. UNTERMYER. I am not speaking of acceptances based on bills of lading to any extent. The merchant can use the acceptance without the bill of lading if the acceptor has credit. There is no bill of lading required. That business will have to develop as it has developed abroad, and for this reason: We will say the merchant to-day has a book of $100,000; that is, he has credits to the extent of $100,000. It is in the form of open book accounts. It is absolutely immovable. He can go to the bank and borrow. He explains that he owns these book accounts that are owing him, but he has nothing liquid on which to borrow. If we would adopt the form of acceptance that is prevalent in other countries, he would have something liquid.

Senator HITCHCOCK. Would not that tend to concentrate all the business near the source of supply of the goods purchased?

Mr. UNTERMYER. I should say not. The country would know that instead of buying goods on open account at 90 days he accepts at 90.

Senator HITCHCOCK. Let me give you an instance. Suppose a merchant out in my section of the country buys a bill of goods and it is shipped to him and he pays cash for it. In order to get the discount and in order to get the cash he puts the note in the local bank. Under the new system, when the goods are shipped to him, the eastern manufacturer or merchant would draw upon him. He could accept it and the eastern manufacturer would then deposit that acceptance in the eastern bank where he does business?

Mr. UNTERMYER. Yes; that is right.

Senator HITCHCOCK. Would not that tend, therefore, to concentrate the banking business, instead of allowing it to be local as it is now?

Mr. UNTERMYER. I think not, and for this reason: The man who pays cash would continue to discount his notes. It is the man who wants the credit and gets the credit whose credit would be converted into a liquid thing instead of being immovable.

Senator BRISTOW. Yes; but, Mr. Untermyer, the local bank which has been loaning the money to this merchant to discount his bills would no longer loan him the money, and Senator Hitchcock says the bank where the wholesale house is located would do business and the local merchant would have to meet the payment. He could not go to his local bank and have it extended if collections had not come in, as he does now.

Mr. UNTERMYER. But when he wants to buy for cash there is not any acceptance, anyway; then it is a sight acceptance.

Senator BRISTOW. But the note he gives to get the cash with which to discount his bills you are discrediting here by refusing it to be discounted as commercial paper.

Mr. UNTERMYER. I have not said it should not be discounted; but I have said it would release a vast amount of immovable unliquid assets in business in the form of open accounts. You can not do anything with an open account. If you could get for that open account a form of obligation on which you could issue currency and banking liquid and merchants could get along with less capital.

Senator BRISTOW. Do I understand that you want to revolutionize the whole of the commercial customs that have grown up between wholesaler and retailer, and make them carry their accounts in a different way, by this legislation?

Mr. UNTERMYER. No; you can not revolutionize these things of a sudden, but you can improve them, and I say if this acceptance is liquid and can be rediscounted in this way, you will help the business of the country by enabling the merchants to do business on less capital.

Senator BRISTOW. That is, you would require the wholesaler to change his methods of business?

Mr. UNTERMYER. I would not do anything of the kind. I would give him an opportunity to change it, because he would have a liquid asset. He does not need to change, but he would be given the opportunity to make the most out of his assets.

Senator SHAFROTH. Because it would be to his own advantage?

Mr. UNTERMYER. Yes, sir.

Senator REED. Are you through, Senator Bristow?

Senator BRISTOW. Yes.

Senator REED. I want to follow that. Over in Europe, where we seem to be going for all our light and inspiration in regard to this bill, they do have the system of acceptances thoroughly established. Is not that so?

Mr. UNTERMYER. Yes, sir.

Senator REED. And it is a common thing over there if a country merchant sells a farmer a bill of goods upon credit to take his acceptance—it may only be $50—and then to take that acceptance and put it into the bank?

Mr. UNTERMYER. I believe that is so, Senator.

Senator REED. We had a system of acceptance once in this country, did we not?

Mr. UNTERMYER. Yes.

Senator REED. And the American citizen simply refused, to use a slang phrase, to "stand for it" any longer, did he not?

Mr. UNTERMYER. I do not think so.

Senator REED. Is not this true, that if you would ask a farmer—possibly you have not had much direct contact with them—but the ordinary farmer, out in the State of Kansas, we will say, where they are pretty independent, would be asked by his merchant for an acceptance for a bill of goods. That farmer would say, "Well, my credit is not good. I will just go some place else."

Mr. UNTERMYER. The taking of an acceptance is giving him credit.

Senator REED. I can say to you now, as far as that class of people is concerned, that it is my opinion, that if you would ask him for an acceptance or a note, or anything else except simply to extend the credit, that he would go out of your store in a minute.

Mr. UNTERMYER. That may be so, until you establish a different custom. Of course, when you ask a farmer for an acceptance and he gives it, you are giving him credit; but leaving that out of the question for a moment——

Senator REED. I am trying to get some idea, Mr. Untermyer, of the practicability of this plan.

Mr. UNTERMYER. The plan does not involve that, at all. It involves simply that you should know—you must know—what is commercial paper.

Senator REED. We are of one mind on that; but speaking of the question of acceptance as a matter of distinguishing: Do you not think this is also true, that if the small country merchant, always accustomed to buy his goods upon 30, 60, or 90 days' time, or open account, with the right to discount his bills upon payment of cash, is to be asked by the traveling man representing a house to sign an acceptance, he would transfer his account mighty quick to some other house that did not have that system?

Mr. UNTERMYER. That depends on whether he would make more money by the one method of doing business than by the other. It depends on how this new system would work out.

Senator REED. My own judgment about it is that if you take the ordinary country merchant and undertake to change this system you would find very grave difficulty.

Mr. UNTERMYER. I am not asking that you change the system.

Senator REED. You are assuming, however, for the purposes of this present discussion, that an acceptance is the desirable form and that it is one means of determining whether you have really a commercial paper.

Mr. UNTERMYER. I think everybody will agree that it is the more desirable.

Senator REED. I think maybe from some standpoints, possibly not from others. Bur the point we have got to meet as framers of this bill is to make a bill that will fit the present conditions of this country. We can not inaugurate a system that must work for a number of years until new methods of business have been devised or forced. Of course you would not be in favor of forcing it?

Mr. UNTERMYER. No.

Senator REED. Therefore, it must be a matter of development; and as our country has been developing in the other direction, away from acceptances which used to be common and which no longer are indulged in to any great extent, if you are going to take that as the test of what is commercial paper—it seems to me we would be doing something in this bill that would be impracticable.

Mr. UNTERMYER. I do not think that I have given the impression—I certainly have not so intended—that that is the only test of what is commercial paper.

Senator REED. Oh, I know; but I am speaking about that one test. I am not trying to contradict you, not at all. I am trying to direct your thought to a particular phase of this thing and get your opinion, which I value very highly. I want to see if I am beclouded about another matter. You spoke about acceptances, and let us assume that we have them necessarily representing commercial transactions where the transaction itself would discharge the bill of acceptance. I can readily understand that would be true in this sort of case: We ship 100 bales of cotton to Liverpool, England. I make a sight draft, or I make a draft for the money that is payable 20 days or 60 days from date. The bank over there, or my customer, accepts that, and that cotton will be turned into money and will pay that off and discharge it. Of course in that transaction there is no guarantee that the money derived from the cotton will ever be sent back to me. It might be diverted to other places unless there is a bill of lading attached. Would you advise requiring a bill of lading to be attached?

Mr. UNTERMYER. Not at all, because in the ordinary course of business, judged by human experience, that cotton is going into consumption, and somebody is going to pay the acceptor of that bill for that cotton. He is going to get paid in some way for that cotton.

Senator REED. But what we have to rely upon, then, is the credit?

Mr. UNTERMYER. The current course of business.

Senator REED. The ability of the man to pay, and as these things are speedily realized upon, in the grand aggregate, there would be a flood of money flowing in substantially equal to the outgo?

Mr. UNTERMYER. You have got to judge those transactions by the sum total and average of human experience.

Senator REED. Let us see if an acceptance necessarily means that the thing which has been purchased and which is represented by the acceptance is going to be turned into cash.

Mr. UNTERMYER. Not necessarily.

Senator REED. I am going to take your automobile illustration. You are an automobile dealer. You sell me an automobile. I give you my acceptance. It was a commercial transaction. But it is a commercial transaction which represents, so far as I am concerned, a continuous outlay thereafter. That is true, is it not?

Mr. UNTERMYER. Yes; but I do not consider that a commercial transaction.

Senator REED. There is a multitude of transactions, then, which might be represented by an acceptance which would not be commercial within the meaning of the term as you use it, namely, there would be no means of repayment out of the proceeds?

Mr. UNTERMYER. Did you understand that I assumed that everything that was represented by an acceptance was a commercial transaction?

Senator REED. No.

Mr. UNTERMYER. No; not at all. I think it is a somewhat easier way of reading the transaction from the face of the paper, but in the the two instances I named I suggested, I made it clear, that an acceptance could represent a commercial transaction and could represent something that was not a commercial transaction.

Senator REED. I so understood you. That brings us to this point: An acceptance may represent a commercial transaction, as you used the term, and it may represent any other kind of a transaction. So that when a man comes to a bank with an acceptance, or that bank carries that acceptance to another bank for rediscount, the fact that it is an acceptance does not determine at all whether it is commercial paper within the term as you employ it.

Mr. UNTERMYER. No; but it does determine that it is a transaction, while if, for instance, you are in the manufacturing business and you sit down and write your note to get capital to put into your business, you go to the bank and get the money on that note. That, you know, is not a commercial transaction.

Senator NELSON. Will you allow me to ask a question bearing on that, Senator Reed?

Senator REED. May I ask one further question, because it is attached to what has been said?

But suppose that I am a manufacturer and I want capital to put into my business. For instance, I buy 100 tons of steel that I am going to put into the walls of my factory. I can give an acceptance for that, can I not?

Mr. UNTERMYER. Yes, sir. That would show the transaction; but if you bought the steel and went to borrow money on your note in the bank and that note was presented to the reserve bank, that would not show any commercial transaction, would it? It would show that you had gotten the money to put generally into your business where your business needs it.

Senator REED. In that case, having gotten it from the bank, it would show; but there would be no reason why I could not go and get money from B, not a banker, and give him an acceptance instead of a note, and take that acceptance and put it into the bank, and it would be nothing but a loan.

Mr. UNTERMYER. Who would be the drawer in that instance?

Senator REED. Why, I would make my draft upon this man.

Mr. UNTERMYER. Then it would be your draft, and he would accept.

Senator REED. Yes; and I would take that and put it into the bank.

Mr. UNTERMYER. What would he get for this acceptance?

Senator REED. He would be lending me this money and probably taking my note for it. What I am trying to get at is whether it could not easily be used to cover transactions in two ways?

Mr. UNTERMYER. Not so easily as by the present system.

Senator REED. First, I will go back to my factory illustration. I give an acceptance, and I find too that acceptances are prime commercial paper in banks, upon which I can borrow all the money I want, because the bank can take it and use it to have money issued upon it. Thereupon, desiring to borrow $10,000 from the bank, the bank says, "Bring me a good acceptance and I will let you have it." And I say, "Well, my friend, Untermyer, I want to borrow $10,000. I will give you my note," and you accept my draft. I take that over to the bank and get the money. How long do you think it would be before we would have a plan like that worked out?

Mr. UNTERMYER. It could not work very well. It has not worked in other countries, and it would not work here. In the first place, the people who deal in that sort of paper know pretty well the character of the transaction. The first thing that would occur to them would be, What is your business, and what is mine? On what account have I probably given that acceptance? Have I sold merchandise? Am I in a business that deals with and has relations with transactions of that character? Is this legitimate paper, or is it an accommodation acceptance? That is one reason why I think you should have 12 reserve banks instead of 4 or 5. The directors of those 12 reserve banks will be in closer contact with the business of their member banks and will know something about the relations of the customers to their banks.

Senator REED. It comes back, then, not to the form of the instrument, but to the knowledge which the banks have of the transaction and the purpose of the transaction?

Mr. UNTERMYER. Not so much so as one would say at first thought, Senator Reed, for this reason: If you are going to use a promissory note, made in the ordinary course of business, on which to get money from the bank, there is no outward indication from which to determine whether that represents an actual transaction in the purchase and sale of merchandise. A man may use a note for commercial paper, or the proceeds of it, or he may not. It does not on its face represent a purchase or sale of a commodity. It may be that it will work out that it did represent a purchase or sale, but in the other case you read on the face of the transaction more of it than you do in this one.

Senator REED. Possibly you might, but now you speak about limiting this to commercial transactions. What are you going to do with a case of this kind? I am a wholesale merchant and I buy $1,000,000 worth of goods. I buy them upon credit, and I give my promissory note to the manufacturer. By virtue of your knowledge of the man who made the note, of his dealings with the payee, you would know as a banker that it did represent a purchase, just as much as you would if you had an acceptance, would you not?

Mr. UNTERMYER. Yes; that is just as legitimate a form as the other.

Senator REED. The reason is that that good paper depends not upon the form but upon the fact that it is a transaction which pays itself out. But now it does not pay itself out; I have got the million dollars of goods upon my shelves and have not been able to sell more than $500,000 worth of them, when the note to the manufacturer is due. Thereupon I go down to my local bank and I borrow $500,000 to pay the manufacturer, and my local bank now has a note which represents an actual commercial transaction and a note which can be discharged by the sale of those goods, just the same as it could in the first instance. That is true, is it not?

Mr. UNTERMYER. Except that the second transaction does not represent what is defined as a commercial transaction.

Senator REED. Well, it is the obligation of a commercial transaction, for I took that money and paid it in.

Mr. UNTERMYER. But you are borrowing money now to carry that first transaction.

Senator REED. Yes. Then I take those goods and sell them to A, B, and C and they give me their promissory notes and when those notes mature they have sold the goods and got the money, they have paid me and I have paid the bank, and that ends the transaction. I may be dull, but I am unable to see why that is not just as much of a commercial transaction as the other.

Mr. UNTERMYER. Because, in the first instance, the obligation represents an actual exchange of merchandise. In the second instance it does not represent an actual exchange of merchandise. It turns out from your illustration, with all the premises assumed that they had the money with which to pay those bills, and so it would be if a man had his money in the bank and just took it out of that fund. You must have a general rule to define a commercial transaction, and there is but one rule that defines it, and that is that it represents a transaction of commerce—a trade, an exchange, a purchase, or sale of a commodity, of a salable commodity intended for resale or consumption.

Senator REED. And when the sale has once been made there can be no money borrowed to carry it through to its completion, its fruition. That would be a commercial transaction? Is that your definition?

Mr. UNTERMYER. No.

Senator REED. Of course, you said a moment ago that I had assumed a lot of premises; but the premise I assumed was that of the ordinary everyday business that appears in the form of millions of transactions in this country every year.

Mr. UNTERMYER. If you have goods on your shelves and you want to carry them, and you borrow money from your bank for the purpose of carrying those goods until you can sell them, that does not answer the definition of a commercial transaction, any more than if you borrow that money to put machinery into your factory.

Senator REED. You exclude that sort of paper that we have just been talking about, that you just defined, borrowing from the bank to carry a transaction.

Mr. UNTERMYER. As a basis of currency issue?

Senator REED. Yes.

Mr. UNTERMYER. I do not see how it could be made except to a very limited extent the basis of a currency issue. What I said was this, that it did not come within the definition of commercial paper. The European banks do not entirely exclude it. For instance, the the Bank of Germany and the Bank of France lend on merchandise up to a limited extent, on merchandise in warehouses. They lend upon it, but they do not call that commercial paper.

Senator REED. Just to the extent that you did limit the ability of the merchant to go to his local bank and get its help, you limit his ability to buy from a wholesaler, do you not?

Mr. UNTERMYER. No, I do not limit his ability to go to his local bank. There is no idea of limiting that. You could not do business without it.

Senator REED. Let us see if you do not necessarily limit it. You have now two classes of paper. One of these is an acceptance representing the transaction between the merchant and the manufacturer?

Mr. UNTERMYER. Yes.

Senator REED. That class of paper is so good that money can be issued upon it, just as is stated with absolute frankness. Therefore that class of paper would be in demand by banks more than any other class, would it not?

Mr. UNTERMYER. Yes.

Senator REED. You propose to create a system here by which banks are to get money, and they can get it only upon that class of paper?

Mr. UNTERMYER. They can also get it upon a note made by a man who is buying goods indorsed by the man who receives the note for the goods, and that is a commercial transaction in the present form of promissory notes.

Senator NELSON. I think, Senator Reed, you confused so-called bills of exchange and promissory notes.

Senator REED. Yes; possibly.

Senator NELSON. If you will allow me to draw out the question here in connection with what you say, it will appear.

We have two kinds of bills of exchange, commercial bills and finance bills?

Mr. UNTERMYER. Yes, sir.

Senator REED. A finance bill is drawn upon what we call an acceptance house?

Mr. UNTERMYER. Yes.

Senator NELSON. Who accept it and give it credit?

Mr. UNTERMYER. That is right.

Senator NELSON. A commercial bill is a bill drawn accompanying the bill of lading for the commodity?

Mr. UNTERMYER. Not necessarily drawn accompanying the bill of lading for the commodity, but it is drawn for a commodity and accepted by the merchant who gets the commodity.

Senator NELSON. Yes. That commodity is shipped, and the bill is supposed to be for the goods.

Mr. UNTERMYER. Yes, sir.

Senator NELSON. That is a commercial bill?

Mr. UNTERMYER. Yes, sir.

Senator NELSON. In the panic of 1907 the City Bank upon commercial bills of cotton and wheat and flour imported over $90,000,000 of gold?

Mr. UNTERMYER. I do not know as to that.

Senator NELSON. Is not that a matter of history?

Mr. UNTERMYER. I have heard it so stated.

Senator NELSON. When you come to promissory notes, you can not have anything in the nature or in the form of a commercial bill; you can only have it in the shape of signers, the men who sign the notes, but you can secure it by chattel mortgage, as a commercial bill of lading drawn against the shipment of goods.

Mr. UNTERMYER. It is not in the form of a commercial bill against documents, but of course it is a commercial bill.

Senator NELSON. It is a commercial paper, all the same?

Mr. UNTERMYER. Yes, sir.

Senator NELSON. You confused the two. A promissory note may be a commercial paper in that sense. It is a paper arising out of trade, but it is not commercial paper in the sense of a bill of exchange as it is drawn against shipments of goods.

Mr. UNTERMYER. No; it is a commercial bill as distinguished from a commercial bill with documents attached.

Senator REED. Of course, Mr. Untermyer has already said that he did not propose to require the attachment of the bill of lading to the warehouse receipt, so that we are left more or less to the form.

Mr. UNTERMYER. Yes; Senator Nelson's description of the distinction is very precise.

Senator NELSON. If you will allow me, Senator Reed, a commercial bill is like this: For instance, the millers at Minneapolis ship a lot of flour to Liverpool. They draw a bill of exchange against that flour and get that bill discounted. The acceptor pays it out of the proceeds of the flour. That is a commercial bill of exchange, and it is the best kind of paper there is in the world, because it is drawn against a necessity of life, and that necessity—that shipment of goods—pays for the bill.

Mr. UNTERMYER. That goes into consumption, and the bill discharges itself.

Senator REED. I think we understand that particular fact. Can you go back to my question, Mr. Stenographer, at the time that Senator Nelson began to ask questions?

(The stenographer read the question referred to by Senator Reed, as follows:)

You propose to create a system here by which banks are to get money, and they can get it only upon that class of paper?

Senator REED. You have got a system now by which banks can issue money based upon acceptances. I will use that for the mere sake of shortening the question. You say acceptances. It would necessarily follow, would it not, that acceptances would have a utility that ordinarily promissory notes would not have?

Mr. UNTERMYER. Yes; the class of acceptances to which Senator Nelson refers would have a utility and are of a higher order than the ordinary promissory notes.

Senator REED. Would not the result of that be just as Senator Hitchcock indicated, to force the commercial world to insist upon acceptances?

Mr. UNTERMYER. Not necessarily.

Senator REED. Would not that be the inevitable tendency?

Mr. UNTERMYER. I think that would be the tendency and that would be the natural growth and that would be a blessing to the country, because it would release this vast amount of immovable book accounts.

Senator REED. If that is true, then why was not Senator Hitchcock absolutely correct when he indicated by his question that instead of the merchant going to his local banker, as he does now, and securing money from him to discount the bills and transacting the business at home, the wholesale house having begun to exact acceptances, would put those acceptances in their banks in the home cities and thus transfer that portion of the business from the country banks to the great metropolitan institutions where the factories are situated.

Mr. UNTERMYER. Because the home merchant, in like manner, in selling his goods, would get some evidence of debt which he would put in his bank, and his bank would give him the money in that way instead of on his note; instead of saying to the home bank, "I have so much in open account," he would say to the home bank, "Here, I have got so much representing sales I have made."

Senator REED. That implies, then, the extension of this system clear up until you finally reach the farmer, who, instead of buying his goods upon credit, must sign an acceptance?

Mr. UNTERMYER. But that is the same credit; he is buying them on the same credit. He is not getting less credit; he is probably getting more.

Senator REED. Is there not a great deal of difference in the practical application, in the first place, of these two men, one of whom has been dealing with his merchant and has been carried along in an open account, and every once in a while when he sells a load of hogs or a carload of cattle he comes in and squares up, and another man who has got an acceptance in the bank and he must meet it at a given time?

Mr. UNTERMYER. It is the best thing that could happen to the country merchant.

Senator REED. I am not speaking of the country merchant, but about the ultimate consumer.

Mr. UNTERMYER. But it does not hurt the farmer, because if he is going to get six months' time to pay up he will get six months' time in the form of an acceptance.

Senator REED. Let us see if it really does not hurt him, now, in practical operation. I am not talking about the hurt in dollars and cents; but I say, again, is there not a great difference between the farmer who knows that the merchant is extending him a credit and to whom he owes an account that he expects to pay within reasonable limits, but there is not absolutely any fixed date, and he goes in and pays it at his convenience, and that farmer who has signed an acceptance, that comes due on a certain date, and that acceptance has gone into the local bank, and the local bank has sent it on up to a reserve bank so that when that day comes around he must have that money; is there not a big difference in the two men?

Mr. UNTERMYER. In the first place——

Senator REED. Maybe you never owed a grocery bill. I have.

Mr. UNTERMYER. I decline to commit myself. [Laughter.]

Senator REED. Every man has a right to his constitutional privilege [Laughter.]

Mr. UNTERMYER. In the first place it does not follow that every bill from a country merchant is going to be represented by an acceptance, any more than that is so in other countries. In the next place when the merchant goes——

Senator REED. Then would you understand that that is not the system followed?

Mr. UNTERMYER. No; it does not follow at all, because in any system there is a certain proportion of goods to be canceled in the way of open accounts, everywhere, and it does not follow that every transaction is going to be represented by an acceptance; but at present the local merchant goes to his bank and borrows money, and he tells his bank, "I have so much invested in my business and so much in accounts." He can not borrow up to the limit of these accounts, for every dollar he has invested or anything approaching such a limit; he can borrow only a certain proportion in that way. If he had half his sales that are now in book accounts represented by documents, he could get more money than he could get to-day.

Senator REED. That might be a great misfortune to him.

Mr. UNTERMYER. It is a kind of misfortune we are trying to provide for by this bill. It is the kind of misfortune that gives the people money to do business. But if we can come back to this discussion, the point we are discussing is this: Here is a bill that provides that reserve banks may rediscount certain kinds of paper which nobody can possibly contend is commercial paper.

Senator REED. I think you are right about that.

Mr. UNTERMYER. That is the point. It is not a question of criticizing every other system, but of finding some way to make this work.

Senator REED. You want to confine it to this limited class. You would like to have a phraseology that would limit the issues of money to commercial bills, as you define them?

Mr. UNTERMYER. Not entirely. There has been a great hue and cry since this discussion has been on about the supposed danger of issuing currency against cotton, grain, etc. There was some suggestion when this bill was in the House that it should be so amended that currency could be issued against cotton and grain in responsible warehouses. The unfounded criticism was made that it would be revolutionary and that it was reckless finance to permit a certain fixed amount of currency to be issued for cotton and grain in warehouses that is to go into consumption within a limited course of time. There has been, however, no hue and cry about, but a general acquiesence in, the proposition in the bill to issue currency based upon pretty much everything else on earth that is not anything like as liquid or as legitimate a subject of currency issue as cotton and grain evidenced by warehouse receipts.

Senator REED. Yes, I thought I had here a mark, but I see I have got the wrong copy. The very thing that you are talking about now I underscored to call attention to it when my mind was directed to it; but I want to ask this further question, I know the language is loose: If we were to limit the issuance of money upon the kind of security we have been just discussing, can you tell me what per cent there is of the present $8,000,000,000 of bank loans that is represented by that class of paper which you denominate commercial paper?

Mr. UNTERMYER. I do not know.

Senator REED. It is very small?

Mr. UNTERMYER. I should not say so. I should say it is quite considerable, when we exclude the financial transaction on the stock exchange. Of the balance, I should say it was very considerable. At the outset of this discussion I suggested that the Federal reserve banks should not be restricted entirely to the rediscount of paper that would be the basis of currency issue. We are talking about what might be the basis of currency issue. As the bill now stands, they can only rediscount paper that will be the basis of currency issue. If you make the basis of currency issue any note or bill of exchange drawn for agricultural, industrial, or commercial purposes, or the proceeds of which may be used for that purpose, it will not take very long before the permanent currency issue in the country will be such that we will be stranded. You will not be able to issue any more money.

Senator REED. That phraseology is no limitation at all, is it?

Mr. UNTERMYER. I should say not. I should say it was an invitation to inflation, but it is a mere question of phraseology after all. It is not fundamental. I mean I do not believe that the framers of the bill intended to put it in that way.

Senator REED. You think, as a lawyer, under that bill, within the provisions of that bill the door would be open so wide that almost any kind of paper would be admitted?

Mr. UNTERMYER. Yes; I think that in the end the Government would find that it had issued currency for permanent improvements and for the purchase of land and for a lot of things, of a nature that could not come back, and that that currency the local banks would have to keep on rediscounting and renewing, and you would have the door closed to the issue of legitimate paper in times of need.

The CHAIRMAN. It would convert what was intended as an elastic currency into a permanent currency?

Mr. UNTERMYER. Yes.

Senator BRISTOW. Are you through, Senator Reed?

Senator REED. Yes.

Senator BRISTOW. There was a question or two I wanted to ask Mr. Untermyer before he went away. Speaking of these acceptances which the local merchant would ultimately have to take in order to change this system which has been suggested by Mr. Untermyer, as was brought out by Senator Reed, it would change the present local method of doing business so that when the farmer bought his bill of goods, instead of having a running account he would give an acceptance, and that acceptance would go into the bank and that would be due, and of course it would have to be paid or it would not be renewed?

Mr. UNTERMYER. It would probably be renewed. The local banks do not expect to have all their assets liquid. They only expect to have a certain proportion of them liquid.

Senator BRISTOW. That would have to be renewed, we will say. Of course, this would be a great inconvenience to the farmer, as you will understand, because he is accustomed to having a running account and paying his bills when, as Senator Reed says, he sells his hogs or his wheat or his cattle, and he holds his wheat until he has got a better market. He does not have to meet it to-day or next week. When he does, it is to his interest to dispose of his assets, and he gives this acceptance and it has to be met. He goes to the bank and he wants to hold his crop a little longer, and he gives his note, pays it by a note instead of by cash. Wherein is that liquid then, any more than any other note that is renewed?

Mr. UNTERMYER. He gives his note instead of giving this acceptance?

Senator BRISTOW. Instead of giving cash he pays in a note. Wherein is that acceptance any more liquid than if he had given a note in the first instance and renewed it?

Mr. UNTERMYER. You are assuming that he has given no acceptance at all.

Senator BRISTOW. No; that he gives an acceptance and it was due in 90 days.

Mr. UNTERMYER. If people are going to pay their debts in notes, you will not have much of a financial system based on that.

Senator BRISTOW. That is just why I say if the customer has not the money when the acceptance is due.

Mr. UNTERMYER. Then the bank has to take up that acceptance and carry that farmer.

Senator BRISTOW. The farmer comes in and he has not sold his crop yet, or his hogs, or it may not be matured, so he gives the bank a note to pay this account that is due, and the bank does that instead of forcing him to sell on probably a low margin. Wherein is that acceptance in this commercial transaction any more liquid than a note in the first place would have been?

Mr. UNTERMYER. Because the bank has had the benefit of that acceptance during all that time and has had the money out of it. He has to pay it back at some time, and the bank has had the money meantime.

Senator BRISTOW. How is that, when there was no money paid? It was simply a credit.

Mr. UNTERMYER. As I understand it, the merchant took the farmer's acceptance and drew on the farmer for the amount of that bill.

Senator BRISTOW. And he accepted it, due in 60 or 90 days?

Mr. UNTERMYER. And the bank took that to the reserve bank and got the money on it. It has had that money meantime, and if the farmer can not pay, the bank can get a new acceptance from the farmer and put that in the reserve bank and take up the old one, or it can withdraw that acceptance and carry the farmer.

Senator BRISTOW. It can either take a new acceptance or a note, as it pleases?

Mr. UNTERMYER. It seems to me we have given rather undue weight to this question of whether there shall be a note or an acceptance or an open account. The whole basis of the discussion is as to the character of paper for which currency shall be issued.

Senator BRISTOW. Yes.

Mr. UNTERMYER. It does not involve any such revolution in systems of doing business as we are discussing, because I quite appreciate that you can not bring about that sort of a revolution overnight, but it would gradually lead, in my opinion, to replacing to some extent the present method.

Senator BRISTOW. The custom now is that the farmer or the citizen, whoever he is—I will speak of the farmer, because he does carry an account, as a rule. He carries it with the local merchant. His wheat may have failed and he will wait for his corn crop to come on, or some later crop, or the merchant may have so many of these accounts, it being a dull year, business is slow, and so he carries him along. He goes to the bank and states the situation to his banker, which the banker knows quite as well as the merchant does, and he gives his note for money to meet his bills and extends the credit to his customer a little longer, and the banker helps him out. That is his business. That is what he is in business for. The note which the merchant gives to the bank you would bar as not fit upon which to base a currency, but if that had been in the form of an acceptance from this farmer, and then a renewed acceptance 90 days later, you would give it in that form the credit of being made the basis of currency?

Mr. UNTERMYER. I have not said that I would bar the note, but I have said the acceptance method offers the best way of reading more of a transaction on the face of the document. But apart from that we will assume that the merchant is giving the farmer a 12 months' credit under the present system. If he wanted to change the system, he might still give him 12 months' credit, and, if you please, he can take the 12 months' acceptance; and the bank that now gives him credit, knowing that he would not be able to pay for a year, would give him the same credit that it had before; that when that acceptance got to within 90 days of its maturity that bank would have something upon which it could get some money, whereas it would have to wait the whole 12 months under the other plan. It would always have this maturing paper. The substitution of the new system, while not interfering with the farmer's term of credit, would give the bank the opportunity of using its capital more frequently and more liberally than it does at present.

Senator BRISTOW. Of course I think that if you lived in the country, as we do, you would not entertain any such opinions at all as to the feasibility of such a proposition.

Mr. UNTERMYER. It is not an essential part of anything I have said.

Senator BRISTOW. I think you would abandon that just as readily as I would refuse to accept any such a theory and undertake to go before my constituents with it, as it would be very short lived.

Mr. UNTERMYER. Why is it that it works so well in other countries?

Senator BRISTOW. I do not know why it works so well in other countries. Unfortunately, I am not very extensively informed as to what they do in other countries; but I know what our people do and what they will not do, and you could not put any such a proposition through at this time in this country.

Mr. UNTERMYER. I do not think we have any such proposition. I have not suggested any such proposition.

Senator BRISTOW. I understood that you had.

Mr. UNTERMYER. What I said was that it would facilitate transactions of this kind and it is bound to come under this system.

Senator BRISTOW. If that is true and the people understand that that is bound to come under this system, this system will never go through.

Mr. UNTERMYER. It is in their interest that it should come.

Senator BRISTOW. That would be for you to convince them of. I would a good deal rather that you undertook to do that than that I should undertake to do it myself, though.

Again, you say that you think that a limited amount of cotton-warehouse receipts or grain-warehouse receipts would be all right, and I am not going to controvert that point with you.

Mr. UNTERMYER. That is not a new proposition, because there again the much-despised experience of the older nations is a guide to us, whether we like it or whether we do not.

Senator BRISTOW. In times past those who have suggested that a currency might be issued on warehouse receipts of grain have been very much ridiculed.

Mr. UNTERMYER. You do not think they ought to be, do you?

Senator BRISTOW. I think that the grain in the bin is a better security if it is put up than the note of the man who has the grain, because the man may sell his grain and not pay his note. If the grain is made the security, he can not sell it, and the one who has got the note has got the grain and the man both. It is better than his note, now, for any purposes. If the grain in the bin is good security in connection with a man's note—and I think it is better than the man's note—why is not the farm upon which the grain is produced a still better security than the grain?

Mr. UNTERMYER. Because that does not convert itself within a limited time. The grain goes into consumption.

Senator BRISTOW. But a mortgage on a farm is a better security than a mortgage on the products of the farm, is it not?

Mr. UNTERMYER. No; if the mortgage is sold, the evidence of debt simply changes hands, and nothing has gone into consumption with which to pay that obligation.

Senator BRISTOW. But the farm is the basis for continual producing, year by year, that which does go into consumption?

Mr. UNTERMYER. So is the merchant's factory the basis upon which he produces his goods; but would you issue currency upon a merchant's factory?

Senator BRISTOW. The factory may burn down; the farm will not.

Mr. UNTERMYER. Then you would not issue it on his land?

Senator BRISTOW. I certainly think that a farm mortgage, a good mortgage properly made, is a better security than any other.

Mr. UNTERMYER. It depends on whether it represents a commercial transaction or not. But I say that a mortgage on the farm is no security for a currency issue.

Senator REED. Are you through, Senator?

Senator BRISTOW. Yes.

Senator REED. I want to ask one question. I have heard all through that this bill shall be so drawn that money should be furnished for commercial transactions. That is a beneficent purpose. Is there any more reason why I should take care of the commercial transaction, transactions between merchants, than the transactions of all of the people?

Mr. UNTERMYER. The transactions in merchandise, as I have frequently said, cancel themselves, pay for themselves in a limited time. Transactions representing fixed property do not. They are permanent investments, while the other is a mere temporary shifting of credits, and the use of them in the course of trade. The currency representing the latter is issued and retired as occasion demands.

Senator REED. You did not catch the point of my question. I understand that you say one will pay off more readily, but I am talking about this thought: I have sat here for two weeks, and I have not heard anybody propose a currency having for its ultimate object the benefit to any class of people except the bankers and the merchants. In drawing a bill ought we not to consider the benefits to the rest of the people?

Mr. UNTERMYER. Who is the rest of the people—the farmer?

Senator REED. Oh, no. You can take the banks out of a community and the merchants out of a community and have left everybody, and they are vastly in the majority, both in numbers and in importance and in usefulness. I do not mean that man for man they are more useful, but in the aggregate they are more useful.

Mr. UNTERMYER. Senator, I understand that we are to have a system of farm credits in this country, which we ought to have, corresponding to the continental systems. That system should be based upon an issue of debentures, taken in small amounts by investors all over the country; that is the ideal way of dealing with that subject. We certainly ought not to make it the basis of a currency issue to any substantial extent, because you would soon get to the end of your tether. You could not call in your farm mortgages every 90 days, and the result would be that the credits would pile up and the notes would pile up until our ability to expand the currency for temporary needs would be gone. I do not mean to imply that a system of financing farm mortgages is not as important as the other. I think it is quite as important, if not more so. But it must be differently dealt with.

Senator REED. I am not talking of inflation. I am talking about this one idea, that everybody's mind must be centered upon the thought that we ought to get a currency system that is a good thing for the banks and we ought to get a banking system that is a good thing for the banks. Incidentially, we ought to benefit the merchant. With both of these ideas I am in hearty accord, but I am just wondering why somebody did not discuss this bill from the standpoint of direct benefits to the rest of the community.

Mr. UNTERMYER. I do not see how you can benefit the merchants of the country without benefiting the rest of the community, and I do not see how you can increase credits and make them more liquid and enlarge the business of the country and furnish the means of doing that business at its full capacity without thereby benefiting every class of the community.

Senator REED. That is the old tariff argument, that if you take care of the manufacturers they will take care of the rest of the country.

Mr. UNTERMYER. No; I am not in sympathy with that old argument. I am a Democrat.

Senator HITCHCOCK. You were unable to give Senator Reed any answer to his question as to what proportion of the $8,000,000,000 of bank loans come within the definition of commercial paper? You are not able to do so?

Mr. UNTERMYER. Certainly not; I have not the remotest idea.

Senator HITCHCOCK. Have you any estimate as to the amount of additional currency which this country requires at any time?

Mr. UNTERMYER. No; I do not think I know enough of the statistics on that subject to be qualified to do anything more than make a wild guess.

Senator HITCHCOCK. Do you think it requires any additional currency, any increase of the volume of currency?

Mr. UNTERMYER. Yes.

Senator HITCHCOCK. On what do you base that, compared with any country in the world?

Mr. UNTERMYER. I base it on the periodical stringency of the market and the inability to get money and the spasmodic way in which discounts move in this country; they are different from that of any other country in the world.

Senator HITCHCOCK. Do you know any country in the world that has the per capita of circulation that we have?

Mr. UNTERMYER. I have not looked at those statistics for a long time, Senator Hitchcock, and I can not state.

Senator HITCHCOCK. I will assume that there is no country in the world that has our volume of circulation per capita.

Senator SHAFROTH. Except France.

Senator HITCHCOCK. France has not.

The CHAIRMAN. France has more. I think it is three times as much, or four times as much.

Senator HITCHCOCK. I would like to see those figures.

The CHAIRMAN. I put them in the record for your information, and you will find them, I think, on page 265.

Senator NELSON. You must remember that the use of taxation in other countries is not as great as in this country.

Mr. UNTERMYER. In England it is more broad than with us.

Senator HITCHCOCK. You believe in a flexible and elastic currency?

Mr. UNTERMYER. Yes, sir.

Senator HITCHCOCK. That is one reason you favor this bill, or something like it?

Mr. UNTERMYER. I favor this bill in its fundamentals.

Senator HITCHCOCK. What degree of fluctuation do you think is necessary? What per cent of fluctuation from maximum to minimum?

Mr. UNTERMYER. I have not gotten down to a study of the figures. Of course it is more the creation of confidence than it is the requirement of additional circulation, after all. The knowledge that credits can be made liquid is one of the things we so much need in this country.

Senator HITCHCOCK. What would be the effect, then, say, within 90 days, of increasing our circulation 10 per cent?

Mr. UNTERMYER. You mean under this bill?

Senator HITCHCOCK. No; any scheme that the country might adopt. What would be the effect of increasing the circulation 10 per cent?

Mr. UNTERMYER. In normal times I do not know that it would have any appreciable effect. It would not be availed of under the bill unless it were needed. At one time more would be required and at another time less.

Senator HITCHCOCK. Would it have any effect on credits?

Mr. UNTERMYER. It would make them more elastic, yes; the knowledge that the credits are there.

Senator HITCHCOCK. Do you think it would have any effect on interest?

Mr. UNTERMYER. I think it would make interest rates cheaper.

Senator HITCHCOCK. Would it have any effect on the stock market?

Mr. UNTERMYER. Under this bill I do not believe the stock market is going to be helped; I think it is going to be hurt temporarily so far as speculation is concerned. All this money is going to be taken out of the stock market. This phase is fully discussed in the report of the Pujo committee and is supported by complete data.

Senator HITCHCOCK. Assuming that the stock market is going to be hurt after the system is once adopted, do you think the prices of the stock market would be affected as the currency inflates or contracts?

Mr. UNTERMYER. No; I do not think the money for speculation will be available.

Senator HITCHCOCK. Do you think the prices will be affected by expanding or contracting this currency?

Mr. UNTERMYER. You mean the prices of merchandise?

Senator HITCHCOCK. Yes.

Mr. UNTERMYER. No.

Senator HITCHCOCK. Generally, the price level of things?

Mr. UNTERMYER. I do not think it will have any effect on the price level of things, except to make business more settled and credits more reliable.

Senator HITCHCOCK. Is it not true that all economic writers attest the fact that to expand the currency expands credits and increases prices, and that a contraction has the effect of contracting currency and depressing prices?

Mr. UNTERMYER. I think it depends on conditions under which the expansion or the contraction takes place. If it is legitimate, and if the expansion is accompanied by sound business and is brought about by expanding business, it does not increase prices. If the expansion is artificially brought about by undue ease with which credits are obtained, it may increase prices.

Senator HITCHCOCK. What would be the effect in this case: Suppose you have seven men that control the rate of interest. Twelve regional banks must pay that money. What possible effect do you think our action might have? Suppose they increase the rate of interest from one-half of 1 per cent up, say, to 5 per cent, what would be the effect on the country?

Mr. UNTERMYER. It would depend on whether the country needed the money so badly that it had to pay the interest. Either jacking the price of interest up or jacking the rate down is not going to have any great effect unless the money is going to be of use. If the money is a drug on the market, if the banks can not utilize it, if business is slack and the merchants do not need it, or if these men stand here and say, "We will let you have money cheap," we will not add to the inducements of the people to take money. They will take it as the demands of commerce require them to take it.

Senator HITCHCOCK. Is it not true that in Great Britain the sole resource of the Bank of England to increase its supply of gold and maintain prices is——

Mr. UNTERMYER. To bid for money.

Senator HITCHCOCK. To bid for money.

Mr. UNTERMYER. That is only for the purpose of attracting gold.

Senator HITCHCOCK. But is it not a fact that the Bank of England, by simply raising or lowering the rate one-half of 1 per cent, can affect the stock market?

Mr. UNTERMYER. No; not unless conditions warrant.

Senator HITCHCOCK. Does it not actually occur?

Mr. UNTERMYER. It occurs that they do it when conditions warrant. If they did it when conditions did not warrant, nobody would pay any attention to it.

Senator SHAFROTH. World prices have a bad effect on the circulating medium of our country.

Mr. UNTERMYER. Yes.

Senator HITCHCOCK. I want to ask you whether or not you consider it safe to place in the hands of seven men the enormous power to control the interest rate, practically without any limit, for the whole banking community of the United States?

Mr. UNTERMYER. I do not concede that they control the interest rates, and I think that it is perfectly safe to put that power in men whom I believe will be the right kind of men. They are just as likely to be bad if selected by anybody else, and more so.

Senator HITCHCOCK. You say that they do not control the interest rate?

Mr. UNTERMYER. No.

Senator HITCHCOCK. They control the deposit of $250,000,000 of Government funds.

Mr. UNTERMYER. Control it in what way?

Senator HITCHCOCK. They can place it wherever they wish.

Mr. UNTERMYER. No, they can not; under the bill they must place it equitably.

Senator HITCHCOCK. They can place it in reserve banks and take it out of one bank and put it into another bank.

Mr. UNTERMYER. Under the bill they can only place it in equitable distribution.

Senator HITCHCOCK. They will control it.

Mr. UNTERMYER. They control it more now than they will under this bill. It is now controlled by one man under the present system. He can put it wherever he pleases.

Senator HITCHCOCK. They control the deposit of $250,000,000, and can take it out of one depository and put it in another.

Mr. UNTERMYER. But within the limits of the bill; that they must apportion it equitably.

Senator WEEKS. What does "equitably" mean?

Senator HITCHCOCK. I do not care to go on with that, except that it gives the board power over the regional banks. Now, then, it is proposed to issue United States notes without any limit under this bill?

Mr. UNTERMYER. That is right, too.

Senator HITCHCOCK. There may be $500,000,000 or there may be $1,000,000,000.

Mr. UNTERMYER. If they had a limit it would be an incentive to inflation, would it not?

Senator HITCHCOCK. We will say they only issue $700,000,000 to start with. It is only proposed, however, to begin with the retirement of national-bank notes, and when those national-bank notes are retired they will be replaced by United States notes controlled by this board.

Mr. UNTERMYER. $700,000,000.

Senator HITCHCOCK. So that then the whole currency of the country will be under the control of this board, except United States greenbacks and gold certificates.

Mr. UNTERMYER. I do not agree with that.

Senator HITCHCOCK. They control this issue of this $700,000,000?

Mr. UNTERMYER. They can only issue it when it is asked for. They can not simply say, "We are going to issue it." When the reserve bank comes and says, "We have a certain gold reserve, and we have certain security, and we are willing to pay certain rates, that you will fix," then they can issue it; but if the reserve bank does not need the money it is not coming there, and they can only issue in response to demand.

Senator HITCHCOCK. I think it is for the member banks to decide in all cases whether they need the money. They can refuse to issue it?

Mr. UNTERMYER. Yes.

Senator HITCHCOCK. They can make hard times by refusing to issue it?

Mr. UNTERMYER. I do not agree with you about that.

Senator HITCHCOCK. Can they not cause contraction by refusing issuance.

Mr. UNTERMYER. They can produce absence of further expansion.

Senator HITCHCOCK. So that in the hands of these seven men you propose to place the power largely to control the commerce of the country and control the prices of the country by giving them control of the interest rate?

Mr. UNTERMYER. I do not agree. I think that is a very——

Senator POMERENE. Do you mean that a bank can close its doors if it can not pay the rate?

Mr. UNTERMYER. It is a violent assumption to say that they have the fixing of the interest rate. If the rate is too high the member bank will not pay the rate. It is only when the member banks can make money and have special need of this currency that they will take it.

Senator HITCHCOCK. Let us assume the rate is excessive and the reserve bank refuses to take it. That limits the power of the reserve bank, and when its member bank applies for discounts it replies, "No; we have no funds."

Mr. UNTERMYER. It is not as much limited as it is to-day.

Senator HITCHCOCK. Please answer my question. That will be the inevitable result; the reserve bank will have to say to the member bank, "No, we have no funds," and the member bank will have to say to its customer, "No, we can not lend you money," and the men who needed the money to do the busienss of the country on would have to curtail their operations. The man who had the goods to sell will have to curtail his operations, and the men who had the corn to sell will have to curtail their operations, likewise the man who had the cotton to sell; and the men who had live stock would be compelled to market their stuff, because they could not carry it.

Mr. UNTERMYER. Yes; but not to anything like the extent to which they are obliged to do to-day. If you take all your premises and apply them to those conditions you will find that even assuming all you say, conditions are better under this bill than they would be to-day because to-day if the member banks have to refuse customers, they can not go and get back part of the reserves from their reserve banks and in that way increase their facilities and loan money to their customers; they have to stop. If there was not another dollar of currency issued under this bill the system would be better than it is to-day, far better, because the reserves that are now rigid and that can not be used are put within their grasp, so that the member banks have the use of those reserves.

Senator REED. When they are within their grasp and use they cease to be reserves, do they not?

Mr. UNTERMYER. No, because they are represented by liquid securities in the hands of the reserve bank.

Senator REED. So is every dollar that goes over a bank counter and loaned out on 30, 60, or 90 day paper represented by paper.

Mr. UNTERMYER. The present reserve is largely a humbug.

Senator REED. I agree with that.

Mr. UNTERMYER. A country bank sends on its reserves to New York City. Is that a reserve there for the country bank? Not at all. The New York City bank is allowed to loan out three-fourths of it, is it not?

Senator REED. I understand that that may be something of a——

Mr. UNTERMYER. It is a humbug from beginning to end.

Senator REED. I do not call it a "humbug."

Mr. UNTERMYER. It is very deceptive and misleading.

Senator REED. I did not intend to interrupt you, Senator Hitchcock.

Senator HITCHCOCK. I was only going on to say, suppose I am a dealer in cattle out West and the bank has been carrying me. I have some cattle and the bank is refused by the reserve bank on the discount of its notes. Then the bank is compelled to call me—the cattle dealer—to pay my paper, and I must market my cattle because these seven men in Washington have raised the rate of interest so high that the reserve bank can not take care of me.

Mr. UNTERMYER. I do not think that that is a fair deduction at all.

Senator HITCHCOCK. That is inevitably the case.

Mr. UNTERMYER. Just at present this cattleman, if his bank has not the money, can not get it either; and the bank can not go anywhere to get it. This will give them a place to go.

Senator HITCHCOCK. Throughout the West you will find banks that are independent—practically independent—of eastern concerns. They have got their own deposits; they are owned in the community; the directors are there; they are not compelled to go to any reserve bank and ask for the discount of paper. If they are not able to accommodate their own customers, they can go to a hundred different towns and procure discounts.

Mr. UNTERMYER. There is nothing in this bill that stands in their way of continuing to do that.

Senator HITCHCOCK. This bill, however, proposes to take 20 per cent of their capital away from them?

Mr. UNTERMYER. Ten per cent.

Senator HITCHCOCK. It proposes to require them to keep their reserve in a certain place, which they are now permitted to keep elsewhere, and when they have put it in this certain place they will have no claim upon these other banks where they now keep their reserves, and yet you favor a plan under which the individual bank can not of right demand a discount of its notes, and you favor a plan under which seven men here in Washington, the creatures of the President, can absolutely tighten the credits of the country to such an extent as to force property upon the market?

Mr. UNTERMYER. I favor it unreservedly, and I favor it because I believe it is going to make the assets of the country liquid and to give us a scientific system instead of a crude, barbarous system, and I can not see, Senator Hitchcock, the point in the argument that a bank that is independent now will not remain independent. If it is so independent now that it does not need the help of anybody else, it will remain much more so than it is to-day, and you have no right to assume—I can not understand why anybody should assume—in passing upon this bill, that it is going to be unjustly and despotically administered.

Senator HITCHCOCK. Are you not by this bill making it dependent upon the reserve bank?

Mr. UNTERMYER. No.

Senator HITCHCOCK. You make it dependent upon that bank for rediscounts.

Mr. UNTERMYER. On the contrary, I am giving back to that bank the chance to get two-thirds of its reserves back.

Senator HITCHCOCK. You are not giving it to it as a matter of right. It all depends upon the ipse dixit of the men who run the reserve.

Mr. UNTERMYER. It takes nothing away from it that it has as a matter of right now. By this proposition you are adding to the resources of that bank by giving it the privilege—assuming that the bank is going to be honestly managed by its own members, of which this man is one, you are going to give back to this man two-thirds of the reserves that are now put beyond him. You are going to increase the resources of that bank by reducing the requirement of reserve; and then of the now required reserve he gets two-thirds back. You say that formerly he could go and borrow from the bank where he had his reserves. That was not a matter of right either; that was a pure matter of privilege; and if his reserve bank happened to have the money in Wall Street, he would not get it.

Senator HITCHCOCK. But he now has his reserves in a number of different banks, as a rule. If he fails to get the proper accommodations from that bank, he removes his reserves to another bank where he will get accommodations. He not only has in New York City the choice of 30 banks, but he has the choice of three central reserve cities and 48 reserve cities to which to go.

Mr. UNTERMYER. He has to go somewhere.

Senator HITCHCOCK. Under this bill he has only one place to go, and when he goes to that place he gets nothing as a matter of right but only as a matter of favor.

Mr. UNTERMYER. Could you ever make it a matter of right?

Senator HITCHCOCK. I think so. That is one of the discrepancies of this bill. It must be made a matter of right for the individual American banker to go and get what this bill seeks to give him—the privilege—and not leave it optional with somebody else.

Mr. UNTERMYER. How would any system be workable that way? Just consider that for a moment, will you? Here is a reserve bank under the administration of the member banks, of which it is a part. It has participated in electing this board; 6 out of 9 members are its nominees, and there are going to be 12 regional banks; and if every bank joins each regional bank is going to have about 2,000 bank depositors there on an average.

Senator HITCHCOCK. I would go into that, but I think Senator Reed expects to go into this organization of regional kanks for the purpose of developing your idea, and I will not trench on that now.

Mr. UNTERMYER. All that I wanted to say in that connection was that you can not have a system that is so rigid as to say to the reserve bank:

> You have got to lend each man two-thirds of his reserves back.

Senator HITCHCOCK. Do you not thir k——

Mr. UNTERMYER. Somebody might not want the funds and they would be unused. There are times when certain industries require money and others do not. There are some banks with small capital and vast deposits, and others with large capital and small deposits, There are a thousand contingencies that could not be met or anticipated by such a rule. It would destroy any system.

Senator HITCHCOCK. You think then that an individual bank, no matter how well run, should not as a matter of right be able to go to the reserve bank and secure a rediscount?

Mr. UNTERMYER. How much of a rediscount?

Senator HITCHCOCK. My judgment is that the proportion should depend on its capital.

Mr. UNTERMYER. In other words, the reserve bank, according to your idea, would not even be entitled to its pro rata share of the money it puts in in the way of reserve. According to that, if half the banks in a regional bank were willing to avail themselves of that privilege and wanted it, and the other half did not, what would the regional reserve bank do with the other half of the money? If it loaned that other half out, the next day another member bank might come along and say, "We want ours"; it would at other times have to leave a large part of its capital dormant. The capital of a bank is no criterion of its business or needs.

Senator HITCHCOCK. I am opposed to the creation in the banking world of imperialism. I think that the present system is democratic.

Mr. UNTERMYER. I am equally opposed to it and fearful of it, as you know; I think we are so near imperialism now in finance that we are trying to get away from it. This bill is going to try to take us away from it. That is why I am so ardent a champion of it with all its minor defects.

Senator NELSON. Would it not be safer, Mr. Untermyer, to leave these reserve banks to determine upon the amount of currency they wanted, and simply give this board the right to pass upon the securities they offer, and pass upon the commercial paper they wanted the currency on? Would not the regional banks be the best judges of what they wanted in that region?

Mr. UNTERMYER. You mean reserve banks?

Senator NELSON. And as to the amount of currency they needed, and if you left this question to the national reserve board to simply pass upon the quality of the paper they tendered for the currency they wanted, would not that be ample?

Mr. UNTERMYER. You mean to make the issue of currency compulsory on the part of the reserve board?

Senator NELSON. No, I mean let each reserve bank determine how much of this currency they want.

Mr. UNTERMYER. That would make the issue of currency compulsory on the part of the Government, would it not?

Senator NELSON. No, not necessarily.

Mr. UNTERMYER. If the reserve bank determines it wants so much currency——

Senator NELSON. It would not make it compulsory on the part of the Government, because the reserve board would have to determine on the commercial paper they tendered.

Mr. UNTERMYER. Assuming the commercial paper was all right, it would make compulsory on the Government to issue the currency, because these regional reserve banks wanted it?

Senator NELSON. Does not that commercial paper represent the trade and traffic and commerce of the country, and why should there not be currency to represent that business?

Mr. UNTERMYER. Then it does come down to this, does it not, Senator Nelson, that the proposition is that when a regional bank presents a certain amount of good commercial paper that the Government should be compelled to issue currency to it?

Senator NELSON. It indicates that in that region there is that volume of business and traffic represented by that paper, and why should there not be currency to cover that?

Mr. UNTERMYER. I should certainly think it would be rather a dangerous thing to make it compulsory on the Government to issue currency because the paper was forthcoming for the security of that currency. It would simply encourage a riot of expansion in a given region. The reserve bank members would say:

> We will go right a head and do all the business we can do, because the Government is bound when we present the paper to issue the currency.

Senator NELSON. Here is another point in connection with this bill which I want to direct your attention to.

Mr. UNTERMYER. I think it would be the worst kind of invitation to inflation.

Senator NELSON. Does not this bill ultimately throw the whole burden of gold redemption on the Federal Government instead of on the banks?

Mr. UNTERMYER. So far as the public is concerned, yes. But as between the reserve banks and the Government, the Government is only a guarantor and the principal debtor is the reserve bank.

Senator NELSON. Let us look at the facts, Mr. Untermyer. The reserve bank may, in place of gold, put in lawful money. That means greenbacks and silver dollars?

Mr. UNTERMYER. I do not agree to that proposition. I think that ought to go out of the bill.

Senator NELSON. That is in the bill. Now, they tender that for redemption. A man comes into the reserve bank and wants the notes redeemed. They tender greenbacks and silver dollars that is good redemption for the banks, but the man who gets the silver dollars and the greenbacks may not be satisfied. He may want the gold and he goes to the Government. So that the ultimate burden of redemption in gold is thrown on the Government under this bill, is it not?

Mr. UNTERMYER. It is if——

Senator NELSON. As it is framed now?

Mr. UNTERMYER. Yes; it is thrown upon the Government in that respect, and in that respect it has seemed as though the words "lawful money" ought to come out of this bill and that the redemption should be absolutely and unqualifiedly in gold.

Senator NELSON. Otherwise the burden is ostensibly assumed by the reserve banks, but is ultimately cast upon the Government?

Mr. UNTERMYER. I do not think there is any question about the justice of that criticism, Senator Nelson.

Senator HITCHCOCK. Mr. Untermyer, there is nothing in the bill, and you would not favor putting anything in the bill, to require the reserve bank to rediscount any amount of paper for any bank?

Mr. UNTERMYER. I would not; I would leave that discretion in the reserve board, because I have confidence in the Government's appointees.

Senator HITCHCOCK. I am talking now about the reserve banks.

Mr. UNTERMYER. Yes; I would not require the reserve bank by any rule to discount for any member.

Senator HITCHCOCK. You would permit it the option of refusing any member any discounts at all?

Mr. UNTERMYER. Yes.

Senator HITCHCOCK. Then, you also favor letting it discount any amount of paper for any member?

Mr. UNTERMYER. Yes.

Senator HITCHCOCK. So that would permit the grossest amount of favoritism to develop?

Mr. UNTERMYER. You are assuming that the member had the necessary collateral, and assuming that these men——

Senator HITCHCOCK. I am assuming that the man presents good collateral.

Mr. UNTERMYER. Assuming that these men, who can be turned out every few years, and three of the six men turned out by the reserve board at any time, are going to be recreant to their duty, then you are quite right. But you have no right to build any system on such an assumption. You can not start anywhere or get anywhere with any sort of legislation on that basis. Is it not true that in testing any system you have got to assume that the people who are going to act under the system are going to act under the law?

Senator HITCHCOCK. They would be entirely within the law.

Mr. UNTERMYER. They would be entirely within the law, and they are going to act conscientiously and they are going to act intelligently.

Senator HITCHCOCK. Then you would not favor putting checks on them?

Mr. UNTERMYER. Why, yes; you put certain checks upon them by this bill.

Senator HITCHCOCK. Where are the checks here?

Mr. UNTERMYER. In the proposition the reserve bank can not lend more than twice the amount of its reserve.

Senator HITCHCOCK. I am talking about the favoritism. What check is there against favoritism?

Mr. UNTERMYER. Oh, I might answer you by asking you what check is there against the United States Supreme Court, or against the Interstate Commerce Commission, or against any public body in any part of the world.

Senator REED. I will undertake to answer that by saying the checks of the Constitution, the checks of the statute; the certainty of impeachment if they deliberately violate the Constitution.

Mr. UNTERMYER. You have got the power of removal here.

Senator REED. You have got the power of removal here, I grant you that, but you have got something else than the power of removal with the Supreme Court. You have got the written law and the precedents of 1,000 years, and above all that and better than all that, you have got a spirit that permeates every part of our population, that the courts must do justice, and they have nearly always done it.

Mr. UNTERMYER. Undoubtedly, but still you have had more judicial legislation in the Supreme Court, and it has all been in the right direction; nobody complains of it.

Senator REED. I do not think the Supreme Court has ever gone very far away from the principles of the Constitution and the old common law of England.

Senator NELSON. Mr. Untermyer, what have you got to say about this feature of the bill, giving this board of seven men authority to compel one regional reserve bank to discount the paper of another reserve bank, whether they are willing to or not?

Mr. UNTERMYER. It is necessary——

Senator NELSON. Take a concrete case, for instance: Suppose New Orleans is the center of a regional reserve bank. They are hard up for money. Suppose this board here at Washington concludes that the reserve board at St. Louis, which is at the head of another regional reserve, ought to help out the New Orleans bank and discount their papers, whether they are willing or not, and suppose that the men managing that St. Louis bank felt as though they needed all their resources to accommodate their regional district. Are you in favor of giving this board here at Washington absolute power to say that at St. Louis they should be compelled to help out the New Orleans banks, whether they are willing or not, whether they felt that the conditions justified it or not to discount the paper of New Orleans?

Mr. UNTERMYER. I certainly am, and the restrictions of this bill, which I think——

Senator NELSON. What are the restrictions? In the first place, are they anything more than mere restrictions?

Mr. UNTERMYER. 1. That a bank must have the unanimous consent of all the members present. 2. There has got to be an emergency. I do not think unanimous consent ought to be needed. There is a great deal to be said on the other side of that proposition. You can not mobilize the reserves of the country in times of emergency without giving that power.

Senator NELSON. Why not leave, Mr. Untermyer, these regional banks in that matter the same as the constituent members of the bank to determine whether they discount the paper or not? The members that compose——

Mr. UNTERMYER. Because you will convert this from a reciprocal cooperative system into a competitive system the first thing you know. I understood that these regional banks were to be pipe-lined in this way for the purpose of being of aid in a comprehensive system.

Senator NELSON. And then you wish Washington here to pipe the funds of St. Louis to New Orleans if they thought proper?

Mr. UNTERMYER. If they were needed there.

Senator NELSON. In the discretion of this board?

Mr. UNTERMYER. Discretion must be lodged somewhere. You can not construct a currency system on a given set of rigid rules. The subject is too complex. Contingencies are bound to arise that can not be foreseen. You must have elasticity. That means discretion lodged somewhere. Senator Nelson, let me suggest this: In the first place, these regional banks are holding Government funds.

Senator NELSON. Yes.

Mr. UNTERMYER. The same result would be accomplished by the Government transferring its funds to where they were needed.

Senator NELSON. Yes.

Mr. UNTERMYER. So that it is dealing practically with its own funds. You can not conceive of a case when any regional bank would require any more money than the Government happens to have on deposit with these different banks.

Senator NELSON. Suppose you limit the bill, then, and say that they could compel it to the extent that the bank had Government funds to rediscount. What about that modification?

Mr. UNTERMYER. I would not be willing to assent to it, so far as my judgment is concerned, because I do not believe that such a scheme is going to be workable. For years the Aldrich bill was extolled because of the fact that it mobilized the reserves, and the only purpose of this provision is to mobilize the reserves. The banks did not object to mobilizing them permanently, so long as they controlled. Why do they object to this simple and temporary mobilization of the funds which leaves them in their localities until the emergency arises, mobilizes them where the emergency exists, and redistributes them in the localities whence they came when the emergency has passed?

Senator NELSON. But there was nothing compulsory about discount or rediscount or about becoming members in that bill. There was nothing compulsory in the whole scheme, either in the way of discount or anything else.

Mr. UNTERMYER. It was compulsory in the sense that it was a scheme for control by the banks, with the power of issue in the banks of the currency of the Nation, a thing that is repugnant to all ideas——

Senator NELSON. Is not this power here vested in this board of seven men?

Mr. UNTERMYER. I beg your pardon.

Senator NELSON. Is not this power here vested in this board of seven men?

Mr. UNTERMYER. The ultimate power to shift reserves by unanimous consent when an emergency arises, yes, but a power that is responsible to the people; these members are responsible to the people. Under the Aldrich system they were not responsible to anybody except their stockholders consisting of the banks, and I think that if it was a good thing to mobilize reserves permanently it ought to be a good thing now to mobilize them temporarily.

Senator NELSON. How could it be responsible here, except in a roundabout way. They are not Government officers; we could not impeach them.

Mr. UNTERMYER. They are responsible to the administration; the administration is responsible to the people for them. Every Government official, I assume, is in some way responsible to the people, and it is incredible, you know, that there should be such a thing as a genuine fear of the abuse of this great power. We can not proceed on any such principle; you could not write any bill on any such principle.

Senator REED. I do not want to interrupt——

Senator BRISTOW. If you are going to follow this up——

Senator REED. Yes. Just by way of introduction, I think the objection to the mobilization scheme of the Aldrich bill was that the people rather concluded that under that system all the money of the country would be mobilized by these banks into their own coffers and kept there.

Mr. UNTERMYER. This is a mere temporary expedient, and it ceases when the emergency passes. It is ideal, I think.

Senator REED. Of course, we all understand that under this bill the President of the United States could remove members of this board, and I am going to assume for the moment that the President of the United States in the future will always be, as I think he has always been in the past, without exception, a patriot; but Presidents have different views as to what is good for the country, and they respond to different influences. You say that it is inconceivable that a board should arbitrarily raise the rate of interest, for the reason that if they did arbitrarily raise it without some just cause, they would be subject to removal. But suppose——

Mr. UNTERMYER. It would also be ineffective, I said.

Senator REED. I believe you did; but let us deal with the one reason for the moment. Suppose that the President himself wanted the very thing done they did; then he would not remove, would he?

Mr. UNTERMYER. I think that is a fair supposition.

Senator REED. Is it not entirely conceivable that we should get a President sometimes who could be persuaded by shrewd and keen men, having great interests, that it was for the good of the country that expansion should be curtailed and the brakes put upon business?

Mr. UNTERMYER. Yes; I can conceive of such a thing, but I can not conceive of a rise in the interest rate by the bank under such conditions being in the least way effective, unless it was necessary——

Senator REED. That is the other reason, but sticking to the one road that we are traveling now, that is not only conceivable, but the fact is that the discretion to make this order would have to be vested in a human being, in the last analysis, who might or might not decide the question right.

Mr. UNTERMYER. There is no doubt about that. I think we will agree there, anyhow.

Senator REED. So that we get down to this proposition, that so far as raising or lowering the rates of interest are concerned, you would have a board appointed by the President, responsive to his will and likely to obey his suggestions?

Mr. UNTERMYER. Yes; I think that is a fair assumption.

Senator REED. You say that could not do any harm, because if you expanded the currency—I am coming to the other reason now——

Mr. UNTERMYER. I do not want to say unreservedly that a board of the character of which this board should consist would be responsive to the will of the President if the members believed it was contrary to the public interest. I do not think that the President's point of view would necessarily govern.

Senator REED. In all the history of this country that has happened since I can remember; I know of just one Cabinet officer who resigned because he did not agree with his chief, in regard to a policy, and in that event I think he resigned because he did not want to part company with his party more than he resigned because he did not agree with the President's idea of the silver question.

Mr. UNTERMYER. But, how many times have you known the President to ask improper influence of these high officials?

Senator REED. I have known the President to advocate policies—to be father confessor for all the other advocates of that policy, which I believed and which you believed, if you are a Democrat—and you say you are, and I believe it—were utterly inimical to the country. There were lots of good men who believed the other way, but it does not place the President above the point of an advocate.

Senator WEEKS. If the board were as subservient to the President as the majority in the House and Senate are at this time, he would not have any trouble in controlling it.

Mr. UNTERMYER. That is because he is doing good work and they are in sympathy with him.

Senator REED. No; the illustration is a fit one, because we fully understand it has happened more than once in our country that there have been two or three men even in the great independent legislative bodies who have gone to the White House for their inspiration and who have not had to report to a caucus when they came back; they just told them what to do and they did it.

Mr. UNTERMYER. They probably got good inspiration.

Senator REED. I do not know whether there is a question about that. The people of the country concluded the last time that they did not, and they frequently come to that conclusion. But we are getting away from the question.

I wanted to discuss with you the question of whether or not it would not be possible now, and very possible, to produce stagnation and partial paralysis of business through the changing of the interest rates. Let us assume this——

Mr. UNTERMYER. You mean the rate at which the reserve board says the Government shall issue currency?

Senator REED. Yes. Let us assume this condition, that we have barely enough money out to properly conduct the business of the country in normal times; that there comes a period, we will say, for illustration, of crop moving, when another $100,000,000 could be absorbed by the country; if it was put out it would facilitate the crop moving and business generally. That period having now arrived, the banks under this system come to the reserve board and say, "We think there ought to be $100,000,000 more money out," and the reserve board says, "We will not issue it for less than 10 per cent interest." It would not go out, would it, unless there was a great emergency?

Mr. UNTERMYER. It would not go out.

Senator REED. Then the business of the country would be contracted and would be to that extent interfered with?

Mr. UNTERMYER. It would be better off than it is to-day.

Senator REED. I am not talking about the comparison of this new bill with evils now existing, because if we have got, in making the new bill, to make one where we must choose between evils we would hardly be making the best bill. We ought to try in making a new bill to avoid all evils, if that is possible. I am just discussing the question now, and I think I have found an illustration that meets your statement that ordinarily it could not change and alter business, because if you said it was issued too low at the time the country did not need it, it would not go out; if it was too high at the time the country did need it——

Mr. UNTERMYER. It would not go out.

Senator REED. It would not go out; but the business of the country would be destroyed just to that extent.

Mr. UNTERMYER. Assuming that we have always got to meet the need of every emergency.

Senator REED. If you do not meet the needs of an emergency, and just in proportion as you fail to meet the needs of an emergency, you have failed to have that elastic currency and that elastic system which we are now trying to create.

Mr. UNTERMYER. What I said was that if you put the rate too high, if the money is not needed and you offer it, why, then nobody will take it—it is not effective—and that if the money is needed and you put it too low, why, then so much money will be asked for that you will have to put it high enough to meet the evil.

Senator REED. A man now running this would do this very thing. But let us assume that somebody does just the wrong thing. Let us reverse these conditions. We are talking now about issuing money; we are not talking about banking, because with respect to all banking there is a natural limit to what we can do, and the loans that they make. But we are talking now about going to the very source of everything, namely, the circulating medium. Let us assume that there is plenty of money out, so that there is enough there to do the legitimate business of the country, and that legitimate business could justly bear a rate of, say 4 or 5 per cent. Everything is prospering, and everything is inclined to be rather on the boom. There is plenty of money out; and the more money, the more the tendency is to boom. At that period, when the brakes ought to be put on and the rate ought to be raised, this board drops it to a half per cent. Do you not think more money would go out and speculation would become a little more active, new enterprises would be floated. Would not that happen if that was done?

Mr. UNTERMYER. If such an impossible succession of premises——

Senator REED. Is it impossible? Is it impossible now that we have got a period in out country——

Mr. UNTERMYER. We are getting into the realm of the improbable.

Senator REED. Is it improbable? I want to stick to that. We will just take a condition like we had here two years ago, going back to my illustration. You take a condition where we have had prosperity for several years; we have had good crops; we have had no financial disturbance; the money market is all right in Europe; we are building new roads; we are buying new automobiles; we are laying out parks and boulevards; we are building railroads; values are mounting; there is not a black spot in the sky; everybody has confidence; a large amount of confidence. That is bound to make itself felt. It influences most careful bankers; it influences the most careful business men; it would have its influence everywhere. Now, with that condition, would it not be entirely likely that that influence would make itself felt with this board of control, and that it would be inclined to make a low interest rate?

Mr. UNTERMYER. On the contrary, I should think it reasonable to presume that business men when they saw that condition would put on the brakes; and if they did not put on the brakes, there are brakes in the bill. One brake is that the reserve bank has got to have gold when it comes for money.

Senator REED. Coming down to the question which I think is fundamental, and that is that a system created ought to have some checks which are applied automatically, not by some human being's fiat or decree, but by the creation of a condition so that when the wagon is going too fast the brake is applied. You have indicated one way, namely, that the gold reserve of the bank, if put out at 33⅓ per cent, the scarcity of gold might put a limitation upon the amount of currency.

Mr. UNTERMYER. That is one brake. Another brake is that the reserve banks are composed of men selected by the bankers; that is brake No. 2. You have got more brakes in this system than in any other known system in the world, by the way. In other systems there is no brake.

Senator REED. Is there any other system where they just take notes of hand and issue money against them?

Mr. UNTERMYER. Yes, certainly.

Senator REED. Is there a limit in the law on the amount in every one of those systems?

Mr. UNTERMYER. I do not think so.

Senator REED. I am not sufficiently familiar with European banking to talk about it.

Mr. UNTERMYER. I do not think so, I do not know of any limit.

Senator REED. There is a limit, is there not, there, in the bank of England? Am I incorrect?

Senator SHAFROTH. By practice there is.

Mr. UNTERMYER. Not in the law.

Senator HITCHCOCK. In England the bank can not issue——

Mr. UNTERMYER. They have to have gold.

Senator HITCHCOCK. They can not issue currency unless the gold is on deposit.

Mr. UNTERMYER. In Germany the gold ratio goes up and down; there is no limit on the gold.

Senator REED. Speaking about the brakes in this bill—and I am speaking about a possibility, not of a probability—but it seems to me that as they are only required to keep 33⅓ per cent gold in their vaults, that it is possible to take that other 66 per cent, which is a credit, turn it into cash, loan it out again, take out 33⅓ per cent, turn it back into cash, and let it out again, so that there is a possible expansion in this bill that would make it so that we could have about three times the amount of currency that we have now.

Mr. UNTERMYER. Let us see——

Senator REED. Of course, now, I am talking about possibilities. I assume that the men handling the system and that this Government board would exercise a wise discretion, but in framing the law we have got to frame it not only for the wise and prudent and the patriotic, but as fair as possible for the foolish, the unwise, and even criminal.

Mr. UNTERMYER. But you must have a discretion lodged somewhere. Just consider the brakes of this system. In the first place, there is the member bank; that is a brake upon the borrower. Second, there is the character of the securities; that is the brake upon the borrower at the source, the member bank. Then, there are the associates of that member bank, in the reserve board, who can sit there, and who constitute a brake upon their member banks, and who are quick to see whether the member bank is being caught by some wild inflation, because their own interests are involved. They are not going to let him run away with their money and imperil their system. Then, you have got the gold reserve as a brake.

Senator REED. That is an absolute brake.

Mr. UNTERMYER. Then, you come up to the Federal board, and you have a brake there. It seems to me you could not have many more without making the system——

Senator POMERENE. They are subject to removal by the President?

Mr. UNTERMYER. Yes.

Senator REED. What about this idea that when a certain amount of this currency has been issued that no more shall be issued unless there is a greater gold reserve deposited?

Mr. UNTERMYER. The difficulty about that would be that if you put a limit in the bill, when the limit is about half reached it will lead to inflation, because every bank in the system, fearing that the limit may be reached, will go for more and get its share before the limit is reached and will take out currency it does not need. That was the objection to the original limit.

Senator REED. It would have to turn it back pretty soon.

Mr. UNTERMYER. That was the original objection to the $500,000,000 in the bill. I think it offered a premium upon inflation. That was the objection I had to it. I so expressed myself at the time and urged the change.

Senator REED. Then there is danger of inflation even by these wise bankers. If they could get it a little quicker, would they take a chance and inflate it some?

Mr. UNTERMYER. You can not have any human system without any danger of inflation.

Senator REED. You can have a system without danger of inflation. Of course if you had a gold dollar up for every paper dollar there would be no danger of inflation there.

Mr. UNTERMYER. Unless there was some sudden discovery of gold in the world that would increase the amount very largely, then you would have inflation.

Senator REED. Certainly. We might have that now, sure, if we had the gold.

Senator NELSON. In a good many countries they issue bills to the extent of the gold they have, but they generally require 50 to 60 and up to 70 per cent of gold for every 100 per cent of paper.

Mr. UNTERMYER. Yes.

Senator NELSON. That is, they can issue bills to the extent of the gold, but they generally require 50 to 60 and even 70 per cent gold for every 100 per cent of paper.

Senator BRISTOW. On that point I want to ask some questions.

Senator NELSON. If you will allow me——

Senator BRISTOW. Certainly.

Senator NELSON. There is the safety of it, because their paper is simply credit, while gold represents real value. If you base it on gold it represents industrial, commercial growth; its base is substance. While if you base it on anything else it is piling credit on credit; that is all it is, is it not, Mr. Untermyer?

Mr. UNTERMYER. That is the economic view of it; certainly.

Senator NELSON. The sound view?

Mr. UNTERMYER. Certainly.

Senator BRISTOW. Mr. Untermyer, you declared positively in favor of compelling one regional bank to discount the paper of another regional bank?

Mr. UNTERMYER. Under the limitations of the bill.

Senator BRISTOW. Is there any discretion at all with the bank as to whether it shall or shall not?

Mr. UNTERMYER. It should not be discretionary, if you want to mobolize the reserves.

Senator BRISTOW. Why do you compel one regional bank to rediscount the paper of another regional bank and refuse to compel the regional bank to discount the paper of a member bank?

Mr. UNTERMYER. One rests upon the basis of the public interest, and the other rests largely upon a private transaction; that is a very different thing. You have to get a cohesive, cooperative system, and if you are going to have 12 regional banks in the country, each simply confined to its own region, and not in a position where it would be compelled to help out the general system, you are not going to have a system at all—you will have 12 competitive systems.

Senator BRISTOW. Then, to take Senator Nelson's illustration: If, in the judgment of the member, the New Orleans bank ought to have a part of the revenues or the moneys——

Senator NELSON. Of the central bank.

Senator BRISTOW. Of the central bank; why, the St. Louis bank is compelled to discount those papers. That is in the public interest, because the people at New Orleans need it in the judgment of the board more than the people at St. Louis need it?

Mr. UNTERMYER. Because the whole financial conditions of the country require it, not because New Orleans needs it, particularly.

Senator BRISTOW. The financial condition of the country require it because New Orleans does need it more than St. Louis, in the judgment of the board here in Washington; is not that true?

Mr. UNTERMYER. You may put it that way.

Senator BRISTOW. The member bank goes to the regional bank for a discount because the people in its community needs it?

Mr. UNTERMYER. Yes.

Senator BRISTOW. The regional bank refuses because in its judgment they do not need it, or for any other cause that it may see fit?

Mr. UNTERMYER. You mean, it may do so, not any conceivable case of doing it unjustly?

Senator BRISTOW. It may do so whether it is unjustly or not; it has the power.

Mr. UNTERMYER. If it is justly, you have no complaint. It is only the power to do it unjustly?

Senator NELSON. It can do it without assigning any reason.

Mr. UNTERMYER. In effect, unjustly; that is your complaint—that it has a discretion which would enable it, in effect, to unjustly refuse an accommodation; if it refused justly you would have no complaint.

Senator BRISTOW. You put in the word "unjustly," I did not. That part of my question you interpolated. I suggested that the regional banks had the power to refuse rediscount.

Mr. UNTERMYER. Yes.

Senator BRISTOW. For a member bank.

Mr. UNTERMYER. Quite right.

Senator BRISTOW. And this for any reason. It might think that the condition of the member bank down at Anthony, Kans., we will say, did not justify extending further credit, because there had been a drought.

Mr. UNTERMYER. Any reason that the reserve directors thought was sufficient.

Senator BRISTOW. Because there had been a drought in the vicinity of Anthony, Kans., this board might refuse to rediscount this paper which the bank has taken and which the bank is willing to stand for, and the regional reserve bank would extend credit to some other community where it had a different opinion as to the industrial conditions. You are placing it within the hands of the regional reserve bank to pass upon questions of that kind, are you not?

Mr. UNTERMYER. Certainly.

Senator BRISTOW. But you refuse to give the same discretion to the regional banks as to discounting the paper of another regional bank?

Mr. UNTERMYER. Yes; because that is a necessary part of the system in its own interest, as well as others.

Senator BRISTOW. The relation of the regional bank to the region is the same, or practically the same, is it not, as the relation of the member bank to the member's region—that is, to its community?

Mr. UNTERMYER. No; that is just where we differ, sir. The regional bank has a distinctly public function. In the first place it is getting the currency of the Nation to help it out in its operations; in the next place, it is getting the credit of the Government back of it;

and, besides that, it is getting the Government's funds in its care. It has an entirely different relation to the public from that of the member bank to the regional bank.

Senator BRISTOW. You say it is getting the currency of the Nation—that is, on deposit?

Mr. UNTERMYER. No; the Government is issuing currency to that bank.

Senator BRISTOW. But that bank hypothecates for that currency securities which it receives from the member banks, does it not?

Mr. UNTERMYER. Certainly.

Senator BRISTOW. So that bank can hypothecate the securities from the bank from Anthony, Kans., for Government currency just the same as it could the securites of another bank in its region?

Mr. UNTERMYER. Presumably.

Senator BRISTOW. You will give to the regional bank the power to say whether or not this Government money which the Government issues, which it has not any interest in, except as trustee to pass it on from the Government to the member bank—to say whether this community shall have the currency or that community shall have the currency, even though the same class of securities are submitted from each community.

Mr. UNTERMYER. Yes; because presumably you have got to put the power somewhere. When the banks come in for rediscounts, somebody has got to pass on it. I do not know of any human, civilized system that does not lodge the power somewhere. Where could you lodge it better or more fairly than with the people who are to be accommodated? The banks themselves are passing on it. These men who are exercising their discretion are the nominees of the bank at Anthony, Kans. It has named them.

Senator BRISTOW. I understand that. I won't invade that field, because I think there is nothing more preposterous than the vision here that some of you gentlemen have that the banker at Anthony, Kans., is going to name this board. He is not going to have any more to do with it than the delegate who used to come up from the township to the county convention had in nominating his county ticket; that was all fixed before he got there; and this board of directors will be elected before the representative of this Anthony banker ever gets to St. Louis.

Mr. UNTERMYER. That is not the way the bill reads.

Senator BRISTOW. That is not the way the bill reads, but it is the way it will work, and anybody who has had any practical experience in American affairs must know that that is true.

Mr. UNTERMYER. Every bank has as much to do with that as every other bank.

Senator BRISTOW. And every delegate to the convention——

Senator NELSON. I think the principle Senator Reed advocated applies very properly here, and that is that it should not be left to the men; that it should be left to the law.

Senator BRISTOW. That is exactly what I am trying to get at.

Mr. UNTERMYER Let somebody try to sit down and try to write that kind of a bill, and see how far he will get

Senator BRISTOW. Some of us may undertake that before we get through.

Mr. UNTERMYER. Then we will have lots of chances to put holes in it.

Senator BRISTOW. That is right; I believe in that.

Senator REED. That is what we are here for; we would rather find the hole now than a year from now.

Senator BRISTOW. Why should not the law provide a means by which the banker at Anthony, Kans., could go to the Government himself with his securities and get the currency instead of having to have this extra, unnecessary machinery of a regional bank created in order that he might do it?

Mr. UNTERMYER. Well, because it would be a very dangerous thing.

Senator BRISTOW. Dangerous in what respect?

Mr. UNTERMYER. If you will try to conceive of such a condition, I think it will occur to you how dangerous it will be and how impossible. There are 26,000 banks in the United States. What would you do, have agents in the localities, so that a man would be subject to the whim, if you please, of a local agent of the Government? Instead of having a board of his own selection to pass upon his rights, he would have some local agent. That is all it would amount to.

Senator BRISTOW. We will see about that.

Mr. UNTERMYER. Then, again, what sort of security would the Government have? It would have the security that the man presented, indorsed by this bank at Anthony, Kans., while now it has back of this issue the responsibility of the reserve bank and its assets and its capital; it has the gold behind it and has a variety of other securities behind it to make it safe. It would be a mighty unsafe thing.

Senator BRISTOW. Well, I will suggest a question or two along that line, but before I do that I will say this: A number of times you have referred to the gold reserve as though there was a gold reserve required of these regional banks, when, in fact, there is not. It is gold or lawful money in the bill, and they do not have to have a dollar of gold.

Mr. UNTERMYER. I agree with that criticism, except that of course they answer the argument on the other side that under the act this lawful money has got to be kept on a parity with gold.

Senator BRISTOW. And the Government has the burden of keeping it there, and the bank has not.

Mr. UNTERMYER. Which is all wrong; it ought to be actually gold.

Senator BRISTOW. But, then, when you are defending the bill——

Mr. UNTERMYER. I have not defended every minor feature of it.

Senator BRISTOW. I do not think that we should assume that this bill required gold reserve when it does not, because that would very greatly strengthen it, in my judgment, if lawful money was stricken out as you suggest it should be; but it is not.

Senator SHAFROTH. Do you not think that the 33⅓ per cent which is provided to be in gold——

Senator BRISTOW. Gold or lawful money?

Senator SHAFROTH. Gold or lawful money.

Senator BRISTOW. Gold or lawful money; but that is not gold. Greenback is lawful money, and the Government has not maintained greenbacks.

Senator NELSON. It might be a silver dollar.

Senator SHAFROTH. Let me see if there is not a reason for that, and whether there is not a pretty good reason for it.

Mr. UNTERMYER. I know there is a reason.

Senator SHAFROTH. We have now national-bank currency, and that is redeemable at the banks in lawful money, and why? Because in times of stringency—times where they are making a raid upon the Treasury, you will have simply a more limited amount of money to make the demand on them, and by reason of that you will have less chance of maintaining your gold reserve.

Mr. UNTERMYER. It is wrong in principle.

Senator SHAFROTH. Let me see whether it is. Let me explain, in order to try to get the theory upon the other side. Suppose you have a nation that has got a gold reserve for all of its money of $100,000,000, and suppose it issues directly money like the greenbacks of $100,-000,000, and then you have got a subordinate currency something like that or like national bank notes of $100,000,000. You have got a demand upon that gold reserve ultimately of $200,000,000 against $100,000,000, but the direct obligation of the Government is only upon the $100,000,000 which it has issued in the shape of greenbacks, and consequently in times of stress, when they present this bank currency it says, "All right; we will take United States notes," and then when the United States notes come they can give me that in gold. Now, it makes one-half of the demand upon the gold in times of extreme emergency less than it would if they had $200,000,000 redeemable directly by the Government or by these banks; in other words, does it not put these banks in competition with the Government if they are all redeemable in gold, and the banks are required to redeem those in gold, for the purpose of getting gold and redeeming this paper?

Senator NELSON. The banks——

Senator SHAFROTH. In other words, it makes twice the strain if all of it is redeemable in gold than if half is redeemable in gold and the other half is redeemable in that paper money, and that paper money redeemable in gold. It seems to me that there has been a purpose in that way of issuing our national bank notes which was in order to make it sure that the Government was not to be strained, and therefore that the gold standard would be maintained, and if that is true and these notes are redeemable one into the other, and ultimately redeemable in gold, and the obligation of the Government is to maintain the parity of the metals in addition to that, it ought to be a safer proposition not to have your gold reserve exhausted under this system than you would in having them all redeemable in gold and letting the crowd rush in all at once and attack the gold reserve, with double the amount of money making demand upon it.

Senator BRISTOW. If there comes a rush in the country for gold and the lawful money for which gold has to be paid is discredited, and that is the only thing that could create a rush on gold——

Senator SHAFROTH. But the Government could do this: You see, the Government could retire the money in that way, and it would have less to retire and it could retire it and wipe out all currency with the $100,000,000, but if there was $200,000,000 outstanding redeemable in gold absolutely, it could not redeem it all, and thereby the chances of a depreciated currency would come much quicker.

Senator NELSON. I want to call your attention to how this worked under Cleveland's last term of office. The national-bank notes could be redeemed in greenbacks; that is true enough; but whenever there was a demand for gold abroad, there was a firm—Mr. Untermyer, you probably remember the name of it—Heigelmeyer——

Mr. UNTERMYER. Heidelbach, Ickelheimer & Co.

Senator NELSON. Yes. They made a business every week of going to the subtreasury with greenbacks and drawing the gold and shipping it over to Europe, and their operations became an endless chain. They did it week after week. You could read in the papers that that firm had taken out that much gold; and under the law they could not retire the greenbacks. There is a law preventing greenbacks being reduced below $346,000,000.

Senator SHAFROTH. Yes.

Senator NELSON. And to-day anybody can use those greenbacks as an instrument for drawing gold out of the Treasury without limit.

Senator REED. Do you not think that ought to be cured in this bill, Senator?

Senator NELSON. How? I think the banks ought to redeem this currency in gold and not throw the burden on the Government.

Senator REED. Is not that provision in regard to greenbacks that they could be retired if the Government wanted to?

Senator NELSON. If we made gold currency in the place of it, it might do.

Senator BRISTOW. To get back to the question that I spoke of, the reserve being required in gold or lawful money—if, as lawful money, the greenback was ever less than gold—why, that would be the money that the banks would use for their reserve, and because it would be cheaper to use it, the gold would disappear.

Mr. UNTERMYER. The Government is under obligation to keep it at parity.

Senator BRISTOW. But the burden is on the Government to maintain that.

Mr. UNTERMYER. Senator, I do not think we differ about that at all.

Senator BRISTOW. That is right. We will go ahead, then.

Senator SHAFROTH. Senator Nelson, is not there a law that provides that when the greenback is redeemed that it shall not be reissued except by the substitution of gold for the greenback?

Senator NELSON. I do not think so. There is a law you know—they went to work after the war, when they tried to fund our debt, and they kept on reducing it. They set out to redeem all the greenbacks, until Congress finally passed a law which stopped it and fixed it at the present maximum. If the Congress had not passed a law they would have had them all retired. That was the scheme in those days.

Senator SHAFROTH. I had an impression that there was a law that a greenback should not be reissued, unless——

Senator NELSON. They can not retire them, because they have no right to retire greenbacks.

Senator SHAFROTH. How?

Senator NELSON. They have a right to retire them to not below $346,000,000.

Mr. UNTERMYER. Senator Shafroth, I do not think the question of expediency in this form of bill—gold or lawful money—is anything like an offset against the discredit that the bill will get in foreign countries by having this provision in it; and, after all, the character of our money and the way it will be regarded and of our credit and our bills abroad depends upon the foreigner's view of our currency;

quite as much, if not a little more, than the view prevailing in our own country.

Senator SHAFROTH. I have always thought that money that was issued by the Government and made redeemable by the Government should be the specific thing—gold, or whatever your currency is; but wherever it is to be redeemed by something else, like a national bank, then it puts the bank in competition with the Government in the attempt to get gold, and that, of course, would have a tendency to make gold increase in price as compared to the circulating medium.

Mr. UNTERMYER. But, under this bill, the obligation is on the Government.

Senator SHAFROTH. No.

Mr. UNTERMYER. So far as the public is concerned, the obligation is on the Government. The gold is redeemable either at the office of the Treasurer in Washington or at the reserve bank; that gives the option to the man who holds the note.

Senator SHAFROTH. Yes; but the note circulating within the district is likely to be redeemed within the district; in fact, if they go to another district they have got to be sent back to the Treasury.

Mr. UNTERMYER. I know; but at the same time there is the option on the part of the holder of that note to go to the Government and demand his money.

Senator SHAFROTH. Of course he has got an option of doing that, but it is not the natural course of redemption that would occur.

Mr. UNTERMYER. That makes it a Government obligation.

Senator SHAFROTH. There is not any doubt but that in the end, if this note should ever go to a discount, the Government would have to come to the rescue, but the redemption is in the regional bank, because there the notes circulate; there the people live who have these notes. If the notes go out of the district, they are immediately sent back into the district, and there is the place of redemption, and if you have the banks having a gold reserve, and the Government having a gold reserve, you are going to pile up that gold reserve so that it will be impossible to issue——

Mr. UNTERMYER. Here is the obligation on the face of it–a Government obligation. There is no obligation on the face of this paper of anybody except the Government. It is a Government debt. But in that aspect I had intended to make the suggestion which I made earlier in the day, that the reserve banks should be required to keep their stock of gold at a central point—in Washington—credited to each reserve bank, but so that the Government, whenever a demand was made, can meet the demand out of the stock of gold belonging to that reserve bank. The gold should all be at one central point.

Senator SHAFROTH. That would relieve the gold very much, but I think it is very serious to have these two redemption points and make them have gold reserves to redeem in each.

Mr. UNTERMYER. But the Government will not have the gold, and that is the reason that the gold should be under its control, because the promise, the obligation to pay in gold is not good except in so far as the gold is there to meet that obligation. That is covered by gold to a certain proportion. It is not good if there is no gold there. Here is an obligation—a direct obligation of the Government to pay in gold, and if the gold or gold reserves are scattered through these different parts of the country, if a man comes along and says, "I want my money from the Government," they have not got it. The Bank of France has been hurt by the fact that it sometimes takes a week or two to give a man his money in gold. It has been said all over the world on that account that they really do not redeem in gold, whilst if you go to our Treasury or to the Bank of England you can get gold instantly.

Senator SHAFROTH. Their notes have never gone to discount.

Mr. UNTERMYER. No, because the crisis has not come, but at the same time a bill of exchange drawn on Paris does not sell like one drawn on London, and when people want to buy exchange for their international transactions, the Frenchman himself will go to London and buy exchange, because it sells better. Because they know that the gold is there.

Senator SHAFROTH. Let me ask you a few more questions.

Senator BRISTOW. I have a lot of questions here that I desire to ask.

Senator REED. I want to ask a question right now, because it is pertinent to just what was being said.

Senator BRISTOW. All right.

Senator REED. You say that there would be some difficulty under this bill or that there might be some difficulty about the gold reserve being scattered in 12 different banks. I want to call your attention right in connection with that criticism that this language in the bill—I refer to section 16——

Senator NELSON. What page?

Senator REED. Page 28, section 16, of the House bill—

that all moneys now held in the general fund of the Treasury, except the 5 per cent fund for the redemption of outstanding national-bank notes, shall, upon the direction of the Secretary of the Treasury, within 12 months after the passage of this act, be deposited in the Federal reserve banks, which banks shall act as the fiscal agent of the United States; and thereafter the revenues of the Government shall be regularly deposited in such banks, and the disbursements shall be made by checks drawn against such deposits.

I take that I am right in assuming that that makes it the absolute duty of the Treasurer of the United States to put into these reserve banks every dollar of our Federal money except 5 per cent of the funds for the redemption of outstanding bank notes, and except the gold coin that is now set aside back of the gold notes.

Mr. UNTERMYER. Gold certificates.

Senator REED. Gold certificates.

Mr. UNTERMYER. And how about the gold set aside behind the greenbacks—$150,000,000, is there not, there, against the greenbacks?

Senator REED. Is that sacredly set aside?

Mr. UNTERMYER. I do not know as to that. I think so. Is it, Senator Nelson, a specific fund? The act of 1900, if we have it here——

Senator NELSON. The gold standard act prescribes it.

Mr. UNTERMYER. I thought it was a special fund.

Senator REED. There may be that special fund.

The CHAIRMAN. It is a special fund held against the greenbacks.

Senator REED. I think that is right; and there would be, of course, excepted from the operation of this bill $1,100,000 held back of our gold reserves.

Mr. UNTERMYER. $1,026,000,000.

Senator REED. $1,100,000,000,every other dollar that we have got and every dollar we get has got to go into those banks.

Senator HITCHCOCK. You have got those figures wrong; that is $150,000,000.

Senator REED. $150,000,000 back of the greenbacks; there is $1,100,000,000 approximately back of the gold certificates.

Mr. UNTERMYER. Is it not $1,076,000,000?

Senator SHAFROTH. It was $1,086,000,000 this morning, but it has run up as high as $1,100,000,000 in the last month.

Senator REED. As I understand this, that takes in all those gold certificates?

Mr. UNTERMYER. I will say $50,000,000.

Senator SHAFROTH. It has gone up as high as $100,000,000 in the last month.

Senator REED. With those exceptions, whatever the exact figures may be, it all has to go into the banks?

Senator NELSON. Not that money.

Senator REED. I say "with those exceptions." He puts the Government in this shape, as to all moneys it gets—gold, silver, or paper—it has to take it over and put it in the bank. How could the Government have any money on hand for the purpose of redeeming, making good this currency, which we are putting into this bank's assets?

Mr. UNTERMYER. That is the criticism I have just made, Senator.

Senator REED. I was out. I did not understand that it had been made. I wanted, in connection with your criticism, to put that language in that way. It seems to me that the privileges of this bill manifestly are to be very carefully dealt with.

I want to ask you another thing in connection with it, aside from the mere question of redemption. Do you believe that there is any element of danger in making a law that compels the Treasury of the United States to disgorge its moneys and put them into this system of banks, willy-nilly, regardless of all circumstances and of all conditions?

Mr. UNTERMYER. I do not see any objection to the Government depositing its money in these banks.

Senator REED. I am not talking about whether the Government is wise and thinks best to do that, but I am talking about making the iron rule a law which says to the Treasurer of the United States:

> You shall not put that money into your vault, no matter what the conditions are; you must put it over here in these banks.

Do you think it wise to make a rule of that kind?

Mr. UNTERMYER. I see no objection to giving the Treasury some discretion in the matter.

Senator REED. I would certainly think it ought to have some discretion in that matter. Ought not the Treasurer to have that discretion which a proprietor has over that which is his own—to put it in there or not to put it in there, as in the course of discretion it ought or ought not to be so deposited?

Mr. UNTERMYER. It depends upon what you are doing. If you are establishing a system and you want to strengthen it, you want to give it all the funds that are available.

Senator REED. If you were in business and wanted to strengthen it, would you adopt that course and make an ironclad rule that you would put all the funds into that business that it required? I hardly think you would want to provide such an ironclad rule as that, to put every dollar you had into that business.

Mr. UNTERMYER. If I was running a department store that had a bank as one of its departments I would put my funds into the bank to strengthen it.

Senator REED. That would be your bank?

Mr. UNTERMYER. Yes, sir.

Senator REED. This is not our bank.

Mr. UNTERMYER. We have, however, a large discretion over and interest in its operation.

Senator REED. But we have no discretion about our putting our money in it, however. Let me imagine this sort of thing. My imagination is not ample; it is only Irish.

Mr. UNTERMYER. Well, that is very close to mine in temperament.

Senator REED. Let us imagine that when we put this system into operation we find that after it has run awhile we have a large amount of paper outstanding, and there has come some calamitous condition in the country and that paper can not be paid—the paper upon which the currency is based. We find that the whole banking system, the whole scheme now, existing in 7,800 independent banks, but under the new bill tied together by 12 regional banks; that at least those 12 regional banks are in a shaky condition and maybe are going to fail, and here is a Secretary of the Treasury with some emergency existing for the Government and demanding this money and he is compelled to put this money into the bank by the ironclad rule of law.

Senator NELSON. Senator, allow me in that connection to say just one thing right here. Under the present law the Treasury Department can deposit Government funds in its discretion with national banks upon security. There is nothing in this bill that I can find that requires these reserve banks to give security for these Government deposits, except you can say that that would come in under that law. There is nothing here.

Senator REED. That is just what I am driving at. I have not found it.

Senator NELSON. It can require security under the present law. They afterwards extended it to Government bonds, and I believe finally now they have added commercial paper and do it on that basis; but there is nothing in this bill that I can see that requires any security to be given for these Government deposits

Mr. UNTERMYER. Yes; and there ought not to be. These Federal banks can incur no obligation except to the Government and for currency loans, and to its member banks for their deposits.

Senator NELSON. They give no security, however.

Mr. UNTERMYER. The ordinary bank has obligations; this reserve bank has no power to incur any obligation except as stated.

Senator HITCHCOCK. But it has deposits.

Senator NELSON. In the State of Minnesota we deposit funds among the State banks, but we require them to give security.

Senator REED. There is nothing in this bill that gives the Government the first lien for the money it deposits. It gives it a first lien as to the money it advances upon assets of the regional banks.

Mr. UNTERMYER. It ought not to have a first lien as against the money deposited by the banks. The Government money ought to be on the same basis as that of the banks, because of the supervisory control it exercises.

Senator NELSON. Another thing, Senator Reed, right in that connection. You are on the right track here. They are virtually compelling the Federal Government to open an account with these regional banks that do all their disbursements by checks, instead of giving it out to you and I and all other Government employees. They give us checks on these regional banks. That would be the system. It is simply making the Government establish checking accounts with all these banks.

Mr. UNTERMYER. It has checking accounts now—a great many.

Senator REED. There is another reason it seems to me. The Government of the United States agrees to make good in gold every note that may be issued at the demand of these banks.

Senator NELSON. Regional banks?

Senator REED. Now, if the Government of the United States collects at its port of entry and by its various other means funds from the country and has the right and power to lay aside in its vaults such gold as it gets from time to time, it has that gold in reserve to meet its obligations; but under the provisions of this bill it is compelled to deposit every dollar it gets in these banks. It no longer has the ability to conserve its gold reserve or to create one; it must carry that gold over the minute it gets in and put it into these banks where only 33 per cent of it is being held.

Senator BRISTOW. None of it is being held, "gold or lawful money."

Senator REED. It seems to me we ought to give that very serious consideration. I have not arrived at any conclusion about it.

Mr. UNTERMYER. I think that the Government stock of gold should be segregated and used to uphold its own credit and that it should not be required to deposit its gold with the reserve banks.

Senator REED. I think you are right about that.

Mr. UNTERMYER. That is why I an offering the suggestions I am making here, in respect to this question of gold. A point that occurs to me is that there is no power in the bill, so far as I can see, to issue currency with which to buy gold. Reserve banks have the right, under the bill, to deal in gold or gold bullion, and the Government has the specific right to issue currency, but only as against certain specified assets, consisting of commercial paper. There is nowhere any power to issue currency with which to buy gold, and thus make good its obligation to maintain the parity and to redeem the notes that are provided to be issued.

Senator SHAFROTH. Does not the law of March 14, 1900, which is reaffirmed in this bill give that right?

Mr. UNTERMYER. Only to preserve the parity of our then existing note issues.

Senator SHAFROTH. To preserve the parity and to use all the powers of the Government.

Senator NELSON. That is only to get the gold to maintain the parity of our money which we had at that time.

Mr. UNTERMYER. Yes; and I understand that they can only do that through bond issues. The Government will have the right to issue this particular kind of currency now under discussion for the purposes and upon the security specified, and for none other. It is specifically provided that this currency shall only be issued for certain purposes, which do not include the purchase of gold. That is my idea.

Senator SHAFROTH. I think you are right there.

Senator NELSON. The law of 1900 provided for the sale—authorized the sale of bonds to replenish the gold reserve. That was to replenish the gold reserve for the purpose of taking care of the greenback and silver currency; but there is no law authorizing the replenishing of the gold reserve to take care of this reserve currency.

Senator REED. You do not think that could be implied?

Senator NELSON. I hardly think so.

Senator REED. It merely preserves the right created by that law.

Senator NELSON. I do not think it could be implied.

Senator REED. It could not be implied to care for this money we are about to issue.

Mr. UNTERMYER. These are all changes largely of phraseology and do not affect the fundamental principles of this bill.

Senator REED. But they are very important.

Mr. UNTERMYER. Yes; they are important. Of course, the bill needs a number of these changes. I have thus far referred to only a few of them. There are many more and some of them important. They do not, however, affect the great question as to whether this is a good system in its fundamentals.

Senator BRISTOW. If you are through with that, we will come back to the system.

Mr. UNTERMYER. If you do not mind, I would like, in connection with my claim that these currency notes can not be issued to buy gold and that no means is provided to supply the gold with which to make good the redemption promise, to call your attention to the following language of section 17:

SEC. 17. That Federal reserve notes, to be issued at the discretion of the Federal reserve board for the purpose of making advances to Federal reserve banks as hereinafter set forth and for no other purpose, are hereby authorized.

That would exclude the power of the Government to issue these notes to replenish the gold reserves.

Senator SHAFROTH. I think it quite likely.

Senator BRISTOW. Now, back some time since, when we got started off on this gold question, I was inquiring why provision should not be made so that this bank at Anthony, Kans., could take those securities direct to the Treasury and get the currency from the Government—this Government currency—instead of through the machinery of this bank; and you suggested it would be a very difficult thing to do.

Mr. UNTERMYER. A very dangerous thing.

Senator BRISTOW. A very dangerous thing?

Mr. UNTERMYER. And it seems to me a very unscientific thing.

Senator BRISTOW. When a national bank wants to issue any currency it goes to the comptroller, does it not, under fixed requirements of the law?

Mr. UNTERMYER. Yes.

Senator BRISTOW. And it gets the currency and it is issued and it circulates among the people. That has not been very dangerous and it has not been very complicated, has it?

Mr. UNTERMYER. It has been very rigid, and is measured by the known quantity of Government bonds of a given character.

Senator BRISTOW. Very will; we will admit that it is rigid.

Mr. UNTERMYER. But it is the Government credit on which they get the currency.

Senator BRISTOW. The Government credit—it takes a Government bond, but the Government deals directly with the bank.

Mr. UNTERMYER. Yes; but the Government originally had the gold from that bond with which to pay this note. In other words, when the bond was sold, the Government got the gold. And so when the man comes over with the bond the Government presumably has the gold that it receives from that bond against the note. That is 100 per cent security.

Senator NELSON. The Government, under this bill, can not get any gold except by the sale of bonds, for the reason that these Federal reserves are to be accepted in payment of all dues to the Government—taxes, customs, duties, and everything else. The Government can not get any gold through these reserve notes. The only way the Government could possibly get it, and that is doubtful, without amending the law——

Mr. UNTERMYER. It can still own the notes. It can exchange those notes for gold. It can sell them.

Senator NELSON. That is, if the regional bank had the gold?

Mr. UNTERMYER. No; it can sell them in the markets of the world.

Senator BRISTOW. What notes do you refer to?

Senator NELSON. The reserve notes.

Senator BRISTOW. The Government sells this currency.

Mr. UNTERMYER. It can issue this currency.

Senator REED. You mean discount it for gold?

Mr. UNTERMYER. Yes. They can not directly discount it for gold. I agree to that. But they could issue those notes through the regional banks and buy gold.

Senator NELSON. Unless it was compulsory it would not work very well.

Mr. UNTERMYER. I do not think you could do it that way—sell the notes and get the gold for it.

Senator BRISTOW. Now, to get back to this system of which you are afraid of the Government dealing direct with the banks. The Government has experienced no difficulty in dealing with the individual banks so far as the present national-bank currency is concerned. Now the only complaint is that that is a rigid currency. It is based on the obligations of the Government. It is proposed here to issue a currency based on the obligations of the individual citizen who is in business—not on the obligations of the Government. If the law would prescribe the kind of security that could be received by the comptroller and currency issued upon such security under certain conditions, why could not the comptroller's office deal directly with the banks?

Mr. UNTERMYER. Because it has not the safeguards thrown around it and you would make a collection agency of the Government. Under the pending bill the Government can rely largely as to the character of its security upon the investigations of the reserve board.

Senator BRISTOW. That would depend, would it not, upon the kind of security the Government decided could be hypothecated for currency?

Mr. UNTERMYER. I am assuming it is such security as the banks have which is owed for the currency.

Senator BRISTOW. If that were State bonds or municipal bonds or security of that kind it would not be difficult would it, because it is well known what the market value of that kind of security is?

Mr. UNTERMYER. When would that money ever come back?

Senator BRISTOW. That would depend upon the tax that was put on its use, would it not, as to when it came back?

Mr. UNTERMYER. To some extent; but it seems to me that a large part of it would naturally not come back except in the course of years if it was loaned on obligations of that character. You would soon get to the end of your tether.

Senator BRISTOW. I think not at all. If a bank paid interest for the use of this currency to the Government—for the use of this currency issued to it upon this security—and a deposit of this security is made to secure the return of the currency, and if month by month the interest charge became heavier it would, as a matter of fact, result in the notes being presented for redemption and taken up. Would not that give elasticity to the currency?

Mr. UNTERMYER. Up to a certain point; but you would not get a currency that would retire itself at all, except by enforced redemption at a high rate of interest; and then you might have to run the interest rate up to such proportions that it would reflect upon the credit of the whole country. If the Government found itself exacting say 7, 8, 9, or 10 per cent interest upon municipal bonds what becomes of our credit throughout the world? All private credits would go up.

Senator REED. Would that be true, then, if this board raised the interest?

Mr. UNTERMYER. I can not conceive of the board raising this interest to any great height.

Senator REED. They are not authorized to stop it.

Mr. UNTERMYER. Yes; they are always authorized to stop it.

Senator REED. Not under this bill.

Mr. UNTERMYER. Yes; they have the right to fix the rate, the right to fix the security, and the right to do those would necessarily imply the right to refuse to issue the paper at all.

Senator REED. The point I am making is in connection with the raising of this interest rate upon the moneys issued to the banks upon the illustration of Senator Bristow. If that would destroy the credit of the country abroad and break down the system, then I do not see why there should be a raise to a very high rate.

Mr. UNTERMYER. No; suppose we analyze it for a moment. Here you have a rate covering a great region of the country, a reserve region of one-twelfth we will say of the whole country, based upon short-time paper, that is to some extent self-redeemable and self-payable. It is not within the range of probabilities that the rate would go up to any extortionate amount, because the situation is temporary and the paper rapidly maturing. You are dealing with 26,000 banks, and some bank comes in and borrows on municipal bonds or something else due in 10 or 20 years and the rate rises automatically month by month under your plan, and that particular bank is not able perhaps in one to three years to realize on its bonds so as to pay, and the rate goes up to an abnormal figure.

Senator REED. You are assuming that it has now liquid assets: it has notes, etc., to collect.

Mr. UNTERMYER. I am assuming that it will need those assets in its current business, and has on hand a municipal bond which has no market, payable many years from now. It takes it years to get in the money, and I say to Senator Bristow that under his plan he is going to keep automatically raising the rate month by month until the loan is paid, and that is impracticable beyond a given limit. You can not issue currency based on immovable assets or on obligations with a long or uncertain maturity.

Senator BRISTOW. You say this municipal bond is not liquid. Do you expect the Government to collect these notes of Tom, Dick, and Harry out here in California or Oregon and hypothecate them?

Mr. UNTERMYER. No: because between the member banks and the Government you have the regional banks, which are responsible for the debt and must assume the burden.

Senator REED. Do you expect the regional banks to do that?

Mr. UNTERMYER. No: we expect the member banks to collect for them: but we expect them to collect for the account of the regional bank. When the member bank does not collect, of course the regional bank will have to have the machinery for that purpose. But that is a very different thing from the Government having the machinery, itself having running accounts, taking collateral, and collecting if the collections are not made by the member banks.

Senator HITCHCOCK. Suppose it was limited to the national banks, which is as far as this bill goes?

Mr. UNTERMYER. I should hope that was not so.

Senator HITCHCOCK. I think it will be limited to that extent.

Mr. UNTERMYER. Then you will never have much of a system.

Senator HITCHCOCK. Suppose it was limited to the national banks, and suppose we created 48 subtreasury officers to correspond to the 48 cities we have now. Suppose we use the machinery of the comptroller's office which already exists, and under which the banks are periodically examined by the comptroller's agents. Those agents are obtained to examine the banks as to their solvency and they are competent to pass upon the paper in the bank, are they not?

Mr. UNTERMYER. I do not think that follows.

Senator HITCHCOCK. That is what they do all the time.

Mr. UNTERMYER. They do, to a certain limited extent, of course, but in a general way I do not think that is true.

Senator HITCHCOCK. Suppose the bank examiner placed in each one of these subtreasuries, instead of putting up bonds, should pass upon this commercial paper. These experts are just as competent to pass upon that paper as these regional banks, but instead of having 12 we would have 48. What would be the objection to having the national banks secure from the Government an amount of currency, say, equal to three quarters of its capital stock, and have them put up the commercial paper which would be passed upon by the examiners?

Mr. UNTERMYER. It would be bureaucratic. It would be putting the final decision as to the character of the paper put up as security into the hands of one man. Now, the paper is subject to the examination of the banks themselves and the board of directors. Again, you would not have the security you have now. You have now the uncalled liability of the bank. You have a first lien upon all the assets of the reserve bank and on all its deposits.

Senator HITCHCOCK. You can make this a first lien, too.

Mr. UNTERMYER. No; you can only make this a first lien on the assets of that particular bank, Senator.

Senator HITCHCOCK. The agent of the Treasury would be the examiner, then.

Mr. UNTERMYER. I understand that. Some one official would be the examiner. Under the other system there would be a board to do that.

Senator REED. You do not mean that the board of nine members would examine 700 of these members of the regional bank? They would have to do that through agents, would they not?

Mr. UNTERMYER. I do not think so. That is one of the arguments in favor of 12 regional banks instead of a less number—the directors would be selected from the regions where they have the general knowledge which is required to pass upon that paper. But there is a lack of security to the Government behind that sort of note issue.

Senator REED. Where do you get the additional security in the reserve system?

Mr. UNTERMYER. In the first place, you get all the reserve of the bank for every discount and every member bank instead of getting simply the obligation and reserve of the one bank—No. 1.

Senator BRISTOW. While you have the assets of the regional bank, the regional bank has a great deal more obligations to the Government than the individual bank has.

Mr. UNTERMYER. I understand that it is under obligation to the Government to accept the currency and the money deposited by the Government. If you deal through a regional bank, you can get additional security that you do not get when you deal with a member. In the first place, you get the uncalled stock liability.

Senator REED. That is a double liability of the stock.

Mr. UNTERMYER. Yes; and the 10 per cent that is uncalled. Then you get a first lien upon all the assets of that bank, which means that you get a lien ahead of everybody else on the deposits of the member banks with that reserve bank.

Senator REED. You mean to say that you get a first lien upon the assets? Assets are the reserves.

Mr. UNTERMYER. I said upon the deposits.

Senator REED. The reserves that are there?

Mr. UNTERMYER. You get a first lien on those.

Senator BRISTOW. On the assets?

Mr. UNTERMYER. Yes.

Senator BRISTOW. It would not be on the reserves of the bank?

Mr. UNTERMYER. Those deposits are assets of the reserve banks.

Senator BRISTOW. They are debts of the reserve banks.

Mr. UNTERMYER. They are also liabilities; but they are assets.

Senator BRISTOW. How could you have a debt and an asset at one and the same time? They do not mean one and the same thing.

Mr. UNTERMYER. Of course, you would have a liability. The money that the member bank puts in there—those are assets of that reserve bank; it owes the member bank and it is indebted for the amount of the notes.

Senator HITCHCOCK. Instead of a lien on the deposits you mean a lien on the cash?

Mr. UNTERMYER. I mean a first lien on all the moneys they have.

Senator HITCHCOCK. What deposits of any value are there? There is only a third on hand in cash.

Mr. UNTERMYER. But the rest of it they have out in obligations—notes that they have discounted and own. They would have a lien on all those. That means a lien on the deposits. Then every member bank becomes a guarantor for the obligation of every other member bank for the unpaid liabilities.

Senator REED. They become liable to the regional banks to the extent of its stock interest.

Senator REED. Let us capitalize a regional bank.

Senator BRISTOW. Yes; that is an excellent idea. Also capitalize the individual bank and put them side by side.

Senator REED. Now, let us say that here is a regional bank started in the city of St. Louis with 700 member banks and with 10 per cent of the capital stock and those 700 member banks will take up $5,000,000. This is an arbitrary figure. You take $5,000,000 and you put it in the Treasury. You have got now the right to call for $5,000,000 against these member banks.

Mr. UNTERMYER. Yes.

Senator REED. That constitutes the double liability for it. You have $5,000,000 now.

Senator WEEKS. It is not a double liability, for you have to issue stock for that second $5,000,000.

Senator REED. Yes; you just have $5,000,000 in money.

Mr. UNTERMYER. That $5,000,000 uncalled liability is an asset.

Senator WEEKS. Of course.

Senator REED. I am going to put it over here and count it as a real reserve to be drawn against, and we will say you have $10,000,000 of deposits.

Mr. UNTERMYER. And now you have $30,000,000 of deposits.

Senator REED. Now you have $30,000,000 of deposits, which is the reserve which the banks now have in their vaults or have in the vaults of other national banks.

Mr. UNTERMYER. And that $30,000,000 of deposits is invested now in obligations.

Senator REED. We have $40,000,000.

Senator WEEKS. Some of it.

Mr. UNTERMYER. Yes; the rest of it is gold.

Senator REED. You have $40,000,000 in this bank now. Now what happens? We loan that $30,000,000 at once to the member banks and we take the notes of the member banks, and we also loan our $5,000,000, or two-thirds of our $5,000,000, put in for stock. We loan that out.

Mr. UNTERMYER. You can loan that all out; and you can only loan two-thirds of the $30,000,000.

Senator REED. You are correct. We have a bank now with $20,000,000 and we have set aside a reserve of $10,000,000 in gold, and we loan $20,000,000. Now we have $30,000,000.

Mr. UNTERMYER. You loan the 20 and the 5.

Senator REED. We have $25,000,000 loaned and we have the paper of these banks. We thereupon go down to the Treasury with that $25,000,000 and we get $25,000,000 Federal notes for it.

Mr. UNTERMYER. Yes.

Senator REED. Which we in turn loan again to these other banks, for we have it in our hands.

Mr. UNTERMYER. And then when you do that you get their assets.

Senator REED. Now, we have the obligations of these banks in the long run for $25,000,000 and we have given and obtained from the Government $25,000,000 of paper.

Mr. UNTERMYER. But you must add this $25,000,000 to your assets; you must put the $25,000,000 on this side.

Senator REED. Now, you have back of that paper money that was issued by the Government what? You have the $5,000,000 of stock in this bank and you have the $25,000,000 of the member banks' paper, indorsed by the regional banks. If you turn it over again, making the second loan, you then have $50,000,000 of bank paper and $50,000,000 of currency. Each time you turn it over you take out 33 per cent of gold.

Mr. UNTERMYER. But $25,000,000 of this comes behind the Government debt. The currency is preferred. It is a first lien ahead on these reserves.

Senator REED. I understand that, but you lend it out again and go back and get more currency.

Mr. UNTERMYER. You are always $25,000,000 ahead.

Senator REED. I grant that. But you keep on doing this until finally, having taken out one-third each time of the gold reserve, you have $100,000,000 of this currency out. You have $100,000,000 of notes indorsed by the banks and you have that $5,000,000.

Mr. UNTERMYER. You have $125,000,000 indorsed by the banks.

Senator REED. Well—$125,000,000. You have that $5,000,000 of money you originally put in. The rest of this is all the debts of these banks and you have not got a thing to fall back on outside of that money that was originally put in, except the $5,000,000 of additional assessments you can make. Now, then, that is that situation.

Senator BRISTOW. Now, take an individual bank.

Senator REED. Let us take a bank that is organized with $100,000 of capital.

Mr. UNTERMYER. I think you are wrong, Senator Reed, if I may interrupt, if you do not mind. What you have is this: You have back of that $25,000,000 the notes.

Senator REED. You have the obligation.

Mr. UNTERMYER. You have $40,000,000 of securities.

Senator REED. But it is made up of the notes.

Mr. UNTERMYER. The point about it is that the Government's claim for the currency becomes a prior lien; prior to the reserves of these banks, and therefore it is absolutely good. The banks can not get back a cent of their reserves until all that currency is redeemed by the reserve bank.

Senator REED. But they borrow back the reserves.

Mr. UNTERMYER. You have the notes instead; you have a prior claim to the member banks on these assets.

Senator REED. Well, let me grant that for the moment—although I think that what you have got in this transaction is $5,000,000 in money paid in by the banks for this stock, $5,000,000 in liability for the issue, and then you have the notes of the bank representing the money that is issued. Now, we are talking about the security for this money.

Mr. UNTERMYER. Then you have also the gold reserves as further security for the notes.

Senator REED. Yes; you have got your 33⅓ per cent.

Mr. UNTERMYER. I mean that that is your security, too.

Senator REED. That comes out of the aggregate, of course. When you take out your reserve and your gold you set that aside and that is that much margin.

Senator Hitchcock. Senator Reed, I think you have left out still another very important distinction. That is, under that suggestion made by Senator Bristow which I took up, there was a limit on the amount of currency, or credit, which each bank would secure.

Senator Reed. I am coming to that.

Senator Bristow. He is coming to the individual bank.

Senator Hitchcock. But under this scheme there is no limit to the amount of credit which the reserve bank may extend to the individual bank; and instead of extending to the individual bank a limit, of say, 75 per cent, as proposed by Senator Bristow, the reserve banker extends it a credit of 400 per cent on its capital; and that is all the security the Government would get in addition.

The Chairman. May I make just one suggestion there? The primary security against these notes consists of the note of the individual which is discounted, and which, under the terms of this bill, has a short maturity. Under the law of probabilities, the danger of a man who is regarded as good by a bank and to whom the money is loaned failing within 60 or 90 days would probably be about 1 in 25,000.

Senator Reed. That is true of both systems.

The Chairman. Yes, of any system.

Senator Reed. One in twenty-five thousand?

The Chairman. And such a note, before it becomes a security under the system for the issuance of these Treasury notes, must also be indorsed by the member bank. And under the law of probability, the probability of a member bank in good standing, examined by the examiners, and reported as sound, failing within the period of 60 days, or 90 days—the life of the contemplated transaction—is probably 1 in 100,000. And the measure of probability of the failure of the individual maker of the note and of the bank which indorses that note, failing within the limited number of days, would be measured by 25,000 multiplied by 100,000.

If, however, such a contingency should arise, then the note has the further security of the double liability of the stockholders of the member bank indorsing that note.

If, however, those resources should fail, the Government, in that contingency would, against such a loss of security, have the stock of that particular member bank that failed in this reserve bank.

In addition to that, however, it would also have the security of the reserve deposit of this member bank with the reserve bank. If, however, those resources should all fail, the Government would have a further safeguard as to these particular notes, in the 33⅓ per cent gold reserve required against the notes.

And in addition to that it would have a first lien upon the assets of this bank, which you have, in this particular case of exemplification named, amounting to $40,000,000.

And in addition to that you have the double liability of the member bank for the amount, equal to a like sum with their capital.

There never has been, in the history of the world, a note secured by such a volume of security.

Senator Reed. I do not like to differ from the chairman; but I think you have counted your assets at least three times in turning that over, Mr. Chairman.

The Chairman. Then the record is open to the Senator from Missouri to demonstrate that fact.

Senator REED. I can not see it that way. I do not mean that it is bad security; but I mean you have counted it too often.

Senator NELSON. Now, the regional banks are required to keep 33⅓ per cent in gold for redemption.

The CHAIRMAN. Yes.

Senator NELSON. Now, that will be idle money. Why not require them to deposit that reserve in the Treasury Department, with the Treasurer, and then if every bank deposited that 33⅓ per cent the Treasury Department would not have any trouble in getting a gold reserve to redeem the note. Would not that make it safer? Otherwise you would simply have the bookkeeping of the banks.

Mr. UNTERMYER. That is the suggestion I made awhile ago, except that the gold thus deposited should be to the credit of each reserve bank, but deposited so that the Government could make good its obligation to redeem the notes in gold.

Senator NELSON. It should be to the credit of each bank, for the bank note.

Mr. UNTERMYER. We went over that awhile ago.

Senator BRISTOW. Now, I want Senator Reed to work out this little bank problem, to come down to the little banks. For his liability he has got his sacks up just as high. His liability is not as great, but he is just as good.

Mr. UTERMYER. Hardly.

Senator BRISTOW. I think he is better.

Senator HITCHCOCK. His liability is limited to 75 per cent of his capital stock.

Mr. UNTERMYER. Yes.

Senator HITCHCOCK. That is all the currency he can get, whereas through the reserve agent he may get an amount of currency which was 10 times the amount of his capital.

Mr. UNTERMYER. But I think the chances are about 1,000 to 1 on the question of security.

Senator BRISTOW. And then you put behind that 75 per cent—when Senator Reed gets that worked out—you put behind that the gold reserve in the same proportion that you require of the regional bank. You put behind it the assets of the member bank. Have you got that worked out, Senator Reed?

Senator REED. No; I have not been able to do it yet.

Senator HITCHCOCK. Would it not be well to adjourn at this time?

Senator REED. I would like to see it done (and I will do it if nobody else will): Assuming that it proceeded on and got this currency until its ability was exhausted by the amount of gold reserve it had set aside, and see what the asset is back of it; and then take the individual bank, with its limitation, and work it out. Somebody can do that, it seems to me.

Mr. UNTERMYER. Do you think there is any occasion for me to be here to-morrow?

Senator BRISTOW. Yes. We have not got started on the subject yet.

Senator HITCHCOCK. Yes. We have hardly got started.

Senator WEEKS. I have not had time to ask any questions. Mr. Chairman, before we adjourn, I want to make a little statement in connection with a colloquy which I had with Mr. Untermyer this forenoon about the bonds held by two Boston banks.

Mr. UNTERMYER. Yes.

Senator WEEKS. I have not been able to find out the exact facts yet. I have been looking it up in the comptroller's report to find out how many they held, but I have been unable to do so because real estate and other things are lumped with them; but I am inclined to think that I underestimated their holdings. And I want to say that in justice to Mr. Untermyer.

Mr. UNTERMYER. I do not think that was necessary, Senator Weeks, as I understood your point of view. You understand that I did not mean, in anything that I said as to those banks, to reflect on their method of doing business. I was trying to show why it was not to the interest of the great banks of New York to have this system take the place of the present system.

Senator SHAFROTH. Mr. Chairman, when are we going to close these hearings?

The CHAIRMAN. We ought to be able to conclude with the witnesses who are available now by Friday.

Senator WEEKS. Mr. Chairman, I have several witnesses here who would like to be called. I should like to give you the names, if it is going to be the policy of the committee to call those witnesses who desire to be heard. I think the committee had better decide that question now. If it is decided to hear other witnesses, I would like to furnish the clerk with these names, and ask that they be called.

Senator POMERENE. Are they bankers?

Senator WEEKS. Yes.

Senator SHAFROTH. How many are there?

Senator WEEKS. I do not know. There is a telegram from Charles P. Blinn, president of the Massachusetts Bankers' Association, who asks to be heard.

Senator SHAFROTH. Is he the only one from home you have heard so far?

Senator WEEKS. No; I have six. Five of country bankers. Mr. Blinn is vice president of a Boston bank. I understand that he wants to bring two or three country bankers with him from Massachusetts.

Senator BRISTOW. I will furnish the chairman with the names of some country bankers from the West who want to be heard.

Senator POMERENE. Mr. Chairman, I want to renew a suggestion I have made three or four times, and that is that if we would allow a witness, when he comes here, to make his statement and then take up the cross-examination of him in some regular order we would save a vast deal of time and we would get more satisfaction out of it, both from the standpoint of the witness and from the standpoint of the members of the committee.

Senator SHAFROTH. I think so, too.

Senator POMERENE. There is not any doubt about it. We would have saved time this afternoon if we had adopted that course.

The CHAIRMAN. That is a matter, of course, which rests in the discretion of the committee. It obviously is not for the chairman to intervene when an examination by a member of the committee is under way.

Senator WEEKS. I think we have been reasonably regular. I have been sitting here nearly the whole day listening to what was being said.

Senator POMERENE. So have I.

Senator SHAFROTH. Mr. Chairman, can not we agree upon a time to close these hearings?

Senator POMERENE. No.

Senator Bristow. No; we can not.

Senator Shafroth. You will find that there will be more time——

Senator Pomerene (interposing). There will be a reasonable limitation.

Senator Shafroth. Why not make it now?

Senator Hitchcock. What was your suggestion, Senator Pomerene?

Senator Pomerene. Here is Mr. Untermyer, who has come here with well-defined ideas, which he wanted to present to this committee, and he should give them in some consecutive order. Now, let him make his statement, and then let the members of the committee question him, in regular order, upon matters that they may have in mind. In that way we will get the benefit of Mr. Untermyer's thought upon the subject and have them in some consecutive order, it seems to me; and we will save a great deal of time by it.

Senator Shafroth. Well, can we close the hearings, say, Saturday—a week from next Saturday?

Senator Hitchcock. How can we tell at this time?

Senator Shafroth. We have got to end them some time. We can go on indefinitely for 10 years and not get fairly through it.

Senator Reed. Mr. Chairman, I have seen a great deal of time spent in the prosecution of a suit at law over one question; and it was deemed necessary by courts of justice to take that much time to investigate that one question. It is not unusual for an important lawsuit to last six or seven weeks. It occurs to me that, with a question of this kind, involving as it does the very life of the commerce of our country, we can afford to sit here long enough to let those parties who have a real and a substantial interest or a real message to deliver be heard.

Now, we are, of course, wasting time when the committee feels that it has been over this ground and been thoroughly advised; and then we ought to stop. There is this important fact that I want to emphasize.

If Mr. Untermyer, who is a very learned man, is correct in his diagnosis of this bill, then there are a large number of important amendments that he has suggested. We have had suggestions from men here who have spent their life in banking and who have pointed out a great many other suggested amendments.

And I think that before we put a system of this kind on the country that affects all the banks and all the people, we ought to come just as near knowing what we are doing as it is possible for us to know, within our limited experience and intelligence.

I am not in favor of any rush act on this bill. We have lived under the present system. The country is prosperous and I am willing to work as many hours a day as anybody wants to work. I am not willing to make a guess now as to the period of time when we will know just what the best measure to meet the conditions of the country will be. That is the way I feel about it. I am willing to work, and keep on working; but I am not willing to set a time for stopping now.

Senator Shafroth. Do you not think that we will be able to cover all that is necessary by Saturday week?

Senator Reed. If we do, when we come to Saturday week we can say so.

Senator Nelson. We will know better when we come to the end of the week where we stand; we can determine better then.

Senator WEEKS. Mr. Chairman, there is a resolution introduced by me which has been referred to this committee, and I am likely to call it up at any time, because I think the members of the committee can see that it is likely to take most of the fall to get this bill reported out; and if it is going to take as long a time as that, the other Members of the Congress, both Senate and House, had better be given an opportunity to go home.

Senator REED. I would not want to say on that that it was going to take most of the fall.

Senator WEEKS. I do not know that it is, but I think it is going to take some time.

Senator REED. There are men representing great banks coming here asking to be heard. Now, I want to hear them. I want to hear these great bankers——

Senator NELSON (interposing). I do.

Senator REED (continuing). And I want to hear some little bankers, also.

Senator BRISTOW. That is what I want to hear—some of the little bankers.

Senator REED. And if there is anybody wanting to be heard from other classes of people, I want to hear them.

Senator SHAFROTH. But the Monetary Commission published volume after volume upon this subject.

Senator BRISTOW. But the Monetary Commission did not have the men I wanted to hear. I want to hear the men who are affected by it, not the big men.

Senator SHAFROTH. Well, the men who were affected were here.

Senator REED. I might not be any better satisfied with their investigation of witnesses than I am with their conclusion.

Senator SHAFROTH. I think we ought to fix the time when we will close the hearings, because it is then going to take up a great deal of time to get up these amendments and report them; and I feel that otherwise we will not be making the headway that we should; and I think we have had two weeks or more of hearings——

Senator REED (interposing). Has there been any day that we have not found out something new?

Senator SHAFROTH. That might be true.

Senator REED. If the hearings were closed Saturday night we might not have discovered something of great value. Perhaps the members of the committee discovered it; perhaps they had their minds on it; but certainly we had no discussion of the very important thing discussed here this afternoon, namely, whether the Federal Government ought to be compelled to pay all this money in these banks and have no means of securing a gold reserve of its own.

Senator NELSON. And no security for the deposits.

Senator REED. I would rather sit here a month and find out nothing at all for the whole month and then find a thing of that kind than I would to discover it 30 days after the bill had gone into effect.

Senator HITCHCOCK. Mr. Chairman, I move that we adjourn until 10 o'clock to-morrow morning.

(Thereupon, at 5.50 o'clock p. m., the committee adjourned until to-morrow (Tuesday), September 23, 1913, at 10 o'clock a. m.)

TUESDAY, SEPTEMBER, 23, 1913.

COMMITTEE ON BANKING AND CURRENCY,
UNITED STATES SENATE,
Washington, D. C.

The committee assembled at 10.20 o'clock a. m.

Present: Senators Hitchcock (acting chairman), Reed, Pomerene, Shafroth, Nelson, Bristow, McLean, and Weeks.

Senator HITCHCOCK. As there seems to be a quorum present, I think we had better proceed. Mr. Untermyer, will you resume your statement of yesterday?

Senator BRISTOW. I was not through with the interrogatories I had started to make, Mr. Chairman.

Senator SHAFROTH. But had we better not hear Mr. Untermyer through before asking him any questions?

Mr. UNTERMYER. May I make a statement before you ask your questions, Senator Bristow?

Senator BRISTOW. I had started out on a line of inquiry in regard to the things about which you testified yesterday; but I was diverted by other Senators breaking in with questions.

FURTHER STATEMENT OF SAMUEL UNTERMYER, ESQ., OF NEW YORK CITY.

Mr. UNTERMYER. I should like to make just this suggestion, if I may: I find in some of the morning papers a statement which rather misinterprets the intent of what I said, or wanted to say, yesterday with respect to the possible political influence of this reserve board upon the currency system of the country. I have been reported as saying that with my imagination I could conceive of a situation in which such political influence might be exerted. As I remember the occurrence, I was asked the question as to whether or not I could conceive of a set of conditions resulting in such unwholesome influence; and I said that with my imagination I could conceive of that, but that I did not believe it probable, or even possible; and I wanted to be understood as saying that I did not regard the danger from any such source as within the range of possibilities; and that I saw no objection but great advantages to the Nation through its Executive having the control of the system through the appointment of the board and of every member of it, and having no banking representation whatever upon the reserve board.

It seems to me that it is incongruous that there should be any banking representation on the Federal reserve board, because that board is dealing with the reserve banks that are controlled by the bankers. They come to that board with certain classes of paper, and they say to the Government, "We want you to issue currency for this paper." Now, surely they ought not to be permitted to sit on both sides of the table—to be represented on both sides of the bargain, if I may so term it.

Senator HITCHCOCK. You are referring now, Mr. Untermyer, to the question I asked you?

Mr. UNTERMYER. I think so, sir.

Senator HITCHCOCK. Well, I did not ask the question with a view to suggesting that bankers should have a seat or a representation upon the board.

Mr. UNTERMYER. I know you did not, Mr. Chairman.

Senator HITCHCOCK. But rather for the purpose of indicating that there ought to be some check by law upon the discretionary power of the members of the board.

Mr. UNTERMYER. Yes; I quite appreciate that. I know your question had no reference to the constitution of the board itself.

Senator HITCHCOCK. No.

Mr. UNTERMYER. But, answering the demand of the bankers for representation on the board, it seems to me that it is an unjustifiable demand.

Senator SHAFROTH. Mr. Untermyer, the rule, as I understand it, or the reason why bankers are not permitted to sit on the directorate of what is called the court of directors of the Bank of England, is because it would give to any banker actively in business the advantage of knowing when the discount should be raised or lowered; and inasmuch as the raising or lowering of the discount has a tendency to affect the market price of bonds and stocks, it would give an unfair advantage to that director connected with the bank which deals in such things, and therefore it would not be "compatible"—is the word they use—for a banker in active business to sit on the court of directors.

Mr. UNTERMYER. I think that the further reason has often been stated that they would be dealing with themselves. For instance, the Bank of England has no member on its board who is connected with any bank of deposit; that is, any bank that accepts deposits. Six out of its 17 or 21 directors—I forget the number—are what you may call "merchant bankers." They are merchants, primarily.

Senator SHAFROTH. They are not banks that receive deposits, though?

Mr. UNTERMYER. No; they are not banks of deposit, and they are, as I say, primarily merchant traders. You take, for instance, the Rothschilds, who are popularly supposed to be the great bankers of the world. Their business is, and always has been, primarily that of merchants. They drifted almost unconsciously into banking by reason of their activities as merchant traders. To-day they are the largest dealers in the world, or among the largest dealers, in copper, coffee, oil, rubber, and a number of other products. They buy and sell and deal in more of those products, on commission and otherwise, than almost any other people in the world.

And so with other men who are regarded by us as primarily bankers. They became bankers because, first, they bought the product and sold it, and then they took it on consignment and loaned on it; and they were dealing in merchandise, and that is the way these men drifted on to the board of the Bank of England. There are a number of such men, like Sir Cecil Hambro, and a member of the firm of Kleinwort, and a member of the firm of Schroeders, and two or three others of that kind; but no member of any bank that accepts deposits is on the board.

Senator HITCHCOCK. Senator Bristow was asking you some questions yesterday, when he was interrupted. I suppose he wishes to resume.

Mr. UNTERMYER. Do you not think that I should state first, seriatim, the recommendations and objections I have with respect to this bill, and then resume the examination, Senator Bristow? I should prefer to go on with my statement now, if that is agreeable to you.

Senator BRISTOW. That would inject a lot of other matter into the discussion; and I probably would not get to this at all until late to-night.

Mr. UNTERMYER. Well, I want to leave the city to-day, Mr. Chairman, if I may. Even if I must come back, I must get away on the 3 o'clock train.

Senator BRISTOW. We were discussing yesterday, when some other things came up and interrupted us, and I am not complaining because the other members of the committee took up the questions as they did, because I think all the questions were pertinent, and I was glad to have Mr. Untermyer's views on the collateral matters. But we were discussing the question as to why the individual bank should not be permitted to go direct to a governmental agency and get the currency, instead of creating what seems to me to be this superfluous and unnecessary machinery to enable the bank to get it. And your objection to that, Mr. Untermyer, as I understood it, was that it would be impracticable of operation.

Mr. UNTERMYER. I had a number of objections, Senator Bristow, a few of which I had enumerated when I was interrupted.

Senator BRISTOW. Yes. Well, that was the objection that impressed me the most: there would be so many of them.

Mr. UNTERMYER. And then the inadequacy of security, as compared with under the other method.

Senator BRISTOW. And the inadequacy of security. Now, as to the inadequacy of security——

Senator REED (interposing). Senator Bristow, may I interrupt you?

Senator BRISTOW. Certainly.

Senator REED. I just came in. What is it you are discussing?

Senator BRISTOW. We are undertaking to take up the subject where we left off last night, as to the inadequacy of security which Mr. Untermyer suggests of the individual bank in going direct to the Government and getting the currency upon its own initiative, with its own assets, instead of having to get it in this roundabout way——

Senator REED. I have a table prepared on that, which will be read in a few minutes.

Senator BRISTOW. Yes; I have a statement prepared by a bank in Kansas, and your table can follow that.

Mr. UNTERMYER. Another suggestion which I made yesterday was that there would not be that same supervision possible. It would have to be done through a single local agent—that is, the examination of the paper, instead of having the concensus of opinion of a representative board.

Senator Bristow. Yes.

Mr. Untermyer. And I named three or four grounds of objection, but there are others.

Senator Bristow. Yes; I remember. But now, I want to take up, first, the matter of security. Senator Hitchcock suggested that the bank be permitted to issue 75 per cent of its capital stock in this currency. I would not have any objection personally to it issuing its full capital stock.

Now, let us see what security the National Bank of America, of Salina, Kans., would have. I happened to find in a paper last night this statement:

> Suppose it was permitted to issue $100,000 of currency on its assets. Now, what security would the Government have behind that $100,000? The bank has $100,000 capital stock, $50,000 surplus, and $33,000 undivided profits. Now, let us take its resources. I think that probably would be better. Its loans and discounts are $776,000——

Mr. Untermyer (interposing). Its resources—its net resources—are all summed up, it seems to me, in its capital, surplus, and undivided profits. Those are its resources.

Senator Bristow. Yes. But in counting the strength of the regional bank you took in its deposits; and if you count the deposits, or its loans and discounts, as a part of its assets and its security, then you must give the local bank the same credit.

Mr. Untermyer. That is quite true; we counted its deposits, because the Government has, upon the issue of this currency, a first lien upon all of these assets.

Senator Bristow. Then make it a first lien upon all these assets of the individual bank, just as you do in the case of the regional bank. Put them all on the same basis. And I think it can easily be demonstrated that to-day the local bank has more security, a larger percentage of security, behind the deposits than the regional bank.

Mr. Untermyer. I differ from you radically.

Senator Bristow. Well, you may differ from me radically, but I think it has; it is because you have not examined the facts. I think after we get through you can take in their position.

Mr. Untermyer. It seems to me you can never compare the responsibility of a single debtor with the responsibility of a whole section of debtors all combined, all of whose responsibility stands behind each item of credit.

Senator Bristow. Yes.

Mr. Untermyer. And distributed. It does not depend upon the operations of anyone concerned. I think, Senator Bristow, in all fairness, that it is pretty difficult to compare the two. One bank cashier may go off overnight with all the funds in the case of the individual bank.

Senator Bristow. But he can not carry off the assets.

Mr. Untermyer. I do not know about that.

Senator Bristow. He might carry off the cash in bank.

Mr. Untermyer. I have known them carry off the assets.

Senator Bristow. He might do the same thing for the regional bank, so far as that is concerned.

Mr. Untermyer. Hardly.

Senator Reed. Senator Bristow, may I interject a question here?

Senator Bristow. Yes; certainly.

Senator Reed. Now, in all fairness, Mr. Untermyer, does not the law of averages come in there as a protection?

Mr. Untermyer. The law of averages, Senator Reed, would come in when you are dealing with the reserve bank, because you are then dealing with 2,000 banks. But when you deal with but one bank the law of averages is much less pronounced; that is, there are a certain number of chances in a given number that that one bank will be mismanaged or go to pieces. But the chances of all those banks in a reserve bank going to pieces or being mismanaged are vastly less.

Senator Reed. Yes; I understand that principle you express, but——

Mr. Untermyer (interposing). You do not differ from it, do you?

Senator Reed. But, if the Senator will pardon me, there is just one further question.

Senator Bristow. Certainly.

Senator Reed. The Government in advancing the money to these bankers will charge an interest of some amount. Do you entertain the slightest doubt that 2 per cent interest would speedily accumulate a fund that would make up for any loss through the failure of any individual banks?

Mr. Untermyer. Oh, I should say that less than 2 per cent interest would make up such a fund.

Senator Reed. So that if you have a system so large, made up of so many constituent elements, that the aggregate received by way of interest will accumulate a fund that will take care of any individual failure, then the law of averages applies, just as it does in insurance; is that not correct?

Mr. Untermyer. Well, that is the revival of the bank guaranty.

Senator Bristow. Do not say "revival."

Mr. Untermyer. I mean to say that is the application of the theory. I did not mean to use the word "revival" of it; but it is an application of the theory. [Laughter.]

Senator Reed. It is an application of the bank guaranty to the extent of the money issued, but not to the extent of guaranteeing its liabilities?

Mr. Untermyer. Well——

Senator Reed (interposing). But I want to say now, lest I should forget it, that before this bill is finished I hope there will be something done to make the deposits of people a little more secure than they are now. But I am finished now, Senator Bristow.

Mr. Untermyer. I had not intended to imply any opinion on the subject, because I have not been asked; and I find that I have quite enough to do to answer the questions I am asked.

Senator Reed. I understand.

Senator Bristow. Now, let us take the assets of this bank at Salina, Kans., that would be security for the $100,000 currency. It has loans and discounts of $776,000—I will just use the round figures. United States bonds to secure circulation should be counted in this, because that is a part of its assets; it owns its bonds.

Mr. Untermyer. But it has circulation out against that.

Senator Bristow. It has circulation on that. Well, if the national-bank currency is permitted to stand as it is now, that should not be counted. If it is not, but is retired and this currency is substituted for it, as is proposed in this bill, that should be counted to the extent that they are retired.

Mr. UNTERMYER. Yes; but you will have to pay for it if it is retired; so in no event should it be counted.

Senator BRISTOW. Well, we will not count that.

United States bonds to secure deposits.

We will not count that either.

Other bonds to secure postal-savings deposits.

We will not count that, although it is an asset of the bank.

Bonds, securities, etc., $10,000.

That is an asset.

Mr. UNTERMYER. You would not make this a lien on the postal savings deposits, would you?

Senator BRISTOW. No.

Mr. UNTERMYER. Otherwise, you would not have any postal savings deposits.

Senator BRISTOW. No; I would not make it a lien on that. So I did not count that.

Due from national banks (not reserve agents)	$60,000
Due from State and private banks and bankers, trust companies, and savings banks	15,000
Due from approved reserve agents	148,000
Checks and other items	9,000
Exchanges for clearing house	3,600
Notes of other national banks	5,000
Specie	33,000
Legal tender notes	18,000

Now, it has redemption funds, but that we will not count.

Those are live assets, and the aggregate is $968,000, as I have summed it up rapidly.

Now, there are $968,000 of assets. The Government has $100,000 of the best paper in the bank, which it requires it to be——

Mr. UNTERMYER. Yes, sir.

Senator BRISTOW. Hypothecated; and behind that is $868,000 of the assets of the bank. And, in addition to that, the double liability of the stockholders, or $100,000 in addition, as a liability against the directors.

Do you not think that will be pretty good security?

Mr. UNTERMYER. I do not think it will compare with the security you would get under the other method. And besides each bank has a separate showing. Some are weak and some are strong, and you can not take one bank and make that an illustration of what would be the security behind each bank; you do not propose, as I understand it, to examine into the total assets and responsibility of each bank when it comes for currency; you only propose to examine into the collateral.

Senator BRISTOW. Certainly.

Mr. UNTERMYER. I should think you would simply examine the collateral and issue the note upon that. But if you are going into the operation of taking up the responsibility of each bank—its total responsibility—why then it seems to me that you are going into an almost endless task.

Besides that, your whole question assumes limiting the currency to the capital of the bank. It seems to me that the issue of currency should not be limited to the capital of the bank, but to the character of the collateral that is offered by the bank. If you are going to limit the currency that is issued to the capital of the bank, you will simply substitute one inelastic system of currency for another. You have got a basis of that kind now in your bond issue.

Senator BRISTOW. Well, the bank does not have to take out any.

Mr. UNTERMYER. The bank does not have to take it out now, either. But you are not giving us an elastic currency, if you are going to make the capital of the bank the criterion of the currency to be issued, rather than the commercial paper which the bank presents.

Senator BRISTOW. I am giving you exactly the same currency that you are advocating, except that behind that currency I propose the individual bank instead of the regional bank.

Mr. UNTERMYER. No; on the contrary, under the present bill the amount of currency the bank may get is not limited, as I recall the bill, to the capital of the bank. I have not found any such limitation.

Senator BRISTOW. No; there is no such limitation.

Mr. UNTERMYER. No; so that there is no analogy between the cases at all.

Senator NELSON. This bill is an asset currency bill.

Mr. UNTERMYER. Yes.

Senator NELSON. Based upon the assets of the bank.

Mr. UNTERMYER. Certainly. And, therefore, I say that should be the basis of the issue and not the capital of the bank. The capital of the bank has nothing to do with it. It is the assets that constitute the basis for issuance of the currency. Therefore one bank with $100,000 of capital might have $1,000,000 of good, sound commercial paper, and would be better entitled to currency than some other bank with $1,000,000 of capital that only had $100,000 of good commercial paper.

Senator BRISTOW. Well, I am perfectly willing to waive that objection, so far as I am concerned. Senator Hitchcock made that suggestion, and I simply took it from his point of view. But I made the suggestion that I would prefer to take the assets of the bank, and when the bank wants to issue the currency, let it do so without having to ask it as a favor from a regional reserve bank that will be controlled by some personal interest, the same as any other bank is.

Mr. UNTERMYER. You would not give the central authority any discretion as to whether it should issue currency when the bank presents its assets?

Senator BRISTOW. Not any more than it has now with a national bank.

Mr. UNTERMYER. Well, do you not see that if you take your illustration and remove the limitation of capital, then this bank to which you have referred, having seven hundred thousand odd dollars of commercial paper, could go to the Government direct and ask for seven hundred thousand odd dollars of currency?

Senator BRISTOW. No.

Mr. UNTERMYER. Instead of having 8 for 1, then, it would have $1\frac{1}{2}$ for 1.

Senator BRISTOW. You are assuming a thing I have not stated.

Mr. UNTERMYER. But if you remove the limitation of the amount you can borrow to the amount of capital, that is the result.

Senator BRISTOW. Well, but if you will permit me to correct your assumption——

Mr. UNTERMYER. Well, perhaps I speak too rapidly, Senator Bristow.

Senator BRISTOW. No; not at all. When the individual bank presented to the comptroller the securities which the law prescribed that it should have in order to obtain this currency, then it has the right to it; and let the law define what those securities shall be. No one will be foolish enough to say that it could get currency on its entire assets.

Mr. UNTERMYER. That is, all good commercial paper.

Senator BRISTOW. Well, commercial paper I do not think is entitled to any more consideration than a mortgage or a bond.

Mr. UNTERMYER. There we could never agree.

Senator BRISTOW. We very radically differ.

Mr. UNTERMYER. Yes; and could never agree on that.

Senator BRISTOW. Because I think this commercial-paper proposition is in the interests of a certain class of the people and it is establishing a currency system for the benefit of a few merchants instead of for the Nation.

Mr. UNTERMYER. It really establishes a currency for the Nation, if you will look at the experience of other countries.

Senator BRISTOW. Now, if the individual bank should present a certain security for this currency which the law defines, then it would meet your suggestion that the currency would be issued on the assets or security that was presented, would it not?

Mr. UNTERMYER. Yes; it would meet that objection, but it would not meet the objection that that is not sufficient security.

Senator BRISTOW. Not sufficient. But suppose it is what the law requires, then what would you say?

Mr. UNTERMYER. The law might require none at all. That would not alter the fact that there is no security behind the currency issue.

Senator BRISTOW. Yes.

Mr. UNTERMYER. And I would still think it was insufficient.

Senator BRISTOW. But you stated that you did not think we ought to take the reliability or the assets of the bank, or the financial strength of the bank, or anything connected with that; we ought simply to look at the security that was presented and issue the currency on that security.

Mr. UNTERMYER. Yes; the security that is presented, with all the backing of one of these regional banks.

Senator BRISTOW. Well, but you are willing to take the strength of the regional banks into consideration but not the strength of an individual bank.

Mr. UNTERMYER. No; not the strength of the regional bank alone, but the strength of the regional bank together with the strength of all the constituent members of that bank. That is what you get when you issue security to a regional bank. You get the uncalled capital of all those banks. You get the law of averages. You get a variety of factors that do not begin to come into existence when you are dealing with a single bank.

Senator BRISTOW. You get no more factors that are not in existence than when you deal with the individual bank, except that you are dealing with a larger amount, or a number of those factors—a greater aggregate of those factors—and they are standing for a greater aggregate of debts, are they not? The individual bank might take out $50,000 in currency; the regional bank might take out $5,000,000 or $10,000,000 or $20,000,000.

Mr. UNTERMYER. But you are getting all the reserves; you are getting no reserves when you take the case of the individual bank.

Senator REED. Why not?

Mr. UNTERMYER. You are getting the reserves that belong to that one bank.

Senator REED. Yes.

Mr. UNTERMYER. But I am talking about the general average.

Senator BRISTOW. You are simply getting the aggregate of the reserves, then, behind the currency of all the banks instead of the reserves of one bank behind its individual currency.

Mr. UNTERMYER. And you are getting the uncalled liability.

Senator BRISTOW. The uncalled liability is 10 per cent, and behind the individual bank you have got all its liability.

Mr. UNTERMYER. So you have in these cases, because you have got the liability of that individual bank behind it. In other words, when the Government discounts paper for a regional reserve bank it has the indorsement of the member banks on that paper, and its entire uncalled liability.

Senator BRISTOW. Yes?

Mr. UNTERMYER. Apart from the 10 per cent uncalled liability of all the members.

Senator BRISTOW. Yes. There is this element which I recognize, that you have got the obligation of all of these banks combined. They are on each other's paper to sustain a volume of, we will say, $20,000,000 or $25,000,000 currency—or perhaps $10,000,000—whatever it might be, while in the individual bank you have got the same assets, the same quality of security for a limited amount of liability?

Mr. UNTERMYER. No; you have a very much inferior quality of security; you have at least 2,000 times the security when you discount for a regional bank that you have got if you discount for a single bank.

Senator REED. Two thousand times?

Mr. UNTERMYER. Yes; assuming that there are 2,000 members.

Senator BRISTOW. How do you get that?

Mr. UNTERMYER. Assuming that there are 12 regional banks, and that they are equally distributed, when the 25,000 banks of the country are distributed among the 12 regional banks it will give about 2,000 member banks for each regional bank.

Senator REED. You surely have omitted in that calculation one of the elements.

Mr. UNTERMYER. What is that, sir?

Senator REED. When a regional bank, composed of 600 member banks, is created.

Mr. UNTERMYER. I am assuming that all the banks come in.

Senator REED. I am talking about one region, now.

Mr. UNTERMYER. So am I.

Senator REED. And that will take in about 600 national banks.

Mr. UNTERMYER. I am assuming that the State institutions come in.

Senator REED. The plan will certainly work, for calculation purposes, with the 600 national banks. Now, you might assume that all the other banks came in, but that is a violent assumption.

Mr. UNTERMYER. I do not agree with you, and I do not think the thing will succeed unless substantially all the banks join, as I think they will be forced to do in self-defense.

Senator REED. And we might assume on the other hand that all the banks will stay out, which would be another violent assumption. I am taking the national banks (and they will all come in on an equivalent basis), and we will have this situation; and I think for the purpose of the illustration it does not make any difference how many come in. The regional bank is an institution existing by itself. The member banks are not joint partners and are not liable under the laws of partnership. They are stockholders, and their liability, therefore, is limited to the amount they have contributed to this corporation in the way of capital stock paid in.

Senator NELSON. And to the 10 per cent call.

Senator REED. And, second, to the 10 per cent call. Therefore, the primary liability or the primary security that is back of, we will say, $5,000,000 issued to the central bank, is the assets of the central bank which amount, now, we will say, to $5,000,000 and the right to call $5,000,000 more. Now, that is the solitary and only thing that is back of that except individual notes indorsed by individual banks.

Mr. UNTERMYER. Yes; with all the assets of that bank.

Senator REED. Now the individual note, indorsed by the individual bank, does not have—in the first place, those notes need not have come in from every bank; they might have been deposited by only a few of these banks. In the second place, that note does not have back of it, by virtue of that indorsement, all of the assets of the individual bank. The individual bank has 1,000 other liabilities and the indorsement is utterly worthless if the bank is utterly worthless, and it is worth 25 per cent if the bank's assets will pay out 25 per cent upon all of its liabilities, and it is worth 50 per cent if the bank's assets will pay out 50 per cent on its liabilities. So that you do not have back of this money, under this scheme, the aggregate capital of all the member banks.

Senator NELSON. In other words, they are not jointly and severally liable as indorsers.

Senator REED. That is exactly it.

Mr. UNTERMYER. I have not said that they were.

Senator REED. Oh, you have said 2,000 times the amount, and you can not get there.

Mr. UNTERMYER. Yes; I will get there. In the first place, when I said 2,000 times the security, I figured upon every bank being in the system—that is, in the 12 regional banks—and the regional banks would then have 2,000 member banks each.

Mr. BRISTOW. Now, Mr. Untermyer, may I interrupt you?

Mr. UNTERMYER. May I not answer Senator Reed? I think I am entitled to do so. I do not say the Government would be the sole creditor of the individual bank. I answered Senator Bristow's suggestion that the stock liability of that bank—that is, its liability for an amount equal to the par value of its capital—would be an asset available to the Government just as it would be an asset available to the Government in the case of discounts made directly for that bank, and so it would be. In other words, the Government would have behind this obligation all the assets of the reserve bank, and it would also be a creditor of the individual bank and would be entitled to a proportionate share of whatever came out of this stock liability. Now, when I say that the responsibility is 2,000 times that of the single bank, what I mean is that when the reserve bank is discounting paper for 2,000 banks if one bank goes by the board its chance of loss would be one two-thousandths of what that would be if it had only that one bank for which it was discounting. I think I am entirely right in that when you speak of the doctrine of averages.

Senator REED. Isn't this just where you come out, Mr. Untermyer? The First National Bank of Pittsburgh, for the purpose of this illustration, having a capital stock of $1,000,000, takes $1,000,000 of securities to the regional bank and indorses that $1,000,000 of paper. Now you have $1,000,000 of individual notes indorsed by a bank with $1,000,000 of capital, and that security in that shape is taken to the regional bank. Thereupon the regional bank indorses it. You have back of that particular note issue the $5,000,000 of capital of the regional bank and the $5,000,000 that can be called as against the regional bank.

Mr. UNTERMYER. And the deposits of the regional bank.

Senator REED. And that is taken to the Federal Government and the money issued.

Mr. UNTERMYER. You have omitted, of course, the reserves of the bank, if that is an obligation of the regional bank.

Senator REED. Of 33 per cent.

Mr. UNTERMYER. No; I mean of the 100 per cent, the entire reserves that are on deposit, the deposits in the regional banks, of all the banks——

Senator REED. Are included.

Mr. UNTERMYER. Are behind that loan.

Senator REED. Very well; you have this, and that does make an excellent security when we assume that all the other banks stand up, and that all that security lies there intact and unimpaired back of that $1,000,000.

Mr. UNTERMYER. It is a good security if half of them fall down.

Senator REED. Yes; but in the last analysis, what you have back of that money is the individual's note, the indorsement of the individual bank, and the assets of the regional bank. You do not have the assets of all of the banks, do you?

Mr. UNTERMYER. No; you do not have the assets of all of the banks.

Senator REED. You do not have the assets of all of the banks?

Mr. UNTERMYER. Except that part of them which is on deposit with the regional bank.

Senator REED. I understand we have already used that up. Now, we will take the case of the individual bank—this same individual bank. Well, before I do that——

Mr. UNTERMYER. Senator Reed, are you not losing sight, if I may suggest, of the all-important point, the doctrine of averages, nor of the fact that the reserves of the country can not be mobilized under your plan nor taken away from New York nor made useful to the commerce of the country?

Senator REED. Yes; but I am going now to suggest a counter danger. Suppose that this regional bank not only gets money issued in this way that I have suggested for the First National Bank of Pittsburgh, but that it gets approximately the same amount of money for all of the banks of that district. Of course in that event the assets of each of these banks would have to be added to the security. And just in proportion as you issue that money to the member banks the value of the security is lessened, so far as the regional bank's assets are concerned.

Mr. UNTERMYER. There is not any doubt of that.

Senator REED (continuing). Because the regional bank stock security becomes proportionately less and the regional bank's assets being in fact the assets of the member banks, and nothing more, it is of course finally reduced to a proposition, under this illustration, that you have got back of all of this money all the assets of all of the individual banks, and nothing more, because the assets of the individual banks swallow up the reserve bank. Now, suppose that there come some great crash, whereby the banks are closed, as they were in 1907, and this money—gold is demanded for it. You have a system, now, so tied together that if that regional bank goes down and can not redeem this money your currency has gone to pieces, haven't you?

Mr. UNTERMYER. Yes; certainly, if all the reserve banks go down. You could not have any system that would not have an element of that kind in it. There is no known system.

Senator REED. Suppose you take this as a separate transaction. Mind you, in this first illustration we have been using there is absolutely no limit upon the amount of money which may be issued, except the promissory notes—the limit fixed to the promissory notes. You can keep on issuing money as long as there are promissory notes to be deposited, if it is 5 million, 10 million, 1 billon, or 10 billion.

Mr. UNTERMYER. You mean in the regional-bank system?

Senator REED. You can in the regional-bank system.

Mr. UNTERMYER. I do not agree with you.

Senator REED. The Government, under this law, as long as there is what is called commercial paper, no matter if it goes to $10,000,000,000, can continue to issue money.

Mr. UNTERMYER. Yes; but it has a discretion.

Senator REED. But you can pyramid your credits. That is to say, now——

Mr. UNTERMYER. You have got to have your gold reserve, have you not?

Senator REED. Yes. That is to say, you can pyramid your credits in this way: You have $1,000,000 of promissory notes and you put them up and get $1,000,000 of currency. You thereupon set aside 33 per cent as a gold reserve, loan out $666,000 and get more promissory notes. You bring those notes back to the bank and come down to the Government and you get $666,000 of paper money. You take out one-third of that, $222,000, and that leaves you $444,000. You loan that out again and you get some more promissory notes, and you can repeat that operation. Have you figured out how much money can actually be issued until the gold reserve is exhausted?

Mr. UNTERMYER. I think there are a number of big holes in that argument, Senator, if I may suggest. One of them I can puncture now by reminding you that you have got to have paper all the time that is maturing within 90 days, so that new paper is coming in and old notes are being paid off.

Senator REED. And just as it comes in now, with an enterprising banker.

Mr. UNTERMYER. In the next place, you are ignoring the fact that there is somebody in control of this system. There are people who are supposed to see to that.

Senator REED. Yes; I know.

Mr. UNTERMYER. You can take any proposition within the range of finance, business, or science, and deal with it in that way and bring it down to a logical absurdity.

Senator REED. We are trying to build up a system here that is safe.

Mr. UNTERMYER. Safe if properly administered; but no system is safe if not properly administered.

Senator REED. We are trying to build a system that, if made unsafe, the law must be absolutely breached. That ought to be the system we are building.

Mr. UNTERMYER. A single bank, you know, could do the same thing you are talking about.

Senator REED. Wait a moment, now. I differ from you. I am talking about possibilities now and what can be legally done under this law. You can keep on with this system of piling credit upon credit until the 33 per cent gold reserve has ultimately eaten up your power.

Mr. UNTERMYER. I differ from you. I do not think you can do anything of the kind.

Senator REED. Why can not it be done within the law?

Mr. UNTERMYER. I will tell you why. Because, in the first place, you must have genuine commercial paper on which to base your currency. If you have genuine commercial paper to give the Government all the time, that means that the country needs that currency for legitimate purposes. In the second place, the term of the paper is so brief that you can not accumulate any such amount of it in the succession of transactions you have suggested. That is a fictitious illustration that could not occur in the course of events; and, in the third place, all checks of Government control that would render such a situation impossible are ignored. You have all the bars down. You are assuming everybody is away; everything is open, that all they have got to do there is to put something in the slot and automatically pull currency out.

Senator REED. Now, you are too good a lawyer to mistake my illustration. In the first place, I am dealing with the possibilities of the law.

Mr. UNTERMYER. I know you are.

Senator REED. I am leaving out this wise, prudent, supervision which we hope and pray for, but which may or may not always exist.

Mr. UNTERMYER. Every country would be bankrupt if we acted on the assumption that discretion did not exist in the direction of public affairs.

Senator REED. The only limit that is put in this bill on the amount of money that can be issued is the $33\frac{1}{3}$ per cent gold reserve which must be set aside.

Mr. UNTERMYER. And the character of the paper.

Senator REED. And the character of the paper.

Mr. UNTERMYER. That is the essential thing.

Senator REED. Now, you think we have finally reached a time when that class of paper, which is here denominated commercial paper, would no longer exist.

Mr. UNTERMYER. I am not speaking of the paper here denominated, because the paper here denominated, Senator Reed, is too loosely denominated.

Senator REED. Very well.

Mr. UNTERMYER. I am speaking of the paper that you have denominated.

Senator REED. The paper you would denominate as prime commercial paper. Now, you can not tell us the amount of that prime commercial paper that is in circulation now, or that has been in circulation at any period of the country's history, can you?

Mr. UNTERMYER. No; and I do not know that there are——

Senator REED. There is not a human being on this earth that can approximate it, is there?

Mr. UNTERMYER. I do not think so.

Senator REED. Then we are proposing, under this bill, to issue a currency the limit to which, under the law, is a $33\frac{1}{3}$ per cent gold reserve, which, I grant you, is a limit to that extent on the amount of commercial paper; and nobody knows, and nobody can make an approximate estimate, of the amount of that commercial paper.

Mr. UNTERMYER. But you have got a check on the amount that can be issued in the fact that the regional reserve bank is not going to allow inflation in its district. If it chooses to do so, the Government is not going to allow undue inflation. It has a right to stop and say, "We won't do any more."

Senator REED. That comes back again not to what the bill requires, but what the managers may do.

Mr. UNTERMYER. There is no system that can be devised on any other basis.

Senator REED. I think I have one.

Mr. UNTERMYER. Well, the world will acclaim you.

Senator REED. No they won't acclaim me.

Mr. UNTERMYER. Oh, yes; all nations will acclaim you.

Senator REED. It is not anything marvelous now; it has been already suggested. I am coming now to the suggestion of Senator Hitchcock.

A bank can not organize, in the first place, under the law without putting up its capital stock in cash against it.

Mr. UNTERMYER. No; it can not.

Senator REED. And, as long as it does put up its capital stock in good hard coin of the realm, that is solid, isn't it?

Mr. UNTERMYER. Until it is punctured.

Senator REED. Until it is punctured, stolen, or carried away.

Mr. UNTERMYER. Or legitimately lost.

Senator REED. You need not have injected that into it, because that is true of your regional bank. That is true of the Federal Treasury; that is true under any banking laws and that is true everywhere; and where it is lost in a bank, if we have any kind of Government supervision, it is going to be found out it is lost, and then we cease doing business with that concern.

So let us come back and get down to the question of the hard dollars that are paid in, and let us say it is $1,000,000 of gold coin, the paper that is as good as gold, issued by the Government. We have that.

Mr. UNTERMYER. You mean that a bank starts with a million of capital.

Senator REED. Yes. It is not possible, now, to conceive of so many banks being organized and money paid in that we run away there, because there is a limit to the money that is paid into it—a natural limit. We have a total liability, then, of the stockholders of $2,000,000, $1,000,000 of which is absolutely in the Treasury and $1,000,000 of which is in the liability of these men. Now, a bank thus organized wants, under Senator Hitchcock's suggestion, some money. It goes down to the Federal Treasury and shows it has this unimpaired capital, and it gets $750,000 of paper currency issued to it—no; $500,000 of paper currency issued to it. And what was your gold reserve?

Senator HITCHCOCK. I did not discuss the question of the gold reserve.

Senator REED. I am going to assume that it gets $500,000 of capital currency issued to it and has a 50 per cent gold reserve.

Mr. UNTERMYER. You mean in its vaults.

Senator REED. Yes. It is required to keep back, out of the money it gets, a gold reserve equal to 50 per cent.

Mr. UNTERMYER. But it offers no security for this money.

Senator REED. Just wait a moment. In order to get this money it is limited to three-quarters of its capital stock. It has got to do two things. It has got to create a gold reserve of 50 per cent and it has got to put up notes of its customers for the other 50 per cent. Now, I am talking about the question of inflation, of the creating of a system that won't run away, and that bad management, less stealing, will not permit to run away. Your note issue in that event is absolutely limited to 50 per cent of the capital of the national banks.

Mr. UNTERMYER. It is an inelastic currency; it is worse than the present currency.

Senator REED. Let us see if it is inelastic. Let us be fair.

Mr. UNTERMYER. That is what I assume, that you want to be fair——

Senator REED. Certainly.

Mr. UNTERMYER. And you must assume I want to be fair.

Senator REED. Your currency you are discussing under this bill is inelastic when it reaches a point where the gold reserve and the lack of commercial paper has put the brakes on. It ceases at that point to be elastic.

Mr. UNTERMYER. No; it has supplied the commercial needs. In other words, it is measured by the amount of genuine commercial paper that is outstanding instead of being measured by the capital of the bank.

Senator REED. Let us see if the other is not equally elastic, though working upon a different principle. There is money enough in the country to-day to fairly transact the business of the country—to meet the demands of business. You are a banker and you want more money. Why? Because your customers need it. You go down to the Federal Treasury to get it, and when the Federal Treasury issues it to you they charge you interest, and you will not take the money out unless you can use it and make more interest than the Federal Government is charging you. If you keep the money longer than a certain length of time, the interest rate is raised. Now you have got to the place where you can get money when it is necessary, hence you can extend it. You can stretch the rubber band, as somebody said the other day. You then, by virtue of these interest charges, are going to curtail it; you are bound to bring it back within a given time; and you have a currency that will expand every time the bankers find they need the money for legitimate business; and you have a currency they are compelled to contract whenever the interest rates get high enough. And is not that elastic?

Mr. UNTERMYER. No.

Senator REED. Then you and I differ in our conclusions.

Senator NELSON. That is the Vreeland bill.

Senator REED. Certainly; it has the principle of the Vreeland bill in it.

Mr. UNTERMYER. Except it is more liberal in the character of security than the Vreeland bill. The objections are these, if I may say: In the first place, the automatic increase of the interest rate may be such a great hardship upon business that it does not furnish elasticity at all. Business may need money—legitimately need it—legitimately expanding business—and if you are going to put a prohibition upon it by a purely ascending rate of interest that is automatic at given times you are not going to supply the needs of business at all. That is No. 1.

Senator REED. But, Mr. Untermyer——

Mr. UNTERMYER. Won't you let me finish?

Senator REED. I will; but I think we might get along better——

Mr. UNTERMYER. I think you might let me finish one answer, because I have not been able to do so thus far.

Senator REED. I want to get your opinion upon it. You and I are not trying to fence.

Mr. UNTERMYER. Certainly not.

Senator REED. Suppose we raise that interest every month, two months, or three months, a certain amount and we put in this discretionary element to leave it to some central bank to raise the interest as that board thought it necessary. That would be leaving it to some Federal board to raise the interest as that board thought it was necessary.

Mr. UNTERMYER. That you are doing now under this bill.

Senator REED. Suppose you added that.

Mr. UNTERMYER. Let us just take your illustration and see what a dangerous sort of security that would be. It is secured really only to the extent of 50 per cent. The rest of the other security is in the way, as I understand it, of commercial paper and the stock liability of the bank. Is not that right?

Senator REED. I do not agree with you on that.

Mr. UNTERMYER. Is not that your illustration. As I understand it, you say you would take commercial paper for the currency which would be issued at par, and 50 per cent of that would have to go into a gold reserve and the other 50 per cent would be available for general use——

Senator REED. Yes.

Mr. UNTERMYER (continuing). As against that $100,000 of currency we will say you would issue and you would present $100,000 of notes, and $50,000 would have to go into a gold reserve and the other $50,000 would——

Senator REED. Now, we have $50,000 of liability, because the gold reserve takes care of the other $50,000.

Mr. UNTERMYER. Yes.

Senator REED. What is back of that $50,000?

Mr. UNTERMYER. This $100,000 of notes and the stock liability of the bank.

Senator REED. Yes; and the bank's capital.

Mr. UNTERMYER. And the bank's assets.

Senator REED. Five to one, is it not?

Mr. UNTERMYER. You assume that you would borrow $1,000,000, or $750,000?

Senator REED. I took $1,000,000 capital. You just went to the $100,000 illustration, and I went there with you.

Mr. UNTERMYER. Now, then, so far as concerns the stock liability the uncalled liability of individuals on stock, I think, that the experience of the Comptroller of the Currency demonstrates that that is not a very collectable asset were you to ask for it.

Senator REED. That is true of the regional bank system.

Mr. UNTERMYER. That is true of the regional bank system, because your 10 per cent individual capital is payable by the bank.

Senator REED. That is, however, of no value for the banking business.

Mr. UNTERMYER. It is only to pay 10 per cent, and it has 100 per cent to collect; so that it is 10 for 1 which it is able to collect.

Senator REED. Our lien is not prior to the other liens on that.

Mr. UNTERMYER. Yes; you have a prior lien on everything of the bank, as I understand it—for the 10 per cent; not for the general stock liability—so that the uncalled stock liability of individuals in a failed bank experience has not shown to be a very valuable or tangible asset.

Now, all you have left behind this currency are the notes—the assets of that one bank and the promissory notes or the bills that have been put behind it. You would not have anything like the security that is offered by this bill.

Senator REED. On the contrary, I think it is better; and I think it is better for this reason—I have got some figures on it——

Mr. UNTERMYER. Of course, you are assuming that the Government is a preferred creditor in every event.

Senator REED. I mean that the Government is a preferred creditor, and if I were drawing this bill I would make it a preferred creditor not only for the stock bank, not only as far as the currency is concerned, not only for the double liability, but for every asset the bank has.

Mr. UNTERMYER. I think that is wise.

Senator REED. If you do that and you have any kind of an inspection at all I insist that, barring plain, cold larceny, you are bound to have ample security; and for this reason: Here is a bank with $1,000,000 capital. It is to be inspected. If that inspection shows that the bank has not got deposits at least equal to its stock—in fact, four times the amount of its stock—then any bank examiner in the world would know that that institution was rotten to the core. He would not need to know any more.

Mr. Untermyer. But when trouble comes I tell you those deposits disappear pretty rapidly.

Senator Reed. They may.

Mr. Untermyer. You can not count on those deposits. One of the reasons why I say it is not comparable to the security offered by this bill is because of the law of averages, because of the fact that when you have 2,000 banks in one regional reserve bank and 1 fails, or a dozen or 20 fail, it is not as though the Government had a separate loan with each bank, where, if one bank fails it can not make it up out of the others. There is not any resort to the law of averages there, which would tend to the safety of the issue.

Senator Reed. I understand, Mr. Untermyer, perfectly, and I frankly concede that just to the extent that the regional bank has capital and its indorsement of this paper it puts up with the Government adds to the value of the paper.

Mr. Untermyer. But, apart from the question, Senator Reed, of the capital, still more important and a still greater security by far than the capital or the assets of the regional bank is the fact that it has, we will say, 2,000 banks, and they are not all going to fail. Whereas if the Government is dealing with each bank separately it is dealing on the assets of each bank, while if it is dealing with one institution that has all the assets of 2,000 banks it is dealing on the law of averages, which is the only safe law upon which to conduct a financial transaction of that kind. There can be no question about that.

Senator Reed. Let us understand this: You do not mean to say that if a regional bank gets a billion dollars of money issued to it that all of the assets of the 2,000 member banks is liable for that billion dollars?

Mr. Untermyer. No; not at all. I never have suggested such a thing. What I do mean is that if it gets a billion dollars of bills receivable or bills of exchange, that the chances of loss among those hundreds of thousands of bills of exchange are mimimized against the bills of exchange of one individual bank in one city or one locality affected by one catastrophe.

Senator Reed. But now, following that out, we will assume that one member bank, in dealing with the Federal Government, puts off upon the Federal Government a lot of bad paper and the Government loses its money. It might do the same thing to the regional bank, might it not?

Mr. Untermyer. The loss would not be appreciable.

Senator Reed. I am talking about what it can do to the regional bank. It might do the same thing to the regional bank it does to the Government, and the loss, instead of falling directly upon the Government, would fall upon the regional bank.

Mr. Untermyer. Yes.

Senator REED. You say the regional bank can stand that because it has so many banks and is dealing with so many banks that the loss would be distributed.

Mr. UNTERMYER. It would be infinitesimal.

Senator REED. If it is infinitesimal to a regional bank with 2,000 member banks, it would be equally infinitesimal to the Federal Government dealing with not 2,000 banks but with 25,000 banks.

Mr. UNTERMYER. On the contrary, in the one instance the Federal bank does not sustain any loss; in the other instance, the Federal bank does. The regional bank has to take that loss.

Senator REED. Do you think the regional bank can stand that loss?

Mr. UNTERMYER. Very readily.

Senator REED. If the regional bank, that has no assets except that which it gets from the bank, can stand that loss and can afford to stand that loss because it is distributed in the way you have spoken of, why can not the Federal Government.

Mr. UNTERMYER. In the first place, the regional bank is making it up; it is earning money against that loss. In the second place, and still more important, the currency of the Government must have such confidence that there must not be the possibility of any loss occurring in any security for which the currency is issued. As soon as there is a possibility of such a thing the currency loses value and stability. But still more important, and what is in itself fatal to your plan, without regard to the many other considerations that in my judgment renders it impossible, is the fact that you provide no means of mobilizing the reserves. Are they to be used as now, by being sent to New York for stock speculation, instead of remaining, as they do under the bill, where they belong and for the use of legitimate business there?

Senator REED. Let us go back to the question of how the regional bank can sustain the loss. You say because it is making money. It has an income. Now, if the Federal Government issued its money direct and charged an interest for it, it would have an income, would it not?

Mr. UNTERMYER. Yes.

Senator REED. And if we take the loss. If we take the law of averages, of bank failures, total failures of national banks, or partial failures, they do not amount in the aggregate—I am taking the average over the years—to more than about——

Senator BRISTOW. One-twentieth of 1 per cent for the last 50 years.

Senator REED. One-twentieth of 1 per cent for the last 50 years of deposits, which, of course, could not be exactly applied to the currency which would be issued, but it shows the amount and I believe, you said, that 2 per cent collected upon the notes would make up, and more than make up this loss.

Mr. UNTERMYER. I can imagine it would more than make it up; but there is another consideration that I think you have left out of sight, and that is that the Government should not have imposed upon it the task of passing upon the character of commercial paper which would be presented to it. That is another question.

Senator REED. Let us stick to the question we are now considering.

Mr. UNTERMYER. There are dozens of consideration that occur to one against, the practicability of such a plan.

Senator REED. Let us thrash them out one at a time. Let us stick to the question of whether the Government can afford to do it. If 2 per cent would create a fund that would take care of the failures and the Government should loan its money out, at say, 4 per cent, then we would get a fund that would take care of the failures two or three times over and with the great law of averages, namely, that where you have 25,000 banks, the chances of failure are distributed and the income comes in from all the 25,000 banks to meet the failure of the one. I want to know now, why the Government of the United States can not do that safely so far as this one consideration is concerned.

Mr. UNTERMYER. So far as the one consideration is concerned it can. If you want to limit it to that, it can be done. It would lead to the grossest inflation.

Senator REED. Why, my dear sir, you are proposing a system here that has no limit upon it except the gold reserve which you make 33 per cent. In this case I have made the gold reserve 50 per cent. Your other limitation is simply the amount of commercial paper there may be in the country.

Mr. UNTERMYER. And the discretion of men vested with the administration of the law.

Senator REED. Very well. I have limited this to three-quarters of the bank capital and the discretion of these wise and prudent men who are never going to make a mistake in my case any more than they will in yours, but in both cases likely.

Mr. UNTERMYER. No; in the case of the present bill, Senator Reed, these men have not had imposed upon them the discretion of passing upon this paper. That discretion is exercised where the paper is passed upon.

Senator REED. You are going now to the question of passing upon paper. I am talking about the amount of currency and I insist that you have already said, Mr. Untermyer, that the difficulty with the system I am now discussing is that it is inflexible because its limits are absolutely fixed by the bank capital, and yet how can you say in one and the same breath logically that it is inflexible, because the bank capital absolutely limits, and in the next breath say that it opens the door for every kind of inflation.

Mr. UNTERMYER. That is only one of many objections to it.

Senator REED. I am speaking about that one; I want to come to the next one now.

Mr. UNTERMYER. Senator Reed, it is inflexible from the point of view that it is limited by the capital of the bank, and it is liable to inflation from the point of view that you are imposing upon the Government a duty of passing upon this commercial paper, for which it has not the machinery and is unable to supervise. It is not a governmental function.

Senator REED. Very well. Now, I am coming to the question of passing on commercial paper. In the last analysis whether a man is the agent of a bank or an agent of the Federal Government, he is simply a human being, with body, parts, and passions, and all these things have to be worked out through human agencies. That is true. I guess we will agree on that without any further talk.

Mr. UNTERMYER. That is certainly true.

Senator REED. A number of very fine gentlemen, nine of them, are put in as directors of a regional bank; three of them are practical bankers, picked by the banks, the other six are something else. The minority of this board are practical bankers.

Mr. UNTERMYER. I think that a good merchant is as good a banker as any banker. A merchant extends credit of merchandise just as a banker extends the credits of money, and many merchants have finances that are much larger than that of all the banks with which they deal.

Senator REED. That is true.

Mr. UNTERMYER. All this legerdemain about banking and expert banking and all that sort of thing seems to me much overdrawn.

Senator REED. You think a man with good common sense and some business experience can be trusted almost as well as a banker.

Mr. UNTERMYER. I think fully as well as a banker.

Senator REED. You think fully as well.

Mr. UNTERMYER. I do not say that he understands the science of finance necessarily. Of course, banking and finance are somewhat different.

Senator REED. Well, I understand now your reason for differentiating, because a moment ago, Mr. Untermyer, when I was trying to say that this board would only have a minority of practical bankers upon it you at once brought forward the idea that the other men on it might be even wiser than the bankers.

Mr. UNTERMYER. I do not believe I made any such suggestion, Senator Reed. Perhaps you thought you were going to ask me some question of that kind.

Senator REED. No; when you read the record you will find that I am pretty nearly correct. Now, this macinery does have in it an element of great merit, which I frankly admit, namely, that practically the three bankers who are on that board must realize that if they take bad paper from member banks they are liable to injure not only the bank of which they are directors but they are at the same time financially interested in it, and hence I freely grant you they will use all reasonable precaution. I want to concede to this bill wherever there is a virtue, I want to concede that virtue.

Mr. UNTERMYER. I think the virtue lies largely in the other members of the board.

Senator REED. You do?

Mr. UNTERMYER. Yes.

Senator REED. You think they are better than the bankers?

Mr. UNTERMYER. Well, I think they have less interest, because they have no paper to discount and they are supposed to represent the public interest and the commercial and industrial interests of the country.

Senator REED. And you think that, respresenting the commercial and industrial interests of the country, they are a little more to be trusted to manage this system than the bankers, who have financial interest?

Mr. UNTERMYER. I do not say that they are more to be trusted in any such sense as might be implied. I have no doubt that everybody who acts on that board will be entitled to be trusted. What I mean is, that while the bankers represent their own interests, though their financial holdings are comparatively small in this institution, they are also people who will borrow money, while the other directors will have an entirely disinterested public point of view.

Senator Reed. And you think therefore they are a little safer because of that fact.

Mr. Untermyer. Certainly; fully as safe.

Senator Reed. Very well. Now we have got to the point, and I want to nail this point down, because I am going to use it as a point to reason from. Good men selected outside of the bankers are a little bit safer to manage a system of this kind than the bankers themselves, and now I proceed——

Mr. Untermyer. I said fully as safe.

Senator Reed. All right. I will proceed from that point. This Federal reserve bank is located now, for the purpose of my illustration, in the city of St. Louis, in my State, and its territory embraces all of Misouri, Kansas, Oklahoma, and Nebraska, and that is about the territory it would embrace. That is a territory in which you can take all of Germany, all of France, and the Island of England and drop them down and have a little bit of space left on the side, if my geography has not become clouded. There will be within that territory about 600 national banks. They will be, many of them, 300 and 400 miles from St. Louis. How is that board of directors of that regional bank to keep in touch and have a knowledge of the business, the liability, and the safety of these various banks? It must have some machinery. What would be the machinery?

Mr. Untermyer. It ought very largely, in a general way, to know about its customers. That is one of the advantages of 12 reserve banks over 4 or 5.

Senator Reed. I know it ought to know; but I am asking you how it will know and what will be the method?

Mr. Untermyer. It will have statements from these banks all the time. There will be men among these nine men who will be selected from the different regions. They will know the banks in their own region pretty well.

Senator Reed. Do you think any one man will know, of his own personal knowledge?

Mr. Untermyer. All of them should know. Among the nine men they will know. It is a less diversified knowledge than among the great banks of to-day.

Senator Nelson. You mean more diversified?

Mr. Untermyer. No; it is a less diversified knowledge than would be required of the heads of some of the banks of to-day that have thousands of depositors scattered all over the country. Some of the great banks have a vast number of depositors. It will have less depositors and, I think, it will have better occasion to know in a general way about the conditions in that section.

Senator Reed. But you do think that those nine men who are generally scattered in their selection over this vast empire of country I have described—for it is an empire, and that part that Senator Bristow and I live in, and I will have to include Nebraska, too, is a mighty good empire.

Mr. Untermyer. Haven't you included a pretty large territory for your regional bank?

Senator Reed. No, sir; I think that is just about what would come in.

Mr. UNTERMYER. That would be more than one-twelfth of the territory of the United States, would it not?

Senator REED. We are in area, but I do not think we are when you come to the question of the number of banks.

But you think that those nine men could keep track of the financial conditions of these various member banks reasonably well, so that they would be able to—if they could not pass upon the particular paper brought to them by the banks—that they would at least know the bank's standing, the kind of management it had, whether it was a safe, prudent management, and whether its statement from time to time made showed that it was in a healthy condition.

Mr. UNTERMYER. Within a very few years, with the aid of the bank examinations that are required under the act, that will be true.

Senator REED. Yes. Now, I agree that they can keep a pretty close check. Do you know of any reason why if this other system that we have been discussing was adopted the Government of the United States could not form a board of nine men and through that board have exactly the same kind of intimate knowledge which would be possessed by these nine men who are directors of the regional banks?

Mr. UNTERMYER. No reason why they could not set up the same system in some other form if they choose.

Senator REED. A system which embraces the employment or requires the employment of 150 or 200 supervisors or directors will cost the banks of the country a little more.

Mr. UNTERMYER. Yes.

Senator REED. And that expense would ultimately fall on the man who does business with the bank, will it not?

Mr. UNTERMYER. Yes; any system is bound to do that.

Senator REED. Certainly; it has to go there. If the Government was able to establish the same system, it would pay the same number of men and it would not have to pay any more for that, would it?

Mr. UNTERMYER. Yes; there is no doubt of that; of course it would not be anything like as responsible a system. It would not be a local government of finance.

Senator REED. Let us see. You have said that the six members of this board who could best be trusted, or at least as well be trusted, as the bankers themselves, as the men who were not bankers.

Mr. UNTERMYER. There is no doubt about that.

Senator REED. I want to know whether it is impossible for the Federal Government, through the Treasury Department or some other great board that may be established as a permanent board, to pick wise and prudent men just as well as the bankers might pick them.

Mr. UNTERMYER. I have always felt that the Government could do it better.

Senator REED. Now, I think you have got to this point: That it is best for the Government to have an inspection system; it is best for the Government to know about the individual bank; and it is best for the Government to transact all of its business, and that it can do it as safely as the banks would do it.

Mr. UNTERMYER. If they would set up something like the same system, yes.

Senator REED. Very well.

Mr. UNTERMYER. We are discussing this system and not some other system.

Senator REED. Very well; but I am talking about whether there can not be a system that will protect the Government if the Government sees fit to issue money to individual banks, allowing that bank to preserve its independent character, and never for a moment making it subservient to any other bank or combination of banks, but allowing it to go to the Government directly for its assistance.

Mr. UNTERMYER. You lose the security of the intermediate institutions and all that implies, so that it is not as safe——

Senator REED. I am coming to that.

Mr. UNTERMYER. Because of that fact.

Senator REED. And you think 2 per cent interest would make that up?

Mr. UNTERMYER. I have not said that 2 per cent interest would make that up. What I said was that a guaranty fund of 2 per cent would undoubtedly cover losses from bad accounts.

Senator REED. Now, let us take these figures. Let us have a Federal reserve bank.

Mr. UNTERMYER. You are going to let me go this afternoon, because I have got to go. I mean the committee is, because I have not yet really made the statement I was asked to make.

Senator REED. Really, Mr. Untermyer, I do not like to take your time.

Mr. UNTERMYER. I am very glad to be able to give you any information at my command.

Senator REED. And I appreciate your attendance, and I would not dwell upon this matter, but I think the influence of your statement here may be very great with this committee and with the country.

Mr. UNTERMYER. You understand me, Senator. I am glad to give the committee as much of my time as they desire, but if I can not get through this afternoon in time I would rather come again some other time and suit the convenience of the committee.

Senator REED. Very well. As I said, I think your statement may have influence, and weighty influence, with the committee and possibly with the country, and I am frank to say that some of your opinions are—well, I do not think very sound, or, rather, I think they are extreme upon certain things; and that is the reason I am asking these questions.

Mr. UNTERMYER. Of course, you know, I reciprocate that.

Senator REED. Undoubtedly; but I am not the witness or the adviser, and if you are mistaken, or if you have an opinion that is not absolutely sound, I would like to get at it.

Mr. UNTERMYER. I should like to see it the other way around, with you as witness and me as counsel. I have not the same opportunity as witness as you have as counsel.

Senator REED. Yes; I think you do; because I think you argue one side of this case better than I can argue the other.

Mr. UNTERMYER. It is very good of you to say that, but I do not feel that way. A witness is at a disadvantage always.

Senator REED. I think the poor committeeman is at the disadvantage in this case. Now, having sufficiently complimented each other, let us proceed.

Mr. UNTERMYER. I have not begun yet.

Senator REED. Coming back to this question, I want to take up the question of the potential note issue of the reserve banks under this plan. Ten per cent of the national-bank capital would create a fund of $105,691,979.

Mr. UNTERMYER. That is, on the theory of the national banks alone?

Senator REED. No; that is 10 per cent of the national bank——

Mr. UNTERMYER. I say that is on the theory of the national banks alone becoming members?

Senator REED. Yes; certainly. We can not figure the other very well now. The minimum deposits would be $356,231,717; the 33⅓ per cent minimum gold reserve, of course, comes out of that, but that makes a total of what I have just given you.

Mr. UNTERMYER. Out of the $356,000,000?

Senator REED. Yes. It makes a total of assets of $461,923,996, and that, under this bill, can sustain a note issue of $1,385,776,085.

Senator BRISTOW. What are those figures again?

Senator REED. $1,385,776,085.

Senator BRISTOW. Of liability?

Senator REED. Of note issue.

Mr. UNTERMYER. How is it you figure that?

Senator REED. Well, I had a gentleman who can figure take the figures I just gave you and then from them see how much money could be issued under this bill, keeping within the law.

Mr. UNTERMYER. I do not see how he figures it. I would like——

Senator NELSON. No man could figure that, Senator Reed, under this law.

Senator REED. You can, the moment you take as a basis—for instance, we can tell the amount of the capital that would be paid in, the 10 per cent, the amount that that would bring in the national banks, which is $105,691,979.

Mr. UNTERMYER. They could loan out all of that.

Senator REED. Now, the minimum deposits; that is, the reserves which the banks are required to put in, would aggregate $356,231,717. That gives you, then, a total $461,923,996. Now, you can take that, and setting aside each time your gold reserve of 33 per cent, you can figure how much money could be issued against it, and it aggregates $1,385,776,085.

Mr. UNTERMYER. I would like to see how that is figured.

Senator REED. I have not the detailed figures, but the gentleman who figured this——

Mr. UNTERMYER. On what principle is it figured?

Senator REED. The figures were made by an actuary, and it is figured upon the principle that now we have got in this bank $461,923,996.

Mr. UNTERMYER. That is $283,000,000 of loanable funds?

Senator NELSON. That is composed, Senator Reed, as I understand your figures, first, of the stock subscription of the member banks; next of the deposits that they are required——

Senator REED. That they are required to put in.

Mr. UNTERMYER. And deducting one-third——

Senator REED. Then this bank starts to the Federal Government to get money, and it borrows or gets from the Federal Government

$461,923,996 of Federal notes, two-thirds of which is put in circulation, setting aside one-third as the gold reserve.

Mr. UNTERMYER. It puts more than two-thirds in circulation, because it does not need to set aside anything against capital—$105,000,000; it puts $283,000,000 in circulation.

Senator NELSON. He is assuming that you issue notes both for the capital and deposits.

Mr. UNTERMYER. Oh, I see.

Senator REED. Yes; I am talking about this potentiality. Then, having loaned this money out, except the gold reserve, it gets new notes of member banks or obligations of member banks, and having those it goes to the Federal Government and gets more money.

Mr. UNTERMYER. How often?

Senator REED. And it repeats that until it has exhausted its ability to get money, by virtue of the 33⅓ per cent having exhausted the fund.

Mr. UNTERMYER. Your actuary proceeded upon a most violent assumption.

Senator REED. I am talking about the possibilities of this bill, and those are the possibilities of the bill.

Mr. UNTERMYER. They are not even the physical possibilities of the bill.

Senator REED. I do not know why.

Mr. UNTERMYER. You would have to have somebody at every branch bank waiting with commercial paper all day and all night and at the reserve banks straight along. You are assuming that you can keep borrowing day and night. The actuary could make as many figures as he pleased on that. This paper has an extreme maturity of 90 days?

Senator REED. Yes.

Mr. UNTERMYER. You have no right to assume it is going to be 90-day paper. It would probably average 45 or 60 days. He has assumed that from the first day that paper was put in as fast as you can get money you have got new notes that you can keep putting in and getting money every day until the paper matures.

Senator REED. Certainly; and while there would be some loss and some variation, for all practical purposes that would be true, because when this bank is running there is a stream of money going out over the counter and notes coming in, and there is no reason why it should not go across the hall to the Federal reserve agent every day with its notes.

Mr. UNTERMYER. And there is a stream of money coming in?

Senator REED. Certainly.

Mr. UNTERMYER. How can any actuary make figures on that basis?

Senator REED. It is perfectly simple.

Mr. UNTERMYER. He can not make figures on that basis.

Senator REED. I have had made the same sort of figures to apply to the other side. I will now take what I call the "Hitchcock plan" for the present—although I do not think he has indorsed this plan, except by suggestion——

Mr. UNTERMYER. Those are unknown factors.

Senator REED. It is unknown in one case, and they are identical in both cases. I am simply approaching the question of security and the amount that could be issued on that capital. You take the plan of Senator Hitchcock, of a possibility of 75 per cent of money being issued equal to 75 per cent of the bank stock, the present bank capital is $1,056,919,742. The potential note issue at 75 per cent would be $792,000,000. The present note issue is $733,692,820, making a potential note issue against this bank capital of $1,555,692,820.

Mr. UNTERMYER. At what figure does the note issue begin—$792,000,000?

Senator REED. Yes.

Mr. UNTERMYER. If you begin in the one instance with $792,000,000 of note issue and in the other instance you only begin with $283,000,000 of note issue, I do not see why under Senator Hitchcock's plan you do not have many times more the amount of paper than you would under the regional reserve.

Senator REED. Because you are absolutely limited by the amount of bank capital in one case, whereas in the other case you are limited only by the amount of commercial paper, which is utterly unknown.

Mr. UNTERMYER. No; you are not in the other case. If I may suggest, you are limited with a beginning of $283,000,000; that is the loanable funds in the regional bank. Under Senator Hitchcock's plan you start with a loanable fund of $792,000,000. So that in the natural course of things, if you take the same figures for both instances, you will have three times as much paper outstanding on your plan.

Senator REED. But when you get it out you can not go on and multiply it in one case, whereas you can in the other.

Mr. UNTERMYER. I do not know why you can not if it keeps coming in and going out.

Senator REED. But you can not go above 75 per cent of that bank capital in one case, whereas in the other you can go up to the amount of commercial paper.

Mr. UNTERMYER. The $1,000,500,000 is doubled 75 per cent, according to that statement. Under Senator Hitchcock's plan you have got double your limit already.

Senator REED. What misleads you and what appears to be misleading in these papers is that there has been used the present bank circulation, which is based upon Government bonds and not upon the stock of the banks.

Mr. UNTERMYER. Has that been done in both these illustrations?

Senator REED. That is carried into this particular bank-circulation plan.

Mr. UNTERMYER. Has it been carried into both these illustrations?

Senator REED. No; it has not been carried in the other, because the other proposes to retire them. This would not propose to retire them.

Mr. UNTERMYER. If you have included the $746,000,000 in the Hitchcock illustration, I can understand the figures.

Senator REED. Certainly.

Mr. UNTERMYER. Otherwise it will remain stationary.

Senator REED. Let us see what security is back of this. If the Federal reserve banks—[After consultation with actuary.] I think I owe to the committee an apology and to the witness. While these figures bear on another matter, they do not bear on this point. They are different illustrations.

Mr. UNTERMYER. I thought so.

Senator REED. And I can follow those through, and I will now, and then come back to this particular point. These sheets were handed to me a moment ago.

Mr. UNTERMYER. Evidently there is something wrong about them.

Senator REED. I am speaking now——

Senator SHAFROTH. Why can you not cut them out of the record?

Senator REED. No; they are all right. I have simply now put these figures in and I do put them in for the purpose of showing the potential note issue under the two plans. Assuming that the minimum of deposits will be made in the reserve banks, if the deposits in the reserve banks are not at the minimum, if they mount to a higher place, then, of course, the note-issuing capacity is multiplied indefinitely. It is dependent upon the amount of deposits, whereas in the case of the national banks obtaining this money under what I will call the "Hitchcock suggestion" their total issuance, including an amount which is now issued upon the Government bonds, would be $1,525,692,820. And that answers the question of fluctuation, and that is what I had those papers prepared for, but I started to introduce them on the other idea, and it is somewhat confusing.

Mr. UNTERMYER. Have you the figures so that I could look at them?

Senator REED. I have not the details, but will give them to you.

Mr. UNTERMYER. I think there is something wrong about them.

Senator REED. I now take up the question of the margin of safety in the two plans. I want to assume the organization of the Federal reserve banks. As they are given to me, this is the result: The capital paid in at 10 per cent would be——

Mr. UNTERMYER. $105,000,000.

Senator NELSON. That is for the 12?

Mr. UNTERMYER. That is for all of them—$105,691,979.

Senator HITCHCOCK. Mr. Untermyer, do I understand you must leave on the 3 o'clock train?

Mr. UNTERMYER. Yes, sir.

Senator HITCHCOCK. Would you be able to come back next week or some later day?

Mr. UNTERMYER. If it is required, Senator Hitchcock, because I have not really outlined in any sort of sequence or logical order the recommendations that I desire.

Senator HITCHCOCK. Mr. Untermyer, about how long would it take you to make your own statement if uninterrupted?

Mr. UNTERMYER. I should think about three-quarters of an hour.

Senator HITCHCOCK. We expect at 3 o'clock to hear some Minnesota gentlemen. The time after you have to leave we shall give up to the Minnesota delegation.

Mr. UNTERMYER. I should like very much to get away at 2 o'clock, if I can.

Senator HITCHCOCK. Two?

Mr. UNTERMYER. Yes; I have another engagement over in one of the departments which I would like to keep.

Senator O'GORMAN. Senator Reed, might I ask a question? Would it interfere with your plan if Mr. Untermyer were allowed to proceed to the completion of his statement and then later take up his interrogation?

Senator REED. It will not when I get through with this question which I now have before me, but I do not want to leave it in this case.

Assuming that all the national banks came in, each regional bank would have approximately $10,000,000 of capital?

Mr. UNTERMYER. A little less than $9,000,000 on an average.

Senator REED. We will assume it is $5,000,000, which the bill requires.

Mr. UNTERMYER. It would be more.

Senator REED. I am just taking the arbitrary figure.

Mr. UNTERMYER. Yes.

Senator REED. The capital subject to liability would be $5,000,000 more; 5 per cent of the deposits would be $35,000,000. That makes a total of $40,000,000 that you actually have, with $5,000,000 that can be called upon, which makes a total of $45,000,000.

Mr. UNTERMYER. How do you make 5 per cent of the deposits $35,000,000? That includes the Government deposits, too, does it not?

Senator REED. No.

Mr. UNTERMYER. Because the reserves will be $356,000,000. That would only be $17,500,000.

Senator NELSON. That is for the whole system; but he spoke of the $5,000,000 for one reserve bank.

Senator REED. I think these figures are accurate on that point.

Senator NELSON. I do not see where you can assume one regional bank would have this $35,000,000.

Mr. UNTERMYER. No.

Senator NELSON. I do not see where you get those figures.

Senator REED. The figures are assumed in both instances upon the same basis for those in the other banks. I am trying to get the margin of safety. Let me state it again. Take a capital of $5,000,000 for a regional bank, and a capital liability of $5,000,000, and at 5 per cent of the deposit would make $35,000,000. That is a total of $40,000,000 actually in the bank, with $5,000,000 in reserve, a total altogether of $45,000,000.

Mr. UNTERMYER. You have not put in the Government deposits at all?

Senator REED. Not at all.

Senator NELSON. That would not be such a great thing if they were distributed equally among 12 banks.

Senator REED. But the Government deposits are not a margin of safety, as far as the Government is concerned; that is a margin of danger to the Government, if there is any danger in it.

Assuming a note issue of $100,000,000, there would be against that a total protection, so far as the bank was concerned, of $45,000,000 and the proceeds of these notes, which would be $145,000,000. There would be in that case a margin of safety of just the $45,000,000 plus the value of the promissory notes that were put up.

Senator NELSON. But where do you get your assumption of $100,000,000 of note issue?

Mr. UNTERMYER. It is an inadmissible assumption.

Senator NELSON. I do not see what that is based on.

Senator REED. Well, the bank can take its paper down—I am trying to get the margin of safety that will exist back of money that is issued by a reserve bank. A reserve bank has its capital stock, which we have assumed to be $5,000,000.

Senator NELSON. Yes.

Senator REED. It has its capital liability, which we have assumed, of course, to be another $5,000,000. We assume its deposits to be $35,000,000.

Senator NELSON. How do you assume it will issue $100,000,000 in notes?

Senator REED. I am simply assuming that, because you have got to assume a figure. I am going to take the same figures and assume the same proportion on a national bank.

Mr. UNTERMYER. You can keep on reducing the margin of safety by increasing the assumption of notes.

Senator REED. You do not understand me, or I do not understand you.

Mr. UNTERMYER. Yes; I think I do.

Senator REED. And I think I might at least be allowed to ask a question, and then if it can not be understood or if it is incorrect that can be pointed out.

Mr. UNTERMYER. Let me apologize.

Senator REED. No; I do not mean that. I am speaking generally about it. I want to get at an accurate result. I asked a gentleman to assume a condition with reference to a reserve bank, and then apply the same assumption and the same proportions to a single Federal bank, and try to arrive at the question of which would give the greater margin of safety for a note issue. If you take a Federal bank with $5,000,000 of capital——

Mr. UNTERMYER. I understand now.

Senator REED. With $5,000,000 of capital that can be called, and assume that it has deposits of 5 per cent. You have $40,000,000 actually in and $5,000,000 of reserves. Assume, now, that it goes down and gets $100,000,000. It puts up for that $100,000,000 a hundred million dollars of notes which it has loaned out, but when it loaned it out it reduced the cash on hand by that amount, so that it has actually back of the $100,000,000 that it got $145,000,000 of assets, or a margin of safety of 45 per cent.

Now, let us apply those figures to a single national bank. It has a capital of $100,000, a stockholder's liability of $100,000, a redemption fund in the Treasury of 5 per cent, or $3,750; it has the notes against which the paper was issued of $75,000; its assets and stockholder's extra liability all aggregate $278,750. Its note issue is $75,000; its margin of safety is $267,000, as this gentleman figures it, instead of $145,000 as the other plan works out.

I am sure that these figures are correct. They were prepared for me by a gentleman who does a good deal of figuring, but they look on the surface to me as though they were actually correct.

Mr. UNTERMYER. I do not think they mean anything.

Senator REED. I would like to have them verified.

Mr. UNTERMYER. They do not mean anything, because they are composed of a variety of assumptions. Of course you can proportion anything if you assume premises, and you must get the conclusion——

Senator BRISTOW. Just a minute.

Senator REED. If you make the same assumption?

Mr. UNTERMYER. It is not the same assumption.

Senator REED. With the same hypothesis in each instance, and then apply the two different plans, and from that you ought to get——

Mr. UNTERMYER. But you have not made the same assumption. You have assumed in the case of the regional bank that it is going to loan out and issue some currency for twenty times its capital, and you have assumed in the other case that it is only going to get currency for three-fourths of its capital.

Senator REED. Exactly, because I have assumed a law that will only let it get 75 per cent of its capital, and in the other case I have assumed that the system is put into effect that we propose to put into effect under this bill.

Mr. UNTERMYER. It stands to reason that if one corporation only borrows three-fourths of its capital and the other borrows twenty times its capital there is going to be a bigger margin of safety to the one that borrows three-fourths than twenty times; but the facts do not warrant that.

Senator REED. That is just the difference between these two systems. One of them proposes to let a reserve borrow, regardless of its capital, and the other proposes that it shall borrow only three-fourths of its capital, setting aside a gold reserve back of every dollar that it does borrow.

Mr. UNTERMYER. But in the case of the regional reserve you have omitted a number of elements of safety when you say the margin of safety is 145 to 100. You have assumed that there are $1,300,000 of commercial paper in the country at any time for which this currency can be issued, and you have assumed a variety of things, Senator Reed, for which there are no statistics and no warrant for assuming.

Senator REED. Do you think it is safe to draw a bill that is to go into effect as a permanent system in this country based upon an absolutely unknown quantity?

Mr. UNTERMYER. I do not think it is an unknown quantity.

Senator REED. You have just said that you did not know how much commercial paper there was.

Mr. UNTERMYER. What I meant to say was that I do not think it is an unknown quantity in this sense, that there is the safeguard of the regional bank and the reserve board as to the amount of paper. Therefore they have it always within their power.

Senator NELSON. But if you will allow me to interrupt, is not the ultimate question in that case what would the country absorb?

Mr. UNTERMYER. That is the point.

Senator NELSON. What would the trade and commerce and traffic of the country absorb?

Mr. UNTERMYER. That is, legitimately absorb.

Senator NELSON. It is not enough to issue a paper; there must be somebody that wants to use it.

Mr. UNTERMYER. That is what I have been trying to develop.

Senator REED. That would be true in both instances, Senator.

Mr. UNTERMYER. But one is rigid and the other is not.

Senator REED. One is rigid to this extent, that there is a point beyond which inflation can not go, and that point is fixed by the bank capital.

Mr. UNTERMYER. No; but you have a system now under which you can get currency to the full amount of the capital of a bank. That is inelastic. Now, you propose to substitute for it a system by which you can——

Senator BRISTOW. It does not substitute it at all.

Senator REED. We propose to place it in addition to the present law which permits you to have issues upon bonds.

Mr. UNTERMYER. Then, the answer to that is that instead of an inelastic system that allows 100 per cent currency issue against Government bonds, you propose to superadd 75 per cent in equally rigid security. It is not going to do very much good. It will give you more currency.

Senator REED. It is only rigid to the extent that you can not go beyond a certain point in inflation.

Mr. UNTERMYER. But the amount of bank capital is no criterion of the needs of the country. The fact that the banks have just so much capital stock at this time does not measure—in any degree on any theory—the contracting and expanding requirements of the country. The contracting and expanding requirements of the country are measured by the amount of legitimate commercial paper that is available at reasonable rates of discount; and that is the sole scientific test. If you try any other tests you have to have an unreasonable test.

Senator REED. I have heard that asserted a great many times as a fact, that the sole test of the amount of money we need in this country is to be determined by the volume of commercial paper.

Mr. UNTERMYER. Provided it is rigidly tested.

Senator REED. I have not heard anybody go beyond the assertion. I have not heard anybody demonstrate it, and I am not prepared to accept it as necessarily a verity.

Mr. UNTERMYER. But, Senator Reed, those who assert it simply point to the years of experience of other countries where it has worked and where they do not have the violent contractions and expansions in the currency market, and a famine in currency, and a glut of currency.

Senator REED. Let me see. I will take issue with you on that. I suppose you refer to England?

Mr. UNTERMYER. I refer to all the continental countries.

Senator REED. England's panics have been as frequent and as disastrous as they have been in this country, have they not?

Mr. UNTERMYER. Not currency panics.

Senator REED. Well, but panics—banks closing, bank smashes, widespread commercial paralysis.

Mr. UNTERMYER. They have had business panics that have been reflected in the banks, but they have never had, so far as my recollection goes, any instance of them in times of prosperity and normal business conditions. You have not had currency panics when people could not get money against credits, so far as I know.

Senator REED. They never actually did close their banks, I believe, in Great Britain as we did in this country just once in our history, but they have had a panic or crash that has compelled the raising of discounts to very high points, have they not?

Mr. UNTERMYER. I do not remember of their being raised very high. How high do you call "very high?"

Senator REED. They have not gone high, as compared with our board of trade speculations down here in New York, but they have gone up to practically prohibitive points, until gold flowed in from other countries.

Mr. UNTERMYER. What do you call prohibitive points? They do not frequently need to go to 5 per cent to attract gold.

Senator REED. But they have gone to 10 per cent.

Mr. UNTERMYER. I did not know that.

Senator REED. I have been so informed. I am not an expert on European banking.

Mr. UNTERMYER. I do not know that I have ever seen the statistics as to that.

Senator REED. The prime difference between you and me seems to be this, that you insist on a flexible currency—and I agree with you there. I insist that there shall be some absolute limit placed upon the amount of inflation, and I say that, as bank stock is practically stable, that we would furnish some limit, whereas you say that that is inflexible because there is an absolute limit; and you prefer commercial paper, stating that commercial paper measures the business activity of the country. I do not think it does.

Mr. UNTERMYER. No.

Senator REED. I do not think that it measures the activity of the business of the country any more than the building of houses and the putting up of factories and the construction of railroads measures the business acativity of a country; and I do not think that this bill ought to be drawn for the banks alone or for the commercial population alone, but it ought to be drawn with reference to the entire business of the country and every man, woman, and child in it.

Mr. UNTERMYER. I think we would all agree as to that, and I believe everybody who has participated in the discussion of this bill agrees that it should be drawn for everybody in the country—for the general prosperity. So far as concerns inflation, I do not think that you have here a system proposed that leads to inflation. I recognize a great distinction between legitimate expansion and inflation. I think inflation ought to be defined as illegitimate expansion.

Senator SHAFROTH. Do you not think we had better give Mr. Untermyer an opportunity to make his statement and then inquire as to any improvements which he may wish to suggest?

Senator REED. I am through.

Senator NELSON. I would like to ask two or three questions, and they will be very short.

The system to be inaugurated by this bill is really a system of asset currency, as we understand the term, accompanied with a gold reserve of 33 per cent?

Mr. UNTERMYER. That is a very accurate description of the case.

Senator NELSON. Why can we not build upon the present system of national banks that we have, allowing them to substitute in place of a bond-secured currency an asset currency based upon their commercial resources, with a 33 per cent gold reserve? In other words, why could we not apply the same principle of asset currency and 33 per cent gold reserve to the individual national banks, and so operate and build on the system that we have?

Mr. UNTERMYER. That, it seems to me, is what we are doing, except that we are interpolating between the banks and the Government these regional reserve banks, which are a strong element of added security and added supervision and management, which is necessary with an unlimited asset currency.

Senator NELSON. You have the reputation of being a good lawyer, and you know how the common law grew up. Could we not apply the principles of the common law here to our present national-bank system, and build upon that, giving the banks the privilege of substituting currency upon their assets instead of upon bond-secured currency, and requiring them to put a gold reserve of 33 or 40 per cent behind it? Why would not that be as safe a currency as this currency?

Mr. UNTERMYER. Senator Nelson, I take it from my reading of the bill that that is precisely what we are doing under the bill, except that we are adding two elements of further security by interpolating the regional bank between the member bank and the Government, and are providing for a mobilization of our reserves, which would not be otherwise possible. We are also taking these reserves out of Wall Street, where they have been used in speculation.

Senator NELSON. But you rob the individual banks of a part of their capital to get this intermediate institution.

Mr. UNTERMYER. I do not agree to that. On the contrary, I think that instead of robbing the individual banks, as I explained yesterday, we are benefiting the individual banks, because for the 10 per cent capital they have to put up they are almost guaranteed 5 per cent return, in addition to which they get back the subscribed capital in the form of rediscount. They are not losing the use of that at all. Presumably each bank is getting its pro rata and equitable use of that fund. No part of that capital has got to be set aside for a gold reserve. That capital is loanable, as I understand it.

Senator NELSON. Where do they get their gold reserve? Where would the reserve banks get their gold reserves; from what source?

Mr. UNTERMYER. As I understand it, their gold reserve that they are required to put aside is against their demand liability.

Senator NELSON. You do not answer my question. From what source are they to get 33 per cent gold reserve?

Mr. UNTERMYER. There is no doubt that they will get their gold reserve by using their capital stock and some other——

Senator NELSON. Have they not got to take their capital stock to get that gold with?

Mr. UNTERMYER. When they take their capital stock to get their gold with, then they replace their money they have thus taken out of their deposits, because when they have once gotten the gold reserve put aside, they do not need it to put aside again.

Senator NELSON. But their deposits are not their money?

Mr. UNTERMYER. No; but they have to put half their gold reserve against these deposits. There is no gold reserve required against their capital stock.

Senator NELSON. No; it is against the currency.

Mr. UNTERMYER. Only against the currency. What I mean is that they must put aside the gold reserve against the money they borrowed from the reserve bank. If the reserve bank has $100,000 of capital or $10,000,000 of capital, until it borrows currency, it need not put aside a gold reserve, and then only against the currency issued to it.

Senator NELSON. We will take the case of 100 millions of commercial paper as put up to a regional bank, and they issue 100 millions of these reserve notes, these Treasury notes upon that, and the bank is required to keep 33 per cent of gold reserve. From what source does it get it? It can not get it from those notes that are put up as security. From what source will it get its 33 per cent gold reserve?

Mr. UNTERMYER. From the deposits, the proceeds of the reserves that are put up.

Senator NELSON. From the commercial paper?

Mr. UNTERMYER. Yes.

Senator NELSON. The commercial paper will yield the gold? That is your theory?

Mr. UNTERMYER. Yes; that and the capital.

Senator NELSON. And the 5 per cent——

Mr. UNTERMYER. No, no; the 10 per cent. They have to utilize all their reserves.

Senator BRISTOW. How does the bank get its capital back?

Mr. UNTERMYER. Suppose they have $10,000,000 of capital and $100,000.000 of deposits. They lend a part of it. In other words, the banks come to them with $100,000,000 of paper and ask them for currency. They have $210,000,000 of assets, have they not?

Senator BRISTOW. Yes.

Mr. UNTERMYER. And against that 210 millions of assets they issue 100 millions of currency, against which they have to put aside 33 millions of gold. That 33 millions they get out of their entire assets.

Senator BRISTOW. That came from what?

Mr. UNTERMYER. From resources, taken all together.

Senator BRISTOW. That must come from their deposits and their capital, must it not?

Mr. UNTERMYER. And the notes.

Senator BRISTOW. But the bank gets the notes.

Mr. UNTERMYER. I mean the securities put up.

Senator BRISTOW. The Government does not let them take securities and purchase gold with them, does it?

Mr. UNTERMYER. No; the Government holds these securities, but it takes a part of these deposits it has on hand and part of the proceeds from its stock and buys gold.

Senator BRISTOW. It takes part of the 100 millions of deposits?

Mr. UNTERMYER. Yes, sir. There is no reason why the capital which these banks put up, the member banks, at 10 per cent, could not be loaned back.

Senator BRISTOW. How can it be loaned back when it is all hypothecated with the Government?

Mr. UNTERMYER. The capital is not hypothecated with the Government.

Senator BRISTOW. But the capital has been secured when it is put up by the Government.

Mr. UNTERMYER. The deposits may be used.

Senator BRISTOW. The deposits came from the banks?

Mr. UNTERMYER. Yes.

Senator BRISTOW. So you are taking from the country banks their resources and a part of the resources you can not loan back?

Mr. UNTERMYER. I do not agree. I think a part of these resources you can loan back.

Senator BRISTOW. A part, but not all.

Mr. UNTERMYER. Suppose a bank puts up $10,000 to acquire stock. It could get $6,600 back by way of loan, according to your theory, could it not?

Senator BRISTOW. Yes.

Mr. UNTERMYER. But, according to my theory——

Senator BRISTOW. They could borrow it back?

Mr. UNTERMYER. Yes; it can borrow it all back; and, according to my theory, it can borrow it all back because the regional bank can get its reserves out of its deposits and need not get it out of its capital.

Senator BRISTOW. But its deposits are the deposits of the banks. They have been taken out of their own community and sent down to the regional banks.

Mr. UNTERMYER. But the country bank now sends its deposits away and gets none of them back. They are used in the city. Under this plan they get two-thirds of them back—they can borrow two-thirds back.

Senator BRISTOW. The country bank sends that part of its deposits to the city which it needs in the transaction of its business, and the banks in the cities——

Mr. UNTERMYER. I beg your pardon; it does not send what it needs in the transaction of its business. It sends what the law requires it to send.

Senator NELSON. Banks keep accounts all over for exchange business.

Mr. UNTERMYER. Of course they do; but that must be over and above their required reserve, because their balance must be equal to the lawful reserve.

Senator BRISTOW. Bankers have testified here that the lawful reserve was not more than was needed. Many of the banks got as much as was needed in the transaction of their business.

Mr. UNTERMYER. I do not know what other people have testified to, but it does not seem reasonable.

Senator BRISTOW. That is what Mr. Frame, who was from Waukesha, Wis., stated the other day.

Mr. UNTERMYER. They have to have accounts over and above their required reserve to do their exchange business. Under this bill they will have to have accounts in the cities, anyway, but they will be accounts over and above the reserve. I am not talking about the moneys that are needed in the cities for exchange purposes. I am talking about the amount that the law requires them to have for reserve purposes that they do not get back now.

Senator NELSON. Here is the question: This reserve money that is to be put in the reserve banks, this 5 per cent, we will call it—is that to be treated in the reserve banks as reserves are now treated in the national banks? That is, must they be kept there perpetually as an unavailable fund?

Mr. UNTERMYER. I think the bill defines that.

Senator NELSON. What is your understanding? Is that to be a reserve in the reserve banks in the sense that a reserve in a national bank is a reserve now?

Mr. UNTERMYER. Is not that against gold? That is, the 5 per cent deposit against their currency issue. Is that what you refer to?

Senator NELSON. No; I mean the reserve requirements. At present a country bank is required to keep 15 per cent reserves. Nine per cent it can have in central reserve or reserve cities; 6 per cent in its vaults. Banks in reserve cities are required to keep 25 per cent; half they must keep in their own vaults. Under this system, when it has finally culminated, after the end of 36 months, the country banks are required to keep, I believe, 12 per cent—5 per cent in their own vaults and the balance in the reserve bank.

Mr. UNTERMYER. No; 5 per cent in the reserve bank.

Senator NELSON. The question is not whether it is 5 or 12 or 6. It does not make any difference. Is that 5 per cent of the reserve banks to be there somewhat as a fund, as it is now, an unavailable fund, for any purpose?

Mr. UNTERMYER. No; on the contrary, it is available in the hands of the regional banks as a basis on which to loan money; that is, two-thirds of it.

Senator NELSON. Can they pay that money out? Must they keep it constantly in their vaults?

Mr. UNTERMYER. No; on the contrary, that is one of the virtues of this bill, that instead of that money being unavailable it is available except as to the gold reserves that must be kept against it.

Senator NELSON. They are not required to keep any other reserve than a gold reserve?

Mr. UNTERMYER. None other. The rest of their assets can all be in the form of member banks' notes, and that is one of the great advantages to the country banks, that whereas at present their reserves of 9 per cent in the city are unavailable to them, under this bill that reserve is reduced to 5 per cent, and two-thirds of that is available to them.

Senator BRISTOW. I received a letter this morning from one of the leading State bankers in our State, and he gave it to me as his judgment that none of the State bankers of Kansas would come into this; that they could not afford to; and he also said that a majority of them could not go in under the law because their capital is not sufficient.

Mr. UNTERMYER. You refer to $25,000 limitation?

Senator BRISTOW. Yes. He thinks that a great many national banks will take out charters under the State law, because it would be more advantageous to them in doing their banking business than under this Federal statute.

Mr. UNTERMYER. I think it will be, as the law now stands, and I have suggested that it be amended in that respect. As the bill now reads, as I suggested yesterday, a State bank may become a part of the regional reserve bank by subjecting itself to an examination and by having the necessary reserves, complying with the conditions of this bill, and it may do a very much wider variety of business and have a broader charter than a national bank; and this bill, to my mind, leaves no inducement open to a national bank to remain a national bank if it can exchange its national charter for a State charter and get wider charter powers than they have now.

Senator NELSON. They can all do that, except in the matter of issuing currency.

Mr. UNTERMYER. No; but the currency can be issued to a State bank under this bill. That is the difficulty which I would like to develop; that is one of the things I wanted to say. My suggestion has been that any bank that wanted to enter this system, any State bank, should exercise only the powers that are possessed by and allowed to a national bank. If you do not do it as you have now withdrawn bank notes from circulation privilege and as soon as you have now withdrawn the privilege of being a depositary for Government funds, I do not see that you have left the national banks any advantages that would not be possessed by a member State bank whilst the member State bank has powers and can do classes of business that the national bank can not. Therefore, it seems to me you must choose now between one of two alternatives. You must either have a system of currency available to all State institutions and in that way have them all together out of the national system, or you have to make the State institutions conform in their charter powers to the powers possessed by a national bank; and for that purpose you ought, it seems to me, to enlarge somewhat the powers of a national bank. As between the two systems of a State bank or the system of State banks only, under this bill, with limited regulations by the Federal authorities, and the system of national banks and State banks on a par, you ought to choose the latter. If you limit the powers of a State bank to those possessed by a national bank, and enlarge the powers of a national bank, you put the two classes of banks on a par so far as concerns their membership in the association. It has been said that the State banks would not come in. I do not believe it is possible for the State banks or any other banks to stay out of this system.

The advantages of the system are so manifest and so numerous that they could not stand the competition; besides which the stability of a bank in this system, its ability to get money in times of emergency, to utilize its reserves, and in that way to use its deposits over and over again, is so manifestly superior to anything that the bank outside of the system would have that it would only be a little while before the State banks would be bound to come in. But you can not leave it in its present condition. There would be no incentive to a national bank to stay in the system, and every incentive to convert it into a State bank, because it would get all the benefits of membership in the system and none of the restrictions in respect to its charter powers or methods of doing business.

Senator O'Gorman. What would be the objection to enlarging the functions of a national bank to the extent now possessed by the State banks generally?

Mr. Untermyer. I am very much in favor of enlarging those powers, except in certain directions. For instance, in some of the States the trust companies and the banks are allowed to deal in stocks—to buy and sell stocks—and it is an unsafe thing. They ought not to be permitted to do it, and no State bank should be permitted to be a member in this system and get the benefits of currency and the protection of this system unless its charter powers are limited in that way. It would not be necessary, as was suggested yesterday, to alter its charter, but only to provide that no State bank should exercise powers not possessed by national banks and then enlarge the powers of national banks.

Senator Pomerene. In what particulars?

Mr. Untermyer. I would allow the national bank to be a trustee of a deed of trust or mortgage. I should allow it to be an executor. I think those are the principal particulars in which I would enlarge the powers; I would probably allow it definitely to have a certain proportion of its capital in bonds of a certain character. Some of them buy bonds now, but I do not think they have the power to do it. At one time they bought and sold and dealt in stocks until they were stopped by the comptroller. He has not yet stopped them from investing in bonds, but he should have done so long ago. In the larger cities they are promoters, underwriters, syndicate managers, and act as issuing houses and bond sellers on a large scale. It is all wrong.

Senator NELSON. Evidently you are not familiar with banking in the rural communities in the West. The great thing in favor of the State banks is that they can loan on approved bonds, on real estate security; that above everything else. They do not care about loaning on bonds such as you spoke of.

Mr. UNTERMYER. I did not mean loaning on them, but owning them as permanent investments. There is no reason why they should not lend on bonds or stocks.

Senator NELSON. They do not care about owning the bonds, because they can do very much better on real estate loans, first-class farm mortgages. That is the great consideration for State banks out there; and you can not get one of them to go into this system if you deprive them of that privilege.

Mr. UNTERMYER. That ought not to be an insuperable objection, although a farm mortgage is not a very liquid security. It seems to me something can be done in that direction, although I had understood that we were going to have a system of farm credits, agricultural credits similar to the continental systems.

Senator NELSON. That would be an agricultural bank. That is another scheme.

Senator O'GORMAN. You think the power possessed by State banks to buy and sell stock is an unwise power. Has it proved to be unwise in the experience of State banks?

Mr. UNTERMYER. I think it has proved to be unwise in this sense, that in the great cities, some of them, they have become pretty active speculators in the market.

Senator O'GORMAN. State banks?

Mr. UNTERMYER. State institutions; I would not like to say State banks. I would not care to be any more specific.

Senator NELSON. Senator O'Gorman, can the State banks in your State loan on farm mortgages?

Senator O'GORMAN. Savings banks can loan on mortgages.

Senator NELSON. But not the other State banks?

Senator O'GORMAN. No.

Senator SHAFROTH. Have you examined the bill which I introduced with relation to taking in what national bank currency is now outstanding?

Mr. UNTERMYER. I have, and I know the bill, and there is a like bill by Senator Owen. I have that here, and in its main features it is a very wise bill. It seems to me we ought to have something of the kind. As I understand the bill, it proposes to deal with two subjects: First, the gold that is now on storage with the Treasury against the gold certificates for which the Government acts simply as a warehouseman for the moment, and which amounts to in the neighborhood of $1,100,000,000; secondly, it proposes to deal with the retirement of the bank-note currency, which amounts now to $746,000,000.

Senator SHAFROTH. And also for the retirement of greenbacks.

Mr. UNTERMYER. And putting that fund of 150 millions into the general fund.

Senator SHAFROTH. And providing for a 50 per cent gold reserve to maintain that currency.

Senator NELSON. It provides for the issue of a new Government paper currency.

Mr. UNTERMYER. Yes, sir. It seems to me that there is no more convenient or available way in which we can get gold than by canceling these gold certificates as they come in from customs and in other ways into the Treasury and issuing for them a Treasury note with a 50 per cent gold reserve back of them. If you get in all of the gold certificates under that plan you will have $500,000,000 of free gold, and unless you utilize it for the bank note currency—as I understand you propose to sell those bonds—do you not?

Senator SHAFROTH. No; the theory is to take them all and use this gold for all of them.

Senator NELSON. Take up the national bank notes and issue this new national currency?

Senator SHAFROTH. Based on the 50 per cent gold reserve.

Mr. UNTERMYER. The plan that has been a good deal discussed of late, and I think it is a very wise one, would release a great deal of gold. My suggestion would be that instead of utilizing the surplus gold that would come from the redemption of the gold certificates leaving only 50 per cent against those certificates.

Senator SHAFROTH. As it is now, there is 1,100 millions of gold in the gold-certificate fund.

Mr. UNTERMYER. Yes.

Senator SHAFROTH. And there are 700 millions, say, in round numbers, of bank notes. There are 346 millions of greenbacks on which there is a reserve.

Senator NELSON. There is about 2 millions of other notes issued under the gold purchasing act.

Senator SHAFROTH. They are so insignificant that we do not care to take that into consideration.

You are for a gold reserve, then, of about 1,300 millions of dollars, and upon that the most that could be issued would be to replace the certificates, which would be 1,100 millions, to replace the greenbacks, which would be 346 millions, and to replace the 700 millions of bank notes, which, added together, would make about 2 billion, 146 million.

Mr. UNTERMYER. And 1,300 millions of gold.

Senator SHAFROTH. And 1,300 millions of gold, or about 60 per cent in gold, which would make a perfectly safe currency?

Mr. UNTERMYER. It would make an ideal currency.

Senator SHAFROTH. And would not the legal-tender quality being added to the note cause it to increase in value and give it, as a matter of fact, a tendency to keep it on a par with gold?

Mr. UNTERMYER. It ought to have and would be entitled to a legal-tender quality, and the gold reserve back of it would keep it on a par with gold always. That is a very large gold reserve.

Senator SHAFROTH. And the legal-tender quality would strengthen the currency, would it not?

Mr. UNTERMYER. Yes.

Senator SHAFROTH. And would have a tendency to overcome the objection which we now have to national-bank currency, because the national-bank currency is not permitted to be used as reserve?

Mr. UNTERMYER. Yes; it should be available as a reserve.

Senator SHAFROTH. It would be if it was full legal-tender money.

Senator NELSON. But, Mr. Untermyer, how could the Government put that money out into circulation except for the payment of its bills, its expenses, salaries, etc.?

Senator SHAFROTH. It could not; it would come gradually.

Senator NELSON. How would they get it through the Government? Would not the Government have to go into the banking and discount business?

Mr. UNTERMYER. As I understand this matter of gold certificates, they are being paid in every day for customs duties. When they come in, there is certainly no difficulty in issuing Treasury notes in their place.

Senator NELSON. What good would it do to issue the Treasury notes and to keep them in the archives of the Government? It would have to pay out those Treasury notes to somebody.

Mr. UNTERMYER. They should be a perfectly good legal tender.

Senator SHAFROTH. They would take the place of the gold certificates that come in.

Senator NELSON. That come in here, and they issue paper money for it. Who takes that out?

Mr. UNTERMYER. Who takes out the gold certificates as they come in now?

Senator NELSON. They take out the gold certificates, but that is measured by the present volume of the currency. It has nothing to do with the business of the country.

Mr. UNTERMYER. You would pay them out in the ordinary course of disbursement. You would deposit those Treasury notes in your bank accounts instead of your present gold certificates and check against them. This is a perfectly simple process.

Senator NELSON. It would make a better system, then, than this regional reserve system?

Mr. UNTERMYER. No; I think it would be supplementary to the regional reserve system. This does not create any additional currency; this only substitutes one kind for another.

Senator NELSON. It obviates the danger Senator Reed was fearing.

Mr. UNTERMYER. This would perfect that system.

Senator SHAFROTH. You say the gold certificates would still be in existence if anybody wanted them? And it does not force the national banks to surrender their currency unless they find that it is to their advantage to do it, and the advantage which they have by reason of cashing it would be to cash their 2 per cent bonds at par, which they now fear might go to a discount. It seems to me, when it is voluntary on their part, it would be a gradual substitution.

Senator NELSON. Why would it not be an immediate substitution for the regional reserve bank?

Mr. UNTERMYER. It does not create an elastic currency.

Senator NELSON. That is what I was trying to get at and you seemed to evade it. I said how was the Government to pay out this money?

Mr. UNTERMYER. It pays it out in its general disbursements; that is all. It does not give us any more currency.

Senator SHAFROTH. No; it does not inflate the currency a particle.

Senator HITCHCOCK. We will take a recess until 2.30 o'clock. Mr. Untermyer, as you must leave, we would like to know if you can come back on Monday?

Mr. UNTERMYER. Yes; I can return on Monday.

Senator HITHCOCK. Would 11 o'clock on Monday be satisfactory to you?

Mr. UNTERMYER. Yes, sir.

(Whereupon, at 1 o'clock p. m., the committee took a recess until 2.30 o'clock p. m.)

AFTER RECESS.

Senator HITCHCOCK. Mr. Wells, will you please state your name for the record, and your business and your place of residence?

Mr. WELLS. My name, Edward B. Wells, of Minneapolis. I am in the milling business, the elevator business, and connected with an investment securities business.

Senator HITCHCOCK. Have you a statement that you would like to make to to the committee, and is it in such form that you would like to read it?

Mr. WELLS. Yes; without objection, I should like to do that.

Senator HITCHCOCK. Well, you may proceed.

STATEMENT OF EDWARD B. WELLS, OF MINNEAPOLIS, MINN.

Mr. WELLS. This delegation, gentlemen, is here representing officially the Minneapolis Civic and Commerce Association, comprising a membership of something like 2,000 business men of Minneapolis. As you will readily perceive, it embraces all classes of business men; large and small, in every branch of our industries.

Also, the Minneapolis Chamber of Commerce, with a membership of 550, devoted chiefly to the grain and allied industries, milling, etc.; and also the Duluth Commercial Club, with a membership of 1,000, also representing the business interests of that city.

The principal lines of business in the Northwest are represented through these organizations. Would you care to have here the names of the gentlemen composing the delegation and their occupation for your record, Mr. Chairman?

Senator HITCHCOCK. I think each one of those gentlemen may state it as he comes before the committee.

Mr. WELLS. Well, as individuals, I may say——

Senator HITCHCOCK (interposing). If you prefer, however, you may file that with the stenographer.

Mr. WELLS. I can do so, if you wish.

(The list referred to is as follows:)

Delegation representing the Minneapolis Civic and Commerce Association, Minneapolis Chamber of Commerce, Duluth Commercial Club, and principal lines of commercial business in the Northwest.

Edward P. Wells, president Russell-Miller Milling Co., Minneapolis; president Electric Steel Elevator Co., Minneapolis; president Wells & Dickey Co. (investment securities).

Charles M. Harrington, elevator operator and grain merchant, Minneapolis.
F. E. Kenaston, manufacturer of thrashing machinery, farm tractors, and other agricultural machinery, and country banker, Minneapolis.
A. H. Comstock, wholesale hardware (Marshall-Wells Hardware Co.), Duluth.
Hovey C. Clark, lumber manufacturer, Minneapolis.
Fendall G. Winston, wholesale grocer (Winston, Harper, Fisher Co.), contracting and engineering (Winston Bros. Co.; Winston & Deere), and banking, Minneapolis.

As individuals we represent milling, grain trade, lumber manufacturing and jobbing.

We assume no knowledge of the science of banking. We represent a much larger and more important class—the borrowers.

We are come not to instruct your committee nor to support the contentions of the bankers.

It has been claimed that the effect of the bill under consideration will be to restrict the credits of the country. If this is true we should be unfaithful to the business interests of the great and growing Northwest if we do not enter our protest. If the claim is not justified we should be unfair to the framers of the bill if we do not frankly report our conclusions to those who sent us.

The business interests of the Northwest include the small country banker, the merchant, the farmers. For 20 years of my business career I was myself a small country banker, the very small country miller, and as well the farmer. My associates were these men. My best friends were and are to-day found there. But if anything takes place that prejudices the credit and embarrasses the business of the banks, the manufacturers, and the merchants of our northwestern cities it is at once reflected in the diminished prosperity of the country banker, merchant, and farmer. One quite naturally finds his first illustrations in his own business experience. My own company is engaged in the manufacture of flour. We operate 11 mills, and 10 of them scattered through the wheatfields of North Dakota and Montana. We also have elevators at some 80 or 90 other points in these States, primarily to purchase wheat for our mills. Because we want the first choice of the wheat of these States for our own use we can afford to pay, and do pay to the farmer, from 2 to 3 cents per bushel more than the elevators can afford to pay and assume the risk of shrinkage, dockage, short weight, and market conditions in shipping. During the year ending August 31, 1913, our mills and country elevators purchased over 20,000,000 bushels of wheat, on which it is safe to say that we paid an average of more than 2 cents a bushel above current market rates, or to the farmers of those States, dealing with us alone, $400,000. To enable us to purchase this wheat at the time when the farmers wanted to sell necessitated with us that we borrow between $2,000,000 and $3,000,000. If for any reason it had been impossible for us to do this the wheat would have been sold in the open market at current market prices. A similar restriction of credit experienced by the thousands of line elevators and by the independent and farmers' elevators in the Northwestern States would unquestionably have resulted in still lower current market prices and an an additional loss of many hundreds of thousands of dollars to the farmers of those States, with a corresponding shrinkage in their purchasing power, which would have been felt not only by them but by the laborers, the small tradesmen, and the country bankers.

The similar effects that would have been felt I shall leave to my associates in this delegation to tell you of, as it may affect the interests that they more directly represent. If convinced, as I shall be glad to be convinced, that I am mistaken in anticipating restricted credit as a result of this measure, I can offer no criticism of this feature of the proposed legislation. Perhaps as a business man I may be pardoned for saying that I should look with disfavor on a proposition coming from any source to take from me any part of my invested capital to be put into an enterprise in the management of which I was to be permitted no voice and which might under some conditions become the football and plaything of politicians without experience in the business.

I would like to call attention to another provision of this bill, with the purpose of which I am in hearty sympathy, to wit, the prohibition of the use of paper as a basis for credit to be employed for carrying or trading in stocks, bonds, or other investment securities. I am connected with a concern whose business is that of purchasing, carrying, and trading in high-class municipal and corporation bonds and farm mortgages—never in a speculative way, never upon margins, and yet of necessity to meet the requirements of its customers, carrying hundreds of thousands of dollars' worth of strictly nonspeculative, sound investment securities, and often requiring large bank accommodations to enable us to carry the securities. Our concern represents hundreds of other and like concerns engaged in similar business. Is there not some way by which such legitimate undertakings may be recognized without letting in the promotion schemes, the stock jobbing, and the other forms of speculation against which this bill evidently attempts to provide?

There are one or two other points in the bill, and one in particular that I want to speak of very briefly, and that is the feature of the bill that provides for an advisory board and withholds compensation from it. It seems to me that that provision, if made effective, would practically prevent the participation in any degree whatever of that advisory board in the councils of the Federal reserve board. I believe that the business men generally of the country would heartily approve of a provision that should make—at least some part of, or give to some part of that advisory board, its chairman, or its executive committee—compensation upon the same scale as given to the members of the Federal reserve board, and with the condition that that man, or those men, should reside in the city of Washington, should be permitted to sit with the Federal reserve board, and give to it the benefit of their practical knowledge of the subject that may be by them under consideration at all times.

I presume that you have been flooded here with letters from country bankers. I have one, out of a good many that I have received, that is very temperate in tone and so well expressed that I may perhaps be permitted to read it. It is from the James River National Bank, of Jamestown, N. Dak., in response to a simple question from me:

How do you feel with regard to this new currency bill and how will it affect you?

In reply I have only three or fours days ago received this letter, which I will read to you. [Reads:]

THE JAMES RIVER NATIONAL BANK,
Jamestown, N. Dak., September 16, 1913.

Hon. E. P. WELLS, *Minneapolis, Minn.*

DEAR SIR: Replying to your letter with regard to the currency legislation now before Congress known as the Glass bill, I wish to say that we do not regard this bill favorably in its present form. The country banker does not look at all favorably upon the provision in this bill requiring him to furnish capital for the Federal reserve banks, in the management of which the bankers have no voice. Loss of interest on reserves deposited with the Federal reserve banks, loss of exchange, and only a possible 5 per cent return on the capital invested are, to say the least, not attractive.

It certainly seems to us that the banker who is required to furnish the capital and most of the business of these Federal reserve banks should at least be represented in managing them, and we do not look with favor upon the prospect of political management of the banking affairs of this country.

An opportunity to exchange a part of their best paper for cash in time of need is most earnestly desired by the small banks and is, in my opinion, by far the most important matter dealt with by the proposed legislation. We doubt whether the country bank in the Northwest will be able to avail itself of this privilege should this bill become a law in its present form, as the paper ordinarily carried by such a bank does not meet the requirements made. If this rediscount privilege is extended to the small banks and made immediately available in time of need, without delay by reason of cumbersome methods or otherwise, I am sure it would prove a privilege of inestimable value to all banks.

We are glad that some action is being taken by Congress and have no doubt that should the present bill be passed it will be amended later to suit the needs of the country at large, should it not prove entirely satisfactory.

Yours, very truly,

H. T. GRAVES, *President.*

Senator HITCHCOCK. Senator Nelson, have you any questions to ask Mr. Wells?

Senator NELSON. No.

Senator HITCHCOCK. Senator McLean, have you any?

Senator McLEAN. No.

Senator HITCHCOCK. Senator Bristow?

Senator BRISTOW. You speak as a business man, and you are under the impression that it will cause a contraction of credit. What makes you think it will cause a contraction of credit, Mr. Wells?

Mr. WELLS. I should be glad to answer that question personally, Senator Bristow, but it is a branch of the subject that has been assigned to one of my colleagues on this delegation.

Senator NELSON. I want to say to the Senators that there is a delegation here, and they have different subjects apportioned to each of them, and perhaps it would be well to let this go until the gentleman who is to speak on this subject takes that up.

Senator BRISTOW. Of course I do not want to interfere with their plans, but it is a good deal more satisfactory to me to have the opinions of all of them on what appears to be important, because then you get the judgment of six men independent of any conferences which they have had, and I think we would get in that way a better reflex of opinion. That is all.

Senator POMERENE. That is right.

Mr. WELLS. I have not the slightest objection. But I do not want to appear to deprive my friends here of the privilege of presenting their subject. We are in perfect harmony on all of these points. We have reviewed them and assigned them to different members of the delegation. The withdrawal of the capital in this manner, primarily, of course, represents the first shrinkage in the loanable funds.

Senator Bristow. That is, you refer to the contribution of the country bank——

Mr. Wells (interposing). To the central reserve banks.

Senator Bristow. And deposits?

Mr. Wells. The shifting of the reserves from the points at which banks are now getting interest to reserve banks that will pay no interest represents, of course, a great shrinkage. The proposed withdrawal of a vast sum of money that is now in the savings banks departments of our national banks—segregating that and making that usable for an entirely distinct line of investment—takes it out of business channels. Those, I take it, are the three chief channels through which the loanable fund will have disappeared.

Senator Bristow. Now, it has been argued here that, while the country banks contribute their capital stock and of their deposits, it is sent out of the community to a distant city, that they are compensated by being able to borrow back a large amount of it; and that, while apparently it reduces the capital in the national banks individually, it does not. That is the position assumed by Mr. Untermyer here this morning.

Mr. Wells. Well, of course, the country banker, I think, universally claims that the privilege of rediscounting is not in practice available to him. The country banker is not possessed of paper that falls within the restrictions of this bill.

Senator Bristow. Yes.

Mr. Wells. I have a little knowledge of country banking, and I have, of course, conferred with a good many friends who are country bankers. And the country bankers' paper is seasonable paper. It would be utter folly to take from the ordinary farmer, or the merchant who is dependent upon the farmer in the country, a piece of paper maturing at any other time than in the fall of the year. So that, while I was actively in that business, I know it was our custom, with such paper as we could not collect in the months of October, November, and December, to renew it, not until next spring or next summer, but until a year from that time. That, I think, will be found to be the chief asset in most of the country banks in the Northwest. It would be paper maturing——

Senator Nelson (interposing). In six months or a year?

Mr. Wells. It would be maturing in the fall. Of course, very little paper is given by the farmers in the spring. They make their annual clearances and settlement when they have harvested and marketed their crops. They pay their debts as far as their crops will permit, and what they can not pay they renew until next fall, because the lender knows that it would be useless to take paper with an earlier maturity.

Senator Bristow. Yes.

Mr. Wells. Well, so that, to be perfectly frank with you, the country bankers depend for their business upon the farmers, directly or indirectly. Now, farmers are improving in their circumstances, so that it is not as general as it was at one time; but they once marketed all of their crops in the fall within a period of 30 days. So that those conditions are changed to that extent now. But it will be a slow process to change them entirely; and until that is done, a larger part of the country banks' assets will be found in the paper which matures in the fall, and which, if not paid, is extended until the following fall.

Senator HITCHCOCK. Senator Bristow, have you finished your questions?

Senator BRISTOW. Not quite. Then, from your experience as a business man and banker, you are under the impression that the paper that is provided here in the bill as security for rediscounts is paper held by the banks in the large cities more than by the banks in the country?

Mr. WELLS. Yes, sir. And even there I think it would be difficult to find the necessary basis for the credit required, except as paper might be worked off that had already run part of the period. I know that we borrow $1,000,000 every year, and yet I presume that 90 per cent of the paper—I do not know that I am quite correct, but 75 to 90 per cent of our paper—is six months' paper. That would only be available under the bill by catching it in the interval somewhere.

Senator BRISTOW. Yes. You say you borrow millions of dollars every year?

Mr. WELLS. Yes, sir.

Senator BRISTOW. And of the millions that you borrow, not to exceed 25 per cent and possibly not to exceed 10 per cent of it, would be available for use under the provisions of this bill?

Mr. WELLS. Except as I have intimated, that the banks having held that paper until it has come down to the period within which its maturity would carry it.

Senator BRISTOW. Yes.

Mr. WELLS. And make it eligible.

Senator BRISTOW. Yes.

Mr. WELLS. Except as to that, it is true.

Senator BRISTOW. Yes. Well, did you understand from the bill that provision is made for the retirement of the national-bank notes, and the only currency that is to be substituted for it is this currency based on 90-day paper?

Mr. WELLS. No; I can not say that.

Senator BRISTOW. But that is the provision in the bill. I think it is correct that the bill makes no provision for any substitute for the national-bank notes when they are retired, except this currency based upon the——

Mr. WELLS (interposing). Yes; I have understood that.

Senator BRISTOW. Yes. It is claimed by some that that would result in a great contraction of the currency and by others that it offers an unlimited possibility for inflation. What is your view as to that?

Mr. WELLS. The inflation would come through an excess of the use of the rediscount privilege, would it not?

Senator BRISTOW. Yes.

Mr. WELLS. That is the only way you would get the expansion. Now, that, of course, is a question that I am not qualified to answer. I am not a banker. My banker friends all assure me, of course most earnestly, that they would hesitate to rediscount—to become themselves responsible for large sums of money, merely for the privilege of turning around and loaning to their customers. It is contrary to what has been heretofore considered good banking practice. It is possible that you gentlemen, through the medium of this bill, may so change that as to make it so attractive that bankers will fall over each other in order to come in and apply for their rediscounts. But I know it will be contrary to the prejudice of this whole country. There is hardly a business man who analyzes a bank's statement up to the present day who is not prejudiced against a bank in which he finds a showing of a rediscount.

Senator BRISTOW. Do you think, then, that it would be a rather novel and unusual proposition to have the entire currency of the country practically based upon rediscounts?

Mr. WELLS. I certainly do.

Senator BRISTOW. That is all.

Senator HITCHCOCK. Senator Weeks, have you any questions?

Senator WEEKS. Mr. Wells, you read a letter from a Jamestown banker?

Mr. WELLS. Yes, sir.

Senator WEEKS. Do you think that is typical of the opinion of country bankers in the locality which is tributary to Minneapolis?

Mr. WELLS. Why, I have perhaps either talked with or heard 100 or 150 country bankers within the last three months discussing this bill, and I do not remember to have ever heard an expression favorable to the provisions of the bill.

Senator WEEKS. The statement has been made that one reason for such a condition that exists is that bankers in reserve and central reserve cities were using their influence to urge the country bankers to oppose the bill. Do you think there is anything in that?

Mr. WELLS. Well, I do not believe they go so far as to use their influence to urge the country banker. I believe, quite frankly, that the bankers in our cities—the larger cities—more or less do influence the attitude of the country bankers. We can hardly doubt that. I think a great many country bankers either have not felt competent or have not been willing to go into an exhaustive study of this bill and to apply its provisions to their individual cases and determine for themselves what the effects would be. But they see two or three things that stand out conspicuously. The requirement that they shall contribute to a bank a part of their capital—to a bank over which neither they nor others like them have any sort of control, and in which they exercise no sort of influence. That is rather a natural sentiment. I think I would apply it to my own business, and that anybody else would.

Senator WEEKS. It is the same kind of influence which exists at all times in banking, that the country banker depends on his reserve agent for information about the quality of paper and other matters relating to the banking business, is it not?

Mr. WELLS. There is no doubt of that.

Senator WEEKS. And, naturally, he would be influenced by the opinion of the man on whom he depended in other matters.

Mr. WELLS. I have not a doubt about that.

Senator WEEKS. When I returned to my office after this morning's hearing, I found a letter from a New York business man who had recently been traveling through the West, and he said he found an impression among business men quite generally that conditions were such that it was necessary to pass the pending bill, or a bill like it, and do it at once, in order to prevent some great catastrophe. Do you know whether any such condition as that exists?

Mr. WELLS. I do not think there is any such condition as that at all. I do not think the business interests would be prejudiced if no bill were passed at this session of Congress.

Senator WEEKS. You do not know of anything in the business conditions to-day which presents an emergency which did not exist six months ago or a year ago, do you?

Mr. WELLS. No. I think the conditions to-day generally—the outlook—is better than it was as distinguished from any fictitious condition that may result from uncertainties, just like this with regard to the complete upheaval in our banking system.

Senator WEEKS. Do you not think that my correspondent was deceived in his impression which he gained?

Mr. WELLS. That would be my impression.

Senator WEEKS. And that the business men of your section would look with approval on ample time being taken to present a bill which would be as nearly right as a bill could be?

Mr. WELLS. I believe that the business interests of the whole country—not merely those of our section, but of this entire country—would prefer to take the chance of a continuance under our existing banking system temporarily, but long enough to let the business interests of the country familiarize themselves with the proposed legislation, to digest it, and express themselves upon it.

Senator POMERENE. Senator Weeks, did that last question of yours have reference to this bill or to your resolution? [Laughter.]

Senator WEEKS. To general conditions. I heard you make one suggestion in your statement, Mr. Wells, that the members of the advisory council should live in Washington?

Mr. WELLS. Some representation of that committee.

Senator WEEKS. Well, do you mean the members or the secretary?

Mr. WELLS. I said, if you will remember—I qualified it—I will say now that I do not believe that it will be necessary that the entire advisory council should be so provided for, but that some representation, a small executive committee of three, if you please, if we have as large an advisory board as is suggested in the bill, which, I believe, would be 12, as it stands now, or the chairman and the secretary. But some one representative of that advisory board, who might be in constant touch with his associates throughout the country and serve as the point of contact between that board and the Federal reserve board.

Senator WEEKS. That would mean a secretary, would it not, probably?

Mr. WELLS. Well, whatever you choose to call it. The secretary is hardly, I think, the man. That is, there would hardly likely be chosen a man of sufficient importance to fully represent the banking interests of the country.

Senator WEEKS. It struck me when you said that as being an inadvisable suggestion, because if that advisory board is going to be of any real benefit, it is going to confer that benefit from the fact that it is made up of men from all sections of the country who are in immediate touch with business conditions in the sections which they represent and who should live there and be in business there.

Mr. WELLS. I think you are perfectly correct; but I believe there should be some proper medium through which the convictions and the impressions of these men scattered throughout the country should be brought officially to this Federal reserve board, and I do not believe it should be through a secretary. I think they should select their best man as chairman of the board, if you please—or three men as an executive committee, and let them reside here. It is just as important that they should keep in touch with the work of the Federal reserve board and the process by which it reaches conclusions as that the Federal reserve board should keep in touch with the country at large.

Senator WEEKS. I presume the banks would allow themselves to be assessed to pay the expenses, would they not?

Mr. WELLS. I think they would. I would if I were a banker.

Senator O'GORMAN. Mr. Wells, you say the present discount features of the bill will confer no benefit upon the country bankers?

Mr. WELLS. I did not make that statement myself. I said that that is the claim that is made. That is the impression of the country banker—that it would not.

Senator O'GORMAN. Have you any suggestion to make as to what modifications should be made in the pending bill, so as to extend the benefits of the rediscount features to the country banker?

Mr. WELLS. It is a pretty difficult problem. I will tell you right now that I would hate to suggest that the class of paper that the country banker in the remoter districts is obliged to take should be made the basis upon which our currency is issued—the collateral behind it. And that is not in the slightest degree questioning the quality of that security, but how any individual, or any board, is going to pass upon the quality of the paper of Dick Jones, for instance, given off in Wyoming, for a small bunch of alleged sheep, I do not know. [Laughter.]

Now, you can tell about the credit of our large concerns in our leading cities; it is a simple proposition. But when you come to rake the country with a fine-tooth comb and pick up all the pieces of paper that are perfectly good in the hands of those local banks, their neighbors, and pass upon them, and make them as important in the financial structure of this country as is proposed in the bill, I would not make the suggestion.

Senator O'GORMAN. You are in business in Minnesota, are you?

Mr. WELLS. Yes, sir; and in Dakota and Montana.

Senator NELSON. He lives in Minneapolis.

Senator O'GORMAN. The business outlook in that part of the country is perfectly satisfactory?

Mr. WELLS. Yes, sir.

Senator O'GORMAN. Better than it was a year ago?

Mr. WELLS. I can not say. It has been good for some time there.

Senator O'GORMAN. And the advance in business conditions has not been arrested at all by the tariff bill? [Laughter.]

Mr. WELLS. We have not been able to discover it.

Senator O'GORMAN. That is all.

Senator NELSON. We got a bountiful crop in our country, did we not, in Minnesota?

Mr. WELLS. We got a much better crop than we anticipated.

Senator NELSON. Yes. I want to ask you one question. How do you regard farm loans, mortgage loans, on improved farms?

Mr. WELLS. I think my concern carries always in its vaults from $300,000 to $500,000 worth of them. I do not know that any other answer is needed. We have been doing that for 36 or 37 years.

Senator NELSON. Do you regard it as first-class paper?

Mr. WELLS. I regard it not as first-class banking paper, but as first-class investment paper.

Senator NELSON. Is it better than stocks and bonds?

Mr. WELLS. I do not question the value of it. I think there is no better class of security in the world than first-class farm mortgages selected by intelligent men who are familiar with the conditions in the locality in which the property is situated.

Senator O'GORMAN. Might I ask you another question? What is the average rate of interest on your farm loans?

Mr. WELLS. Our farm loans are being made in Minnesota at a net cost to the farmer of 6 per cent.

Senator O'GORMAN. And in the other States?

Mr. WELLS. In North Dakota, I should say (now, I do not have time to give my personal attention to these details), I think I am safe in saying the maximum rate for farmers in North Dakota is 7 per cent, which covers agents' commissions and all expenses. In Montana, I think perhaps you will find the rate is just a trifle higher. As you get further away from the sources of supply and the settlement of the country is more scattered, and the expenses of examinations and all that are greater, necessarily there is a slight additional cost.

Senator NELSON. I think in the southern part of the State it is 5 per cent to 5½.

Mr. WELLS. Five and a half. It is not quite as low, Senator, as the rates were two or three years ago. There has been a highering of all rates in this country in the last 20 years.

Senator WEEKS. Where do you suppose these figures in circulation, to the effect that the farmers are paying 7½ to 8 per cent, originate?

Mr. WELLS. I think the people dream that largely.

Senator O'GORMAN. They are paying extreme rates in the Southern States now.

Mr. WELLS. Yes.

Senator WEEKS. They are paying an extreme rate in the Northwestern country.

Mr. WELLS. Yes. I made a little experiment down in the Imperial Valley that comes near being as good an estimate as anything I could get. I find down there the farmers are borrowing money at 8 per cent, total cost over everything. I do not know where you can find a higher rate than that.

Senator POMERENE. Mr. Wells, have you analyzed this bill so as to place in parallel columns the advantages the banker has under the present system and the advantages he would have under this system?

Mr. WELLS. No, sir; I have not.

Senator POMERENE. Or the disadvantages under either system?

Mr. WELLS. I have not, except as to some minor features of it.

Senator POMERENE. I notice, in answer to Senator O'Gorman's question, you disclaimed stating that it was your judgment that this might be prejudicial to the country banker, and expressed that as being the opinion of some of the country bankers.

Mr. WELLS. Yes.

Senator Pomerene. What is your individual opinion on the subject?

Mr. Wells. I tried to make a parallel yesterday in a case of a single bank. I do not know whether I made it correctly. I am not a banker. I may have made mistakes, but I frankly say to you that it did not appear to be of such great disadvantage to that particular institution in its present condition as I had anticipated.

Senator Pomerene. Do you object to giving the instance you have in mind? I do not care for you to mention names or anything of that character, but give us your analysis of the proposition.

Mr. Wells. I do not know that I have it here. I think I armed myself with everything that might possibly be called for. Yes; I have it. I took the case of a banker with a capital of $100,000, deposits of $600,000. Under the present law a reserve of 15 per cent—$90,000—with 6 per cent in the vaults and 9 per cent in the reserve banks is required. That is $54,000 in the reserve banks, upon which they are getting 2 per cent interest. That would be $1,080. The bill as it now stands, with a 12 per cent reserve, of which five-twelfths, which is 5 per cent, would have to be in the vaults, is $30,000, and $30,000 in the Federal banks, and at the expiration of a certain period, a tentative period, the other $12,000 is optional. Under the new law, in your bill as it stands at the present time, the bank would have $18,000. It would have that amount released from its reserves, which would be a reduction of the percentage from the reserve required. In other words, it would have $18,000 more available to be loaned out than it had under the old law. At the same 6 per cent it would earn $1,080, exactly the amount lost, and it suggested in my mind at once that this committee had had some good statistician work it out so that the proposed reserve would exactly destroy that argument that the bank was going to lose in that case. That seemed rather strange—an instance of that kind—that one would offset the other. The gain exactly offsets the loss. Now, 10 per cent of capital withdrawn—$10,000—reduced the loanable funds $10,000, at a loss, we will say, at the same 6 per cent, of $600 a year. Well, if this new experiment is successful, they earn 5 per cent, which would be $500. The apparent loss in that case would be $100.

I did not check my figures up to see if I had omitted anything or not.

Senator Pomerene. Did you take into consideration the fact that when the national bank desires to issue its notes they must have United States bonds, on which they only get 2 per cent?

Mr. Wells. You mean under the existing law?

Senator Pomerene. Under the existing law.

Mr. Wells. No.

Senator Pomerene. And that as against that, with 10 per cent of the capital stock invested in a regional bank, they would have to get 5 per cent on that?

Mr. Wells. No, sir; I did not take that into account.

Senator Pomerene. Did you take into consideration the fact that this bank may have a reserve in the form of a regional bank, to which they may take their securities and get currency whenever they are pressed for it and need it?

Mr. WELLS. That I purposely omitted from the fact. As I said to you, I doubt if that bank would be in a situation to take advantage of that.

Senator POMERENE. That is hardly a fair statement of the situation, is it? Assume your notes with the country bank now are six-months' paper.

Mr. WELLS. Yes.

Senator POMERENE. There is constantly a certain amount of that maturing.

Mr. WELLS. Scarcely. I think you have overlooked one statement that I made. I am only guessing now at my percentages, but I know that it was strictly true a few years ago, and I think it is true now, that 90 per cent of the paper of a bank is maturing on the 1st day of November or the 1st day of December each year, no matter when it was taken, and, as a rule, it was all taken during the previous fall, winter, and spring.

Senator POMERENE. Let us see what kind of bank you had in mind when you made that statement.

Mr. WELLS. I have the ordinary, common, typical country bank in mind.

Senator POMERENE. One that deals wholly with the farmers and farmers' paper?

Mr. WELLS. Oh, no. The truth is that is the bulk of the paper in these country banks in the Northwest.

Senator POMERENE. What portion of the paper is really farmers' paper, compared with merchants' paper or commercial paper?

Mr. WELLS. I remember at one examination of that particular bank, a few years ago, I found quite a surplus and no merchants' paper. The merchants were in very good condition. But had there been merchants' paper there, it would have quite likely found in the same condition as the farmers' paper, as the merchant looks to the farmers to pay him and to pay his notes.

Senator POMERENE. Do those small banks invest in paper such as Wanamaker's and firms of that kind issue at times?

Mr. WELLS. I tell you, it seems to me that those farm districts are very prosperous to assume that they have any more loanable funds on hand than they can employ right in their own neighborhoods. Occasionally they do have, and invest in the same paper as all concerns do.

Senator POMERENE. I wish you would be a little more explicit in stating what you mean by "country banks." Under this bill here we have been discussing central reserve banks.

Mr. WELLS. And country banks.

Senator POMERENE. Reserve banks and country banks, which includes all banks outside of central reserve in the reserve cities. Would you give the term "country bank" as broad a meaning as we have?

Mr. WELLS. Not at all. In speaking of a "country bank" in Minneapolis, of course we refer to those of country banks lying off in the farming districts.

Senator NELSON. With a small capital?

Mr. WELLS. With a small capital of $10,000 or $15,000, and occasionally we find one like the one I referred to, with a capital of $100,000. That is exceptional.

Senator POMERENE. Are you speaking of State banks or national banks?

Mr. WELLS. Country national banks.

Senator POMERENE. And do those country national banks take farmers' paper for six to nine months in a year?

Mr. WELLS. Yes, sir; bushels of it. If they did not they would go out of business.

Senator POMERENE. They do not do that in our section—oh, I withdraw that statement, but not to a very great extent. It is usually three to four months' paper.

Mr. WELLS. With the expectation that it will be paid at its expiration?

Senator POMERENE. Oh, I could not answer that question. I do not know.

Mr. WELLS. Or do they simply renew it at its expiration? It depends upon what the risks are. If it is horses and cattle, or like the grain crop, they might be able to pay more promptly—in the grain-growing regions.

Senator POMERENE. You are speaking of the conditions that are peculiar to your States?

Mr. WELLS. Well, to the Northwestern States. Several of them in that group.

Senator POMERENE. You would suggest, then, that this limit be extended?

Mr. WELLS. The limit of time?

Senator POMERENE. Yes.

Mr. WELLS. I have not given that very much thought. I think I expressed myself a moment ago as not dealing with that kind of paper. Perhaps it would be capable of such investigation and inspection, but any board that would have to pass on it, it seems to me that inspection would be perfunctory, and practically it would simply have to take the word of the country banker, and believe in the honesty of the country banker.

Senator POMERENE. There is another question I wanted to ask you. You made a statement a moment ago in answer to a question of one of the Senators, to the effect that you had probably talked with from 100 to 150 of these country bankers, and had not heard any one express an opinion favorable to the bill?

Mr. WELLS. Yes, sir.

Senator POMERENE. How many of those bankers have read this bill?

Mr. WELLS. I could not make a guess at that. I did not ask that question. I could not tell you.

Senator POMERENE. Was the sentiment which you have given utterance to here due to the fact that they had studied and understood the bill, or was it due rather to the general objection that prevails among bankers that there should be no change in the banking system?

Mr. WELLS. Well, I do not think really that that sentiment prevails among bankers. I think the general feeling among bankers of the country is that there should be a change.

Senator POMERENE. What change?

Mr. WELLS. Any change. The most simple form that can be devised, that will give to our currency elasticity, that, in case of emergency, will give us the funds that are required for the prosperity of the country. And I think the business men of the country, so far as I got their sentiment, do not want anything but that. They believe we have as good a banking system as there is in the world, if we can just get away from the hard and fast feature of it. They have not got the money when they want it.

Senator POMERENE. That is one of the things we want to provide for. Now, another proposition: Am I to conclude from your testimony here it is really your belief that this bill will restrict credits or contract them?

Mr. WELLS. I had a very valuable suggestion made by some gentleman a day or two ago. I asked him that question. He says, "I doubt if any member of this committee or any banker in this country has gone far enough scientifically to determine that question and give an absolute answer to it"; and the suggestion was made it might be a very wise thing if the right sort of experts could be found to take this thing through and, as far as possible, determine, if possible, whether it will result in a contraction or not.

Senator POMERENE. Mr. Wells, we have been trying to do that, and the great banker Forgan expressed the opinion that it would contract credits.

Mr. WELLS. I know; he told me that yesterday morning; but that did not convince me at all.

Senator POMERENE. And the comptroller, Charles G. Dawes, whom I know very well, expressed the opinion it would expand it.

Mr. WELLS. Yes. There you have it. It would seem to me that both men are absolutely honest and that Mr. Forgan may believe the banks would not avail themselves of the rediscount privilege and Mr. Dawes believes they would take advantage of it on a very liberal scale. I should say under this bill you might have any amount of expansion if the banks will avail themselves of the rediscount privilege. I tried to figure that out yesterday on the train, and I could not see but that the country would have an advantage under the rediscount privilege without there must be something wrong I had not discovered yet.

Senator SHAFROTH. You say, Mr. Wells, that you want elasticity of the currency?

Mr. WELLS. Yes, sir.

Senator SHAFROTH. What is your theory as to how that elasticity would be obtained?

Mr. WELLS. As to the exact machinery that should be set in motion to accomplish that result I would not undertake to advise a committee that has given this so much thought. But, roughly speaking, my idea is that we should make the commercial assets of the banks the commercial paper of our banks, upon which our banking system to-days rests—it would be worthless if that paper is not as fine security as there is in the world—to make that the basis for currency. By reason of its being based upon this commercial paper it would automatically retire when the emergency was over, and it should be issued freely and almost without limit in times of stress, simply based upon that; and a very small and inexpensive machine might be set up here for the getting of the billions behind the paper that we require to do business with in those times.

Senator SHAFROTH. Would you enlarge the scope of the paper which would now form the basis of a loan from the regional reserve bank?

Mr. WELLS. No, sir; I think not.

Senator SHAFROTH. The only thing would be that instead of the banks you would have the Government do it direct?

Mr. WELLS. No, sir; not of necessity. I am not going to express any opinion as to whether I think currency ought to be issued by banks or the Government. I do not care, because I believe it can be made absolutely safe in either case, and I do not care whether the Government does it or whether the banks do it.

Senator SHAFROTH. Then, as I understand, if you are not going to enlarge the character of the paper that is going to be the basis for the issue of this money, it is only as to the machinery you object to?

Mr. WELLS. Yes.

Senator SHAFROTH. Then, do you take into consideration that this bill provides that national banks have a right hereafter to take a mortgage upon real estate and relieve the farmers in that way upon one-year paper?

Mr. WELLS. Yes, sir.

Senator SHAFROTH. That is a privilege which they do not have now.

Mr. WELLS. No; and it would not be of any use.

Senator SHAFROTH. It would not be of any use?

Mr. WELLS. Practically. In my judgment, the farmer has no use for one-year paper secured upon his farm. He will take it upon his cattle or growing crops or without security, but upon his farm he will not do it.

Senator NELSON. It is generally for five years?

Mr. WELLS. Yes, sir.

Senator SHAFROTH. You would not want national banks to tie up deposits by making five-year loans?

Mr. WELLS. No, sir. I am not asking any expansion or enlargement of the paper. If you will just permit—if the country bank is not compelled to come into the system, if you will abandon this whole scheme of the reorganization of our banking and currency system and let it rest where it is, with the additional provision that the commercial paper found in our banks may be utilized as collateral for the issue of currency, in times of emergencies, the country banker is fairly indifferent. He would not have the paper to put behind him and would not need it, because there is collateral enough to spare in the city banks in this country in the case of the larger banks to provide all the currency this country needs, and they would not call on the country bank at all. And if it is not forced into it, it is indifferent to it. If it can have currency when it wants it, it could get it from the larger banks.

Senator SHAFROTH. Then, as I understand you, you would not enlarge the character of paper upon which this currency would be issued?

Mr. WELLS. I would not be willing to say that I would.

Senator SHAFROTH. It would appear the objection, then, that you have, is that the banker has no representation in this machinery.

Mr. WELLS. Oh, no. That is not the principal one. That is the only one I have undertaken to tell you of, perhaps, but there are several features in the bill that I do not approve of.

Senator SHAFROTH. You have stated from your figures the country bank won't have any the worst of it.

Mr. WELLS. I hope you won't think the figures are official, because I think I may have made some mistake in there.

Senator SHAFROTH. Oh, no; because we have gone over those figures right here, only with a bank of $50,000 instead of a bank with $100,000.

Mr. WELLS. And of $1,000,000?

Senator SHAFROTH. And of $1,000,000. Oh, they work out the same way, or nearly the same way. So that there is ultimately no loss to the country bank or the city bank; and the advantage he gains is by reason of having the reserve of 15 per cent, 9 per cent of which would be in banks, cut down to 12 per cent, with only 5 per cent required in bank, and thereby releasing that much more money than under the present law. It gives him an advantage that is about equal to his present conditions and the advantage, of course, in times of stress, times of crises, that he has a reserve bank he can go to, at which he can get money. And while he can have all the money of the bank, he would have to have paper to do that, but he will have some and relieve his conditions to the extent of the paper which he does have.

Now, I want to ask you as to the other objection you made, which was that there was no representation. There is a representation in the reserve bank, is there not?

Mr. WELLS. Yes, sir.

Senator SHAFROTH. Three men are to be selected by the bankers?

Mr. WELLS. Yes, sir.

Senator SHAFROTH. And then three men are to be selected from agricultural and other interests?

Mr. WELLS. Yes. I think that is a very fair apportionment.

Senator SHAFROTH. Now, there are six men, and the other three to be selected by the board constitute the representation upon the board of the Government.

Mr. WELLS. Yes.

Senator SHAFROTH. Now, when a man goes to these regional reserve banks—that is, the bank he does business with and he does business with no other—he has a body composed of six men of his own choosing, as against three men of the Government's choosing, and surely that is a representation of him, if he is a banker. When he goes there, these bankers that are there and selected by the bankers will evidently look to his interests as against any oppression that the National Government might undertake to place on him, would it not?

Mr. WELLS. Yes; but they would be powerless as against the supreme power there—the Federal reserve board.

Senator SHAFROTH. You will find it is not contemplated that the individual bankers should have anything to do whatever with the reserve board.

Mr. WELLS. But the Federal reserve board, I understand, is supreme in control of the whole system, including the regional banks, the reserve banks.

Senator SHAFROTH. Certainly; that is true. There has got to be some kind of control over the reserve banks, but the individual banker does not come in contact at all with the reserve board. It is purely where there are disputes arise. It might be he might have an appeal of some kind that the board did not treat him right; but there are the six men, representatives of the bankers, to see that he was fairly protected?

Mr. WELLS. But, Senator, we will assume now, our next administration was to be Socialist, for instance.

Senator SHAFROTH. Yes.

Mr. WELLS. Would you, if you knew that, and that the appointive power and control of the Federal reserve board was to pass into the hands of that sort of administration, would you favor it or would you feel—I have no right to ask you that question—would you believe it would be possible for them to build up, out of that, a political machine that would be greatly opposed to the substantial interests of this country?

Senator SHAFROTH. I do not think they could. Men have got to be controlled by law, and here is the law with relation to this matter, and they are supposed to follow it. I am not going to suppose people are going crazy, but that we are going to have patriots in every business there is. Now, you take the Federal reserve board, your objection can not stand good as to the regional reserve bank, because the individual bankers have got two-thirds of that board. Now, you take the upper board, and it is true there is no one that is to be a banker upon that board. But do you know that the reason of that is that the experience of all European bankers, the central banks, has been not to have a single banker upon their board of directors? That is the experience in every European bank.

Mr. WELLS. Are you quite sure in that, Senator?

Senator SHAFROTH. Yes.

Mr. WELLS. We do not call bankers here just what they call bankers abroad.

Senator SHAFROTH. I mean a bank that cashes checks. You can not find in the banks of Europe any person who is a banker on the board of the Bank of England, the Reichsbank, or the Bank of France, and the reason is because the power to raise or lower the rate of discount is vested in this central board, this reserve board, and the power to do that imparts a knowledge in advance as to when they will do it, and the raising or lowering of discounts is something that affects markets immediately. It produces a little boom in stocks if it is lowered, and it produces a decline if the rates are raised. The result is that it gives a knowledge to a banker who might be on the board by which his individual bank could profit, and the bankers do not want that. They say that is an unfair advantage to the banker, and for that reason there never has been upon the Bank of England a banker in the sense of an officer in a bank or a stockholder in a bank that cashes checks. That is the reason; with that in view this bill has been drawn. It is not against bankers; it is because bankers, in their wisdom in the other parts of the world, have come to the conclusion that the best men for it are really those who are not bankers.

Mr. WELLS. Just a word in there, if I may ask a question. You are getting pretty deep for me. I told you I was not a banker. In those countries to which you refer, does the Government compel all of the private banks, all of the banks outside of the Government banks, to contribute to the capital of that stock?

Senator SHAFROTH. As a matter of fact the central banks are the banks which relieve the other banks. The policy in providing for those banks is that they shall not be mixed up with the other banks, because they deal practically only with the outside banks. It was thought that for that reason bankers should not be upon this central reserve board, because otherwise it might result in favors being shown to a certain line of banks, or something of that sort. Mr. Morgan's bank might be preferred; Mr. Rockefeller's bank might be preferred; something of that kind might get into it. It is supposed that the merchant is the man who feels first the effects of a shortage of currency or of any inflation of currency. He feels, in the first place, the demands for cash for the bills which he has outstanding, and, second, he feels the first pulsation of a change in the money market, and naturally he would be the first to go to the bank and say "We want more currency; our commercial transactions indicate it." The requirements of a director of the Bank of England is that, first, he shall own stock to the extent of £500 and that he shall own a mercantile business of at least £100,000 or he is not eligible. The theory upon which those rules are made is that that merchant feels the impulse; he feels whether or not more money is needed or less money is needed; whether credit should be expanded or whether it should not be expanded; whether gold should be withdrawn or not. That is their theory for providing those rules. Now, I do not see that we will inflict harm or injury upon anybody by adopting the same policy with respect to that.

Mr. Wells. I will tell you, Senator, with perhaps a slight amendment there you would remove a great objection to this bill. It is very evident that this committee has given great study and thought to this bill, but if you will just make it optional and permit us to come in if we wish, I think it will solve the difficulty. If it is such a good thing, if it will work such wonderful results for the banker and the people of the country, why not leave it optional? If he comes in voluntarily, he is going to feel much more satisfied than if he is lashed in, and if he is lashed in he is going to look for faults.

Senator Shafroth. Well, they do not have to apply for a charter for a national bank. He has a perfect right to go out of it if he wishes. He is not coerced. He can reorganize into a State bank and do the same business and keep his own customers.

Mr. Wells. Well, I would not want to argue the question as to whether it would be a breach of faith in changing privileges which have been granted to the national banks and which have extended over a long period of time. If he goes out of it, if he exercises that option of which you speak and goes out of the system, he certainly has given up a valuable interest. A banking franchise, a national-bank franchise, with a well-conducted bank, having run over a period of years, is valuable, and if you are going to force him either to accept this provision of law or to make a voluntary sacrifice of his valuable franchise, I think it is hardly fair.

Senator Shafroth. Banks have already done that, particularly in some of the Western States, where they have found it to their advantage to go from a national-bank system to the State system. There has been no objection on the part of the Government to their withdrawal.

Mr. Wells. This was optional; they were not forced to go out.

Senator Shafroth. It was optional with the banks, and it was also optional with the National Government. Now, when the Government gives that—the option of staying in on its own conditions or of going out of the system—you say it is a breach of faith. Why should that be a breach of faith? You have subscribed to all these things, and we want you to stay in there. When these banks have withdrawn from the national-bank system the Government has never adopted the position that it was a breach of faith on their part in doing so.

Mr. WELLS. If the bank goes on and exercises its privileges in fixed accordance with the law under which it is organized, could not a breach of faith be implied?

Senator SHAFROTH. Neither could it when we adopt the law we are considering. There is hardly a period of years which elapses——

Senator NELSON. If it is such a good thing why force them to go into it?

Senator SHAFROTH. We want one system. That is the reason. The question as to whether this is to be a universal or not, in my judgment, goes to the fact as to whether all the banks of the country are going to come into one system. I would like to see all the State banks come into the system. Of course we have no jurisdiction over the State banks.

Senator HITCHCOCK. Senator Shafroth, I want to call your attention to the fact that we have six gentlemen in this delegation. We have a New Yorker with us to-morrow and it is very important that we should soon get through.

Senator SHAFROTH. All right. I will not ask any more questions of this witness.

Mr. WELLS. Thank you, gentlemen. I am very happy to get through. I fear I have got into a position of a defender of banks.

STATEMENT OF CHARLES M. HARRINGTON, OF MINNEAPOLIS, MINN.

Senator HITCHCOCK. Please state your name, residence, and business, Mr. Harrington.

Mr. HARRINGTON. My name is Charles M. Harrington. I live in Minneapolis; I am a grain dealer and in the grain-elevator business. The companies of which I am an officer operate in about 300 towns where we buy grain from the farmers. We have large storage elevators in Minneapolis, where we store grain, with a capacity of 7,000,000 bushels, and we have 75 retail lumber yards where we sell lumber.

Before proceeding to a discussion of the banking and currency bill now before your committee, this delegation wishes to express its appreciation of the sincere effort that is being made to give this country a sound banking system, and its hope that it will be able through sound and constructive criticism to contribute to that end. We appreciate the great difficulties that surround this subject, and in the presentation of our views wish to make more clear, if that is possible, the effect upon commercial business of the provisions embodied in the bill.

In presenting the requirements of business in the Northwest, it is necessary to understand that we represent an agricultural country, the largest business of which is that of moving the crops. This movement is of a seasonal nature, requiring a very large volume of money, perfect transportation, and perfect terminal and market facilities if farmers are to sell promptly at the world's prices and realize the maximum return upon their products. Of these products wheat is the principal item and may be considered as properly representing the movement of all cereal crops.

Wheat is sold by the producer for cash at his near-by railroad point. It is there received by line elevators, independent country elevators, or farmers' cooperative elevators for storage or shipment to the terminal markets, as the demand may indicate. The records of the railroad and warehouse commissions of Minnesota, North Dakota, and South Dakota show that there are 2,527 line elevators, 1,130 independent elevators, and 857 farmers' elevators, a total of 4,514 in these States. The managers of the 857 farmers' elevators companies claim to handle more than 50 per cent of the total grain purchased. The line companies largely center in Minneapolis, where the principal market is located and where the greater number of important grain and commission firms are likewise located.

Grain and commission firms largely finance the farmers' elevators in the country as well as many independent elevators. There are more than 90 firms or corporations in Minneapolis doing this kind of business. Farmers' elevators are usually financed by advances against bills of lading or on notes secured by the signatures of farmers—stockholders. The proceeds of notes or advances are used in the regular course of business for the purchase of grain coming in from the adjacent districts. Advances of this character represent a total of from $20,000,000 to $25,000,000 yearly, depending upon the amount of the crop and prices. This sum comes from Minneapolis houses in the grain business, who in turn borrow at Minneapolis banks, but are at the same time very heavy borrowers direct from Chicago, New York, and Boston banks, with whom they have their connections. Line elevator companies supply their various elevators with crop-purchasing funds and represent a very large element in the borrowing for the movement of the crop. Their financing is likewise done in part by Minneapolis and local banks, but largely through direct connections with Chicago, Boston, and New York banks. Country banks have but a minor part in the grain movement at the local points. Elevators not owned by line companies prefer to deal with grain or commission firms. Many independent elevators have the same preference. The amount of business left for local banks is comparatively small, and not being equipped or prepared to afford the special facilities required by the trade, notably at terminals, these banks do not participate to any extent.

Crop movement financing, therefore, falls almost entirely upon terminal market banks at Minneapolis and Duluth, and upon Chicago and eastern banks with which the grain commission and elevator firms have their own connections. The volume of these transactions and amounts annually required to move the northwestern crop are indicated by the following official Minneapolis Chamber of Commerce figures:

The Chamber of Commerce in Minneapolis is the grain-trade organization, and I speak of it not in the sense that the expression "chamber of commerce" is usually used in the East.

The receipts of wheat at Minneapolis for the 90 days from September 1, 1912, to December 1 following were 78,074,900 bushels, which, at 80 cents, represents $62,500,000. Country stocks of wheat on December 1, 1912, were 38,000,000 bushels, which, at 80 cents, represents $30,400,000, or a total paid out in cash to farmers to move their wheat during the fall period of $92,900,000.

During the second period, from December 1, 1912, to March 31, 1913, figured on the same basis, there was used an additional sum of $62,090,000. The same figures for the third period, from April 1 to June 30, 1913, represent a total of $22,650,000.

It should be borne in mind that this total amount, $177,640,000, is for the wheat crop only and but for one market. The average receipts for farm products in the three States is several hundred millions of dollars annually.

It is therefore apparent that any disturbance of the credit relations of the great grain markets will have an inevitable effect not alone on the delicate adjustment of market conditions but upon the prices realized by the farmer. Experience has clearly shown that it is the small market operator, the competitor of the larger firms, who sets the price. With his competition removed, through such a process as might hamper or restrict his credit, the market would be in the hands of the more powerful concerns, which through more important and more solid relations as borrowers, with great banks and financial institutions, would weather a period of restricted credit. The ability of the farmer to promptly sell at the world's price depends entirely upon the ability of grain commission and elevator companies to get credit and supply promptly the cash for local purchases of grain. We anticipate that the operation of this bill, as its provisions are outlined at the present time, would restrict this ability and produce such a period of restricted credit as is above referred to.

I am not a banker or interested in banks, and do not claim to be an expert financier. I will admit being a good borrower, as our companies borrow many millions of dollars each year. I have read the proposed bill and many comments upon it, and have heard it discussed, and I believe because of the loss of the savings funds for commercial purposes, the loss of reserve deposits from country banks, and the Government deposits that there will be a very great contraction of credit. The advocates of the measure will undoubtedly say that this will be offset by the ability of our banks to rediscount. A typical case will illustrate what condition might then arise. The probable loss of deposits of one representative Twin City bank which loans freely in support of the grain, lumber, and distributing business—as of the Northwest—will be $6,000,000, or about 25 per cent of its total deposits. This amount, less reserve held against it, represents $4,500,000 of loanable funds. This bank, to maintain unimpaired its present loaning ability, would be forced to carry at all times rediscounts amounting to $4,500,000 with the Federal reserve bank of its district. Such an amount is one and one-half times its entire capital stock. On such rediscounts the bank becomes responsible, and the loans to it by the Federal reserve bank become a lien upon its assets. It is very doubtful whether the directors or stockholders of this institution would permit the assumption of such a risk.

This same condition would prevail in all cases with Chicago and eastern banks.

We have gotten along very comfortably under the present system in spite of the occasional panics and pinches, and it seems to us that radical changes ought not to be made. If a law can be so framed as to give our currency elasticity, and a place provided for our banks to go to for help in an emergency, the business interests will be best served.

Senator BRISTOW. Take the restricted credits that you referred to. I understood that to be withdrawing of deposits.

Mr. HARRINGTON. That is one of them.

Senator BRISTOW. Which this would force from the banks that are now taking care of the business.

Mr. HARRINGTON. Yes.

Senator BRISTOW. So as to compel all business men who are getting these accommodations, as they are commonly called—I do not like that word myself; I do not think it is any more accommodation to the man that borrows the money than to the man who loans it. As a matter of fact the banker that loans the money gets his money back, and it is an accommodation to him to get the business; but that is the term the bankers use to make you feel that they are accommodating you, specially when they loan somebody else's money, and so I will use it. The business man who is accustomed to go to these banks to get the money would have to go to this reserve association.

Mr. HARRINGTON. If these same banks were to give us the same amount of money we would have no objection. The banks themselves would have to go to the reserve banks and indorse our paper, and we would rather hesitate to ask them to do that.

Senator BRISTOW. Would your paper be commercial paper under the common acceptation of that term?

Mr. HARRINGTON. Our paper is made in that form, but we usually borrow six months, and in borrowing in the fall we usually renew until May or June. We fill up our elevators in the fall when the grain comes in and sell the grain in the spring at the opening of navigation or later on when the mills want it. Our paper is never longer than six months, but it is frequently renewed for another six months, so we have the money all the year.

Senator BRISTOW. Do you ever pay off all your indebtedness to the banks, or do you carry an indebtedness right along?

Mr. HARRINGTON. We have several companies, and many of them pay their indebtedness every year in the summer. Between crops all of them reduce it, and at some time during the year they all pay up—all the grain companies.

Senator SHAFROTH. I want to ask you a few questions. You said:

> I have read the proposed bill and many comments upon it, and have heard it discussed, and I believe it will cause loss of savings funds for commercial purposes.

Wherein would there be any change in the national bank law with respect to that now under this bill.

Mr. HARRINGTON. As I understand the bill the savings deposits are to be segregated and used for loaning on real estate, etc. They would not be available for merchants, jobbers, manufacturers, grain dealers, and others. That is what I mean by that.

Senator SHAFROTH. Is not that practically done at the present time in the discounting of notes that are collateral—farm mortgages or securities of such kinds?

Mr. HARRINGTON. No, sir; I understand not.

Senator SHAFROTH. That is the first time I have heard that objection made, and I do not know the full force of it.

Mr. HARRINGTON. I think you will find that the national banks are only required to keep a reserve of 5 per cent on their savings deposits, and then they can use that money to loan to the grain concerns—speaking of our northwestern territory—to our millers, to our manufacturers, and jobbers, just the same as any other deposits.

Senator SHAFROTH. What proportion do the savings-deposit feature of the banks bear to the total amount of the business of the banks?

Mr. HARRINGTON. One of our members will speak on that subject; he has the figures. Personally, I can not give them to you.

Senator SHAFROTH. Well, at another point in your statement you spoke of the loss of reserve deposits from country banks. That is a matter of where you are speaking now of a city bank?

Mr. HARRINGTON. Yes, sir; we borrow our money in the Twin Cities, Chicago, Boston, and New York.

Senator SHAFROTH. And Minneapolis is bound to keep a reserve in Chicago or New York, is it not?

Mr. HARRINGTON. We borrow there, too.

Senator SHAFROTH. Yes; but the national bank of Minneapolis is bound to borrow there, is it not?

Mr. HARRINGTON. I do not know that they do.

Senator SHAFROTH. It is bound to keep a reserve there. It is bound to keep 12½ per cent there.

Mr. HARRINGTON. Yes.

Senator SHAFROTH. Now, then, it would not have to keep that in these banks in New York, because they could then go and keep 9 per cent with the national reserve banks, and thereby it would save 4½ per cent, would it not?

Mr. HARRINGTON. Would not they have that much less in Chicago?

Senator SHAFROTH. One of the objections which has been made among the people has been that too much of this money centers in New York, and that for that reason it is intended to relieve that situation and ease up the banks in the interior. The three reserve cities are St. Louis, Chicago, and New York. In the case of your Minneapolis bank it would gain actually by not having to put up more than 9 per cent, whereas now it has to send to Chicago or New York 12½ per cent.

Mr. HARRINGTON. That may be true. I do not dispute you.

Senator SHAFROTH. Instead of being at a disadvantage it would be an advantage to the Minneapolis bank, it seems to me.

Mr. HARRINGTON. Their losses there in the case I have cited are entirely from banks for whom their reserve agents——

Senator SHAFROTH. The Minneapolis bank would lose some by reason of these banks distributing to the reserve banks, but they gain by reason of not having to put 4½ per cent as much money in Chicago and New York as the present law requires, and that, I think, you will find is fully as much of an advantage as they have now.

Mr. HARRINGTON. It may figure so. I said in the beginning, you know, that I am not a banker.

Senator SHAFROTH. And you further stated that the Government deposit there will be a very great contraction of credit and loss of reserve in the deposits of the country banks and the Government deposits.

Senator NELSON. I suppose that will be covered by something said by some of these other gentlemen.

Senator SHAFROTH. All right.

Senator HITCHCOCK. Mr. Harrington, you estimate about $60,-000,000 of the reserve deposits of country banks that a single bank in

Minneapolis would be required to part with? Can you give an estimate of the amount of reserve deposits which all the Minneapolis banks could be required to dispense with?

Mr. HARRINGTON. No; there are two other banks of equal size there. There are about 18 savings banks of smaller institutions. It would be about $20,000,000.

Senator HITCHCOCK. If these national banks of Minneapolis are required to turn over this $20,000,000 to reserve banks of that district, do you know how those banks will go to work to secure the necessary cash for that purpose?

Mr. HARRINGTON. They would take notes.

Senator HITCHCOCK. That would produce a contraction of credit with the capitalists and would produce a similar contraction of credit in all the 50 reserve cities of the United States.

Mr. HARRINGTON. Yes, sir.

Senator HITCHCOCK. That is all.

Senator SHAFROTH. I want to ask you about your reference about the $500,000,000 to which you referred. Does not that constitute all of the deposits of the country's banks in the one bank?

Mr. HARRINGTON. No, sir; their deposits are $13,000,000, and an officer of the bank stated that they would undoubtedly lose half of that; and so, instead of calling it $6,500,000, I called it $6,000,000.

Senator SHAFROTH. There is no calculation which has been made as to the exact per cent there.

Mr. HARRINGTON. They went to the bank. They made a statement that there was $13,000,000 of that sort of deposits in one of the banks, and I think probably that would be at least one-half.

Senator SHAFROTH. This country bank, however, instead of depositing that $6,000,000 with a private bank in Minneapolis, would deposit that money in the Federal reserve bank in Minneapoils.

Mr. HARRINGTON. If they went in.

Senator SHAFROTH. If they went in. Then the money would be still there, and the right to get it out by the Minneapolis banks or any other bank would be there by borrowing on collateral, would it not?

Mr. HARRINGTON. I have stated so; but I doubt if a bank would want to go in there and indorse the paper of their customers to the extent of $6,000,000.

Senator SHAFROTH. They do not have to do it.

Senator NELSON. They have to do it to get the currency, don't they?

Senator SHAFROTH. That is all true; but it is the individual bank, the country bank, that indorses the paper. He does not go to the city bank and get it to indorse the paper for him. It is simply the one bank that indorses the paper. If they would do it in one instance, it seems to me it could be done in another instance.

Senator BRISTOW. The Minneapolis bank is going to use the same process that the country bank would.

Senator SHAFROTH. Certainly it would, but it has the collateral there. It has this commercial paper, which it can present there and get currency, and put that currency in circulation, and it will permeate to all parts of the country.

Senator BRISTOW. But it has to get it just as the country bank would.

Senator SHAFROTH. Certainly; the Government is not going to give it to him.

Senator HITCHCOCK. Your point is, Mr. Harrington, that you think it doubtful whether this particular bank, in order to secure the $6,000,000 which it would part with, would be required to indorse $6,000,000 of good commercial paper and discount it with the reserve banks?

Mr. HARRINGTON. That is the idea.

Senator HITCHCOCK. And you doubt whether the bank would care to indorse $6,000,000 of paper?

Mr. HARRINGTON. I doubt if they would be willing to do it. Of course, it would make no difference to us.

Senator O'GORMAN. Do you think a bank would hesitate to indorse good and merchantable paper when the paper was so good that it would be prepared to discount it itself and get the money into its vaults?

Mr. HARRINGTON. I do.

Senator O'GORMAN. Why?

Mr. HARRINGTON. Because it is contrary to all good banking under the present arrangements.

Senator O'GORMAN. This system contemplates the change.

Mr. HARRINGTON. Under the new system, if it should become popular, they might do it. Perhaps they will do it. I hope they will do it, because we will have to do business under this new system.

Senator O'GORMAN. It is conceded at the present time that rediscounting is regarded as poor banking, but if you assume that this legislation will lead to a change in that respect among the bankers of the United States, then the objection you have just pointed out would fall?

Mr. HARRINGTON. Certainly; if we get the same amount of money it would make no difference.

Senator BRISTOW. Is it not a fact that this bill will force either a change of the practice or result in the contraction which you suggest?

Mr. HARRINGTON. Yes.

Senator BRISTOW. It is regarded bad banking to be hawking your paper around and selling it. The customer does not like it and the bank does not like it. It is proposed by this bill either to compel the banks to do that or it will result in a contraction of the credit.

Senator SHAFROTH. Let me ask you one more question. Is not the difference between whether the Minneapolis private bank discounts this paper or the Federal reserve bank discounts it—is not this an advantage in favor of the discounting by the Federal reserve bank, and that is when you deal with the Minneapolis private bank all that it does is to settle differences between customers and the bank itself; whereas, in addition to the Federal reserve bank doing that same thing there is an element of increasing the currency which goes into the hands of the men—the country bank and the business which it does, and it increases the circulation and thereby makes times better. Yet you ignore that great advantage in your discussion of this question with relation to the discounts to be made with the private bank of Minneapolis and the Federal reserve bank of Minneapolis.

Mr. HARRINGTON. Perhaps I have, sir.

(Thereupon, at 5.45 o'clock p. m., a recess was taken until tomorrow, Wednesday, September 24, 1913, at 10 o'clock a. m.)

[END OF VOL. 1.]