BANKING ACT OF 1935

MONDAY, MAY 27, 1935

United States Senate,
Subcommittee of the Committee on
Banking and Currency,
Washington, D. C.

The subcommittee met, pursuant to adjournment, on Friday, May 24, 1935, in room 301, Senate Office Building, Senator Carter Glass presiding.

Present: Senators Glass (chairman of the subcommittee), Bulkley, McAdoo, Byrnes, Bankhead, Townsend, and Couzens.

Present also: Senator Norbeck, of South Dakota.

Senator Glass. Doctor Miller, you may resume your statement.

STATEMENT OF ADOLPH C. MILLER, MEMBER OF THE FEDERAL RESERVE BOARD, WASHINGTON, D. C.—Resumed

Mr. Miller. Mr. Chairman, I want to say a word or two very briefly regarding what I think may have been a misapprehension with respect to a reply that I made to Senator McAdoo Friday morning when he asked me with respect to our currency, whether it was printing-press money, and I replied, "Yes." He asked the question in a technical, matter-of-fact way, and I answered it in a technical, matter-of-fact way, implying by the statement only this, that it was not technically a convertible currency. But no implication was intended by me as to the character or quality or goodness of either our currency or of any so-called "printing-press currency." Of course, our own currency has stood up beyond possibility of criticism since the period of the suspension of gold redemption. The same is true of the British currency. The same is true of the Swedish currency.

There is nothing inherently vicious in the fact that currency is not redeemable. The prejudice against so-called "irredeemable" currency gets its foundation from the fact that usually, in time, and given time, it goes wrong and then becomes an unsound and injurious element in the circulation of the country.

Senator Bulkley. Doctor, will you make clear for the record under just what circumstances a person might get gold now for currency?

Mr. Miller. In this country?

Senator Bulkley. Yes.

Mr. Miller. I know of none.

Senator Bulkley. In the settlement of export balances, is there no way of getting gold?

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Mr. MILLER. There is no method by which an individual American can get gold, unless it be by acquiring a balance on export, or through the purchase of exchange upon some country such as France, we will say, where there is still convertibility of credits in gold.

Senator BULKLEY. That would involve buying French currency. Can you not get gold at all for our currency?

Mr. MILLER. I know of no method. I have not tried it, but I know of none. I have not heard of any. There is no redemption.

Senator BULKLEY. There is no free redemption, but you say there is absolutely no redemption of any kind.

Mr. MILLER. No redemption whatever. If I am in error about that, I would like to be set right.

Senator BULKLEY. I am not sure enough to press it. I was under the impression that there were some circumstances under which you could get gold.

Mr. MILLER. There can be no discriminating redemption, Senator. If there is redemption for one dollar there is redemption for another dollar.

Senator BULKLEY. There is discriminating redemption in France, based on the amount that is redeemed, is there not?

Mr. MILLER. Yes. You have, in certain countries, what is sometimes called "bullion redemption." You had it in England before she suspended the gold standard; that is, you could get redemption only upon amounts of a certain size but no redemption on amounts under that. I think under the British gold standard of 1925 the redemption was absolutely in bullion, and only in bullion, but not in sovereigns.

Senator BULKLEY. Up to a few days ago you could get any amount of gold against francs by having enough to get a bar, could you not?

Mr. MILLER. Yes, sir.

Senator BULKLEY. I believe they have put some new restrictions on it very recently.

Mr. MILLER. I think that is true. However, I am not fully informed as to what the immediate status is. Gold is procurable here on permission for export. That you know.

Senator BULKLEY. But that has nothing to do with currency.

Mr. MILLER. It has a great deal to do in its effects upon the maintenance of the dollar in international exchange, but it has nothing to do with redemption per se.

Senator BULKLEY. Let me ask just one further question. Where does the significance come in of our being attached to the gold standard at all? In other words, what is the practical significance of the fixing of the new gold content of the dollar, and in what way are things any different since that was done than they were when we were off the gold standard and before the Gold Reserve Act was passed a year ago?

Mr. MILLER. I think none, actually, but that is a matter of difference of opinion.

Senator BULKLEY. You think there is no difference?

Mr. MILLER. I think there is none, if I understand your question. I am thinking, in answering the question, of the economic effects that followed the one course as compared with the other, not the legal factors or the legal fictions.

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Senator GLASS. Do you have any expectation or hope of this country getting back on a metallic standard?

Mr. MILLER. Senator, it is easy to indulge a hope; and, of course, I indulge that hope. When it comes to an expectation, I am inclined to think that much, if not all, will depend upon how soon the world returns to a state of normal mentality, and governments, in their relations to one another, are actuated by reasonable respect for world opinion, and interlocking mutual world interests, and upon how good an account of themselves in the interim these various monetary provisional systems that have been set up in the last few years give. If, perchance, they should give a good account of themselves, I would be inclined to think that we would have an international gold standard restored but in a form different from that which prevailed before the suspensions.

Senator GLASS. If you attach no importance to a metallic standard in which paper money may be redeemed, why have it?

Mr. MILLER. Of course, the importance that has been attached to it, and the importance I attach to it, is derived from the fact that up to this day it has never yet been demonstrated that any agency can be invented to which power to govern the currency could be intrusted without ultimately disastrous consequences. Whether that is inhereint in the situation or whether we have a new psychology, a new sense of responsibility and of the seriousness and gravity of the problem, I do not know. I am inclined to think that there has been a good deal of growth of appreciation of monetary problems, the relationship of monetary management to the good functioning of the economic system; and it is possible that out of that may come a better regime in the future than we have had in the past, where we have been willing to trust the economic fate of the country to—call it what you want; in the old-fashioned terms "paper money"; or in the new-fangled terms "managed currency."

Senator GLASS. You will recall very distinctly, I am sure, that those of us who undertook to manage the Federal Reserve bill through Congress encountered the very bitter criticism from Senator Root and others that it was a fiat currency, notwithstanding that we had 40-percent gold reserve, and 100 percent of liquid commercial paper of short duration behind it. Why all that ado if a metallic standard is of no account?

Mr. MILLER. The metallic standard, as I think, justified itself in the past, but I think the more recent economic history of the world, and the history of our own country in the post-war decade, has demonstrated that the metallic standard alone, under certain conditions, is no guarantee of economic safety. The old currency policy of the different countries was to maintain the external stability of their monetary units. External monetary stability on fixed exchanges was what they were after.

Our experience, in the anomalous position of the world in the twenties, showed that a country could be in an impregnably strong gold position, and have its exchanges beyond any possibility of assault, and yet have a regime as to currency and credit that nursed factors of economic instability, so that out of that I think we have had a rather more exacting conception of what—to use the conventional phrase—sound money has got to imply in the future. In

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other words, that it is not alone sufficient that you should have convertibility, redeemability of the currency in gold to insure good credit and economic conditions so far as they are affected by changes in the quantity and quality of a country's money.

Senator GLASS. Do you think Great Britain went off the gold standard willingly?

Mr. MILLER. No. She was swept off by the force of circumstances. There was no alternative.

Senator GLASS. Is it your opinion that Great Britain would very earnestly desire to get back on the gold standard when it has gold enough to justify it?

Mr. MILLER. I would expect that the British will remain true to type, and that when they judge that conditions are favorable—not only material conditions, but the mentality of the world—they would wish to restore the gold standard in some form.

Senator GLASS. Why do that, if it is of no consequence?

Mr. MILLER. Because it gives to the world what the world, I think, will not be able to dispense with, a common international currency, something in terms of which——

Senator GLASS. Why does the world think that, if it is of no consequence at all? Why does the world think it is of consequence? Is not that the history of banking and currency for several hundred years?

Mr. MILLER. Yes. I think it is of consequence, Senator. I think it is of very great consequence, but I think it is also of consequence, in the times into which the world is moving——

Senator GLASS. Do you think that [producing a $10 bill] is money?

Mr. MILLER. Yes. If you do not, I will take it.

Senator GLASS. Will it pass anywhere in the world at its face value?

Mr. MILLER. No.

Senator GLASS. Why not, if it is money?

Mr. MILLER. I said it was money. I did not say it was international money.

Senator MCADOO. No currency of any other nation passes every other nation at par.

Senator GLASS. Oh, yes. When we were on the gold standard, a pound sterling passed America for its face value, just as much as it did in London.

Mr. MILLER. With those who knew it. I fancy if you went into the Ritz in Paris, or the Carlton in London——

Senator GLASS. If you presented a pound note to a man who had never seen one before, he would not know what it was, and would not want it. But I am talking about people who know what it is.

Mr. MILLER. I am inclined to think that if you went into a Paris shop or hotel and offered this, you would not be allowed to get away with it. They would take the note, and you would get the goods.

Senator GLASS. Yes; but you would get them at a very much reduced value. I know that by experience in London. I offered them, and I had to pay the reduced exchange.

Mr. MILLER. You get it at the current exchange. You would not get it at the old gold parity exchange.

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Senator GLASS. Why not? What has the gold parity got to do with it, if you say it is of no concern, and if that is money, why does the United States of America promise to pay you money for it?

Mr. MILLER. That is a question I would rather not discuss.

Senator GLASS. That is a promise to pay. That is not money.

Senator MCADOO. The chairman has an archaic note at the moment. If you get some of the new ones, they do not have that on them.

Senator GLASS. No; I have not got any archaic note, either. I have a note signed by "the greatest Secretary of the Treasury since Alexander Hamilton." That is not archaic.

Senator MCADOO. Where is it?

Senator GLASS. I do not mean any reflection on you.

Senator MCADOO. I thought it was your own note.

Senator GLASS. No; it is not.

Senator MCADOO. You are the greatest Secretary of the Treasury since Hamilton. I yield the palm. [Laughter.]

Senator GLASS. I was the greatest Secretary of the Treasury since William G. McAdoo.

Senator MCADOO. Do not get ironic.

Senator GLASS. This is signed by Mr. Mellon, so it is not archaic. I do not care to pursue the subject any further.

Senator MCADOO. What I mean, Mr. Chairman, is this. This has all been by way of pleasantry. Of course, since we went off the gold standard these notes issued prior to that time call for something which the Government is not now doing. In other words, it is not paying in gold.

Mr. MILLER. That is true.

Senator GLASS. Do you think this note is worth as much as it was before we went off the gold standard?

Senator MCADOO. I think so.

Senator GLASS. You go out and try to buy some white meat, as my chauffeur does, and you will have to pay four times the price for it.

Senator MCADOO. I think it is just as good in domestic commerce as it was before we went off the gold standard.

Mr. MILLER. It is not legally convertible.

Senator GLASS. It passes in domestic commerce, but not at the same value.

Senator MCADOO. That is because the prices of commodities have gone up; not because we have gone off the gold standard, but for other reasons.

Senator GLASS. Why? Because cotton has been plowed under, and hogs slaughtered, and so forth?

Senator MCADOO. Yes.

Senator GLASS. Of course, those things are contributory to the existing condition.

Senator MCADOO. I do not think you can attribute it solely to gold.

Senator GLASS. Not solely.

Senator MCADOO. You have devalued also.

Mr. MILLER. You have devalued. I should say, Senator, that the modern world must distinguish, in order to think on monetary subjects clearly, between technical legal convertibility and what I would call economic convertibility—what you can buy with it.

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Senator GLASS. Let us go ahead with the bill.

Senator McADOO. I would like to interject, if I may, just a word——

Senator COUZENS. We are going to have to discuss all this when we get into executive session.

Senator McADOO. I am very much interested in what you say, Doctor, because I think the trend of all you have presented here is in line with what is being considered even in Great Britain and other great powers, and I think it is inescapable. I think Sir Reginald McKenna, if I have not misread the papers, or if he was not misquoted in what I saw in the papers, has expressed views quite similar to those you are putting forward here.

Senator BULKLEY. Sir Reginald McKenna does not believe in going back to the gold standard at all. I am sure of that. In that respect it is different from what Doctor Miller said.

Senator McADOO. I said "somewhat similar."

Mr. MILLER. I do not want to speak for Mr. McKenna, and I do not presume to know what is in his mind, but I think what may be in his mind is in the minds of a great many people, that we go back to a gold standard that has a bigger element of management in it than the old gold standard before the war, just as the gold standard we had in the twenties——

Senator BULKLEY. He may have changed his mind in the meantime, but about a year and a half ago he told me definitely that England should never go back to the gold standard.

Mr. MILLER. I would not venture to quarrel with Reginald McKenna, for whom I have very high esteem, but I would venture to prophesy that he is in error, and that she will go back, and we will go back.

Senator BULKLEY. You do not think England will ever go back to the old gold content of the pound, do you?

Mr. MILLER. I think they will allow that to be governed by circumstances, and not undertake to make the circumstances. I think they will establish the value of the pound, when they do establish it again, exactly as they did in 1816. They did it then in a very practical way, and I think they will do it exactly on the same basis in the future.

Senator BULKLEY. They established the value in 1816.

Mr. MILLER. They will do it realistically, with the intention of making the value of sterling——

Senator McADOO. In the light of conditions existing at the time.

Mr. MILLER. Absolutely.

Senator McADOO. You do not mean to say you think they will go back, necessarily, to the same standard?

Mr. MILLER. Not at all.

Senator BULKLEY. The value in 1816 represented a devaluation, did it not?

Mr. MILLER. A slight change; but the idea was to get a unit that would maintain itself and therefore be recognized as a unit all over the world, in which you could safely trade. I think they will do it again.

These things are all aside of my purpose, Senator, and I have no desire to pursue them.

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Senator GLASS. Oh, yes; you can trade in paper with more facility than you can in metal, though.

Mr. MILLER. I am inclined to think that their thought in those things will be highly constructive and be based upon the great mass of experiences that have percolated into the British mind and British character.

Senator BULKLEY. Doctor, you did testify that no matter whether we like it or not, we are bound to go into a certain measure of conscious control of currency, did you not?

Mr. MILLER. I do not care anything about the "conscious" part. I think that is gratuitous.

Senator McADOO. We are going into control.

Mr. MILLER. Into a greater measure of management, if you want to use the word.

Senator BULKLEY. Yes; that is a satisfactory word.

Mr. MILLER. Than has been true in the past. I dare say it is quite within the region of probability that there will be some degree of concert of interests and responsibility among the leading gold-standard countries, with a view of tempering and steadying the action of the gold standard so as to avoid those ruptures and breaks and occasional serious disturbances that characterized even the old gold standard when it was working pretty efficiently. Even the old prewar standard in Great Britain had its action tempered by the wisdom of British financial authorities, treasury authorities, and, chiefly, the Bank of England. That is why it was such an excellent standard. They did not simply let it take its own course.

Now, gentlemen, if I may proceed, the two previous hearings have ranged over a pretty wide field. We have come back to the same topic in one connection or another. I want to gather up just a few skeins before I proceed this morning.

I have indicated, in answer to certain questions in the previous hearings, that it was my belief that conditions had clearly indicated that it was necessary to get a more definite concentration of authority and responsibility with respect to the open-market policies of the Federal Reserve System, particularly in the future. I shall presently present a plan or set-up for the open-market committee of the Federal Reserve System which, in my judgment, would, if adopted, promise as good a result as we have any right to expect.

Senator GLASS. Right on that point, and altogether pertinent to the discussion, what trouble have you had with the present statutory open-market committee?

Mr. MILLER. The present statutory system goes back to 1933. There has been only one operation of considerable magnitude that has called for open-market policy.

Senator GLASS. The act of 1933 simply confirmed and continued the open-market system that had long been in practice.

Mr. MILLER. Yes.

Senator GLASS. What difficulty did you have with that?

Mr. MILLER. We had difficulties.

Senator GLASS. What were they? Were they insuperable difficulties, or were they difficulties that were adjusted?

Mr. MILLER. Two or three of them proved to be—I will not say insuperable, but, at any rate, resulted in a determination that, I

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think, the Federal Reserve Board would have preferred not to have been reached.

Senator GLASS. Would you mind giving us the examples for the record?

Mr. MILLER. I have not the record here, but I will say that in 1931 some of the Reserve banks and the Reserve Board had reached the conclusion that it would be desirable to try to relieve the situation by an open-market operation of considerable extent. Strong opposition was encountered on the part of two or three of the reserve banks, with the result that the outcome of the discussions was that an open-market operation was undertaken, but to a very much more limited extent than the Federal Reserve Board and some of the Reserve-bank governors would have wished to see.

Senator GLASS. Do you mean to say you wanted to buy more than two and a half billion of United States securities?

Mr. MILLER. Not all at once. Three or four hundred million, I think, was under discussion at that time.

Senator GLASS. Were not the resources of the remaining 8 or 10 Federal Reserve banks sufficient to have made the purchases if they had wanted to?

Mr. MILLER. Yes, Senator; but under the set-up which had been in effect for several years, we regarded operations of that character as system operations, to be undertaken by the Reserve banks generally in participation, and on this particular occasion there was one of the Reserve banks that, as I remember, was willing to shoulder far more than its proportion if it were decided to go ahead with the operation on the enlarged scale. There was good cooperation, let me say, at that particular time from the New York Reserve Bank, but there were some of the interior banks, and one of the eastern banks, that took a different view and held off. I do not know whether it would have made any difference, and I know no method of finding out whether it would have made any difference in the outcome if the larger operation had been undertaken at that time.

Senator GLASS. The law did not require unanimous action.

Mr. MILLER. No; it did not.

Senator GLASS. And you say that the resources of the remaining 10 banks were ample to take care of the matter?

Mr. MILLER. Yes.

Senator GLASS. Why did they not go ahead?

Mr. MILLER. I am answering your question as to whether or not the thing had always worked satisfactorily. From my point of view, a satisfactory operation is one in which, when the decision is reached, all the banks accept it and go ahead and participate pro rata.

Senator GLASS. Whether their boards agreed that they were in financial condition to do it or not?

Mr. MILLER. They all were in financial condition to do it.

Senator GLASS. You think so, but perhaps their boards did not think so.

Mr. MILLER. Well, Senator, there are times, I should say—and those, in my judgment, are the only times; I have no hesitation in saying that emphatically, that they are the only times—when the Federal Reserve System, whether it is 1 bank or 12 banks, should engage in open-market operations, from broad considerations of national economic interests.

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Senator GLASS. I know; that has been your view all along.

Senator McADOO. Somebody must make the decision.

Mr. MILLER. Somebody must make the decision. Somebody must take the responsibility, and once the thing has been thoroughly discussed and canvassed, and the decision has been reached, I think there ought to be no obstructive action possible by a division of responsibility for action among the several Federal Reserve banks. Open-market policy is peculiarly a national policy, and if it be kept as a national policy and operated only on broad grounds, and when the indications of its need are clear I do not think there is anything to fear in the way of bad action through withholding from any indidividual reserve bank the power of veto so far as itself is concerned.

Senator GLASS. And yet, in the whole 20 years of the existence of the Federal Reserve Banking System, and more, the Federal Reserve Board, so far as I can recall, has never agreed that that should be the case. At least, it has never recommended to Congress that that should be the case.

Mr. MILLER. I have.

Senator GLASS. I know that has been your view all along.

Mr. MILLER. Sometimes, Senator, men do not make recommendations until the situation has become pretty urgent, and experience demonstrates that there has got to be a change in the set-up. I reached the conclusion, after the first great operation in 1924, that the country was going to be in jeopardy economically unless the Board was given a definite responsibility for the outcome of open-market operations.

Senator GLASS. The right to compel banks to use their resources and the resources of their depositors, whether they thought it was prudent to do it or not?

Mr. MILLER. Provided the Board, on full consideration and full canvass of the situation with the operating heads of these banks, as a whole, had reached the conclusion that it was essential in the public interest. Yes; I stand by that.

Senator McADOO. You are really arguing simply for what we do for the President. We give him extraordinary powers to make decisions.

Mr. MILLER. Yes.

Senator McADOO. And everybody respects them. There is a concentration of authority upon important questions which is essential at times.

Mr. MILLER. More important, I think, Senator, is the concentration of responsibility. If there is a blunder then, you know who is responsible for the blunder.

Senator GLASS. You do not think that the people whose property is to be expended should have any voice in the matter?

Mr. MILLER. I would say, Senator, that if the powers are wisely exercised it is going to be one of the best protections of the people whose property is being used for this purpose. That is my feeling; and I should feel, as a private citizen——

Senator GLASS. Of course, anything that is wisely done protects anything to which it is related. But I have never been able to discover that the Federal Reserve Board was any wiser than some other boards.

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Senator McAdoo. We took all the gold that belonged to everybody in the country.

Senator Glass. "We took it"?

Senator McAdoo. Yes.

Senator Glass. You may have. I did not.

Senator McAdoo. I am talking about Congress and the President.

Senator Glass. Congress has surrendered every power it ever had under the Constitution, for that matter, but I did not agree to it.

Mr. Miller. Someone here, I understand, made the inquiry the other day of Governor Eccles as to what difference he thought it would have made in 1928 and 1929—if those were the years; they may have been earlier—if the Board had had the powers that are proposed in this bill. I have not read his answer, but I have seen some notice of it in the paper to the effect that it would have made a difference in 1931. From my point of view it would have made a lot of difference in 1928 and 1929.

Senator Glass. You did not even exercise your simple power to kick a man out of a Federal Reserve bank who told you to go to hell, and that he was going to do as he pleased, and the next day he was going into the stock-gambling market and getting $25,000,000 from the Federal Reserve bank and using it for stock-gambling purposes.

Mr. Miller. I think very much is to be said for your feeling, and I am obliged to say that I think your view is right. I felt that way at the time, but, nevertheless, that is a pretty extreme thing to do.

Senator Glass. It is a pretty extreme thing for the president of one of the biggest banks in the United States, and a member of the Federal Reserve System, to tell the Federal Reserve Board to go to hell, and that he is going to do what the law says he should not do.

Mr. Miller. I entirely agree with you, Senator, and yet I believe that if the Board had been in a position where its responsibility for open-market policy had been inescapable in 1927 and 1928—it did not make any difference in 1929—you would not have had the situation that we got into in 1929, and the gentleman to whom you referred would not have had, probably, any occasion——

Senator Glass. But, Doctor, you bought 2½ billion dollars of United States securities. How many more would you have bought just then?

Mr. Miller. We bought them after that, Senator. At that time, in 1928, we were selling, and late in 1927, we were selling Government securities in order to get control. My belief is that if the Board had been charged with responsibility we would have gone very much more prudently in 1927. We would have paid far less attention to the importunings of the New York Federal Reserve Bank and the maneuverings that went on in some of the interior Reserve banks, because the Board would have been distinctly on notice that it would be held publicly accountable for the results.

Senator Glass. The New York Federal Reserve Bank wanted to stop that excessive stock gambling by raising its rediscount rate.

Mr. Miller. Yes; in 1929.

Senator McAdoo. After the fact.

Mr. Miller. After the fact.

Senator Bulkley. The difference you are referring to is in 1927.

Mr. MILLER. I do not want to get unnecessarily diverted. I do not know how much time the committee wants to give me, but I have certain constructive suggestions I want to get before the committee.

Senator McADOO. I would like to hear them.

Senator GLASS. I will stop.

Senator BULKLEY. The big difference, that you characterized as a "hell of a difference"—what was that, specifically?

Mr. MILLER. Specifically this: That in 1927, when a major operation was engaged in by the Federal Reserve System in the purchase of securities in the open market, and one that gave the final boost to a speculation that proved to be wellnigh uncontrollable—actually uncontrollable, I think, in 1929—I think the Board would have hesitated a long, long time to engage in it, if the full responsibility had rested with the Board, and with it alone. I think the Board would have taken a far more serious view of its responsibility. There had always been questions raised in these discussions as to just where the authority of the Board ended, and where the authority of the banks ended.

Senator BULKLEY. But you think you would not have engaged in that operation of buying Government securities in 1927?

Mr. MILLER. I think there might have been hesitation. I think it would have given a talking point to the members of the Board who at that time had the gravest misgivings about it, and to whom it was constantly replied "The act confers these powers upon the banks. If it intended the Board to exercise them, why didn't it give them to the Board?"

Senator McADOO. I do not think myself, Doctor, and have never thought, that the mere raising of the rediscount rate would, of itself, be adequate to meet that situation. I think that when you have such a wild orgy of speculation as went on at that time people are willing to pay any rate, because they see the chance to make a great profit on the exchange, and the speculative fever could not be controlled by that remedy. Moreover, you could not make the rediscount rate effective so long as you did not have control of the financial situation. The Federal Reserve System controls only a part of the resources of the country. The influx of foreign capital attracted into the market when there appear to be great opportunities for profit on the stock exchanges, the enormous surpluses owned by corporations, and the great wealth owned by individuals, are all thrown into the market, and the Federal Reserve Board cannot control it.

Senator GLASS. Oh, yes; it can do it.

Senator McADOO. Partially.

Senator GLASS. That was corrected in the act of 1933.

Mr. MILLER. That is true.

Senator McAOO. I am speaking of the time prior to 1933. This last act did give the power, but prior to that time they did not have it.

Senator GLASS. That is all swept away.

Senator McADOO. We were talking about 1927, 1928, and 1929.

Senator BYRNES. May I ask if we can let the doctor present his constructive suggestions? At 12 o'clock some of us are obliged to leave.

Mr. MILLER. In a few moments I shall read——

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Senator BYRNES. I should like to hear the discussion on the bill.

Mr. MILLER. This all has its relevance and pertinence, Senator.

At any rate, before I read a set-up for the open-market authority in the future I want to state again my position, with some slight elaboration. The authority should not be conferred upon the Board unless you are prepared to give to the Board a status of complete independence. From my point of view, when I ask for the authority, I lay that down as a sine qua non. By complete independence I mean one that is completely independent of any improper influence, or any legally suggested influence on the part of the banks of the country, or any influence from the side of the Government.

Senator McADOO. You speak of political influence as well, of course.

Mr. MILLER. Both. I do not like the term "political." It is not political.

Senator McADOO. I know; but that is the common denominator.

Mr. MILLER. You were Secretary of the Treasury, Senator McAdoo, at one time, and so was Senator Glass. Both of you had a great part—the foremost part, next to the President of the United States—at that time in the creation of the Federal Reserve System. You had great and rightful pride in your achievement. I recall particularly in the days before the war Senator McAdoo was a very frequent—almost a regular—attendant at the meetings of the Federal Reserve Board, interested in its proper development. There was no political interference of any character. That was true of Senator Glass. It was not so true of one of his assistants during the short period of a year or so that he was Secretary of the Treasury. But those things have changed.

Senator McADOO. I was only referring to political influence in the sense that so many of the bankers have spoken about it here. I assumed, therefore, that what you meant was the exercise of influence through political power upon the Board, whose independence you feel ought to be established beyond question.

Mr. MILLER. I do; and I say again that in asking for the authority I am not by any means minimizing the mental suspiciousness of the bankers. I think there is a real basis for it, but I think that basis can be cured and should be cured before this authority is conferred upon the Board.

Senator BULKLEY. What do you advise us to write into the bill to cover that?

Mr. MILLER. I would advise as a premise that you write into the law an amendment that no member of the Board shall be removable from office during the term for which he was appointed. First and foremost, that.

Senator GLASS. Except for malfeasance?

Mr. MILLER. I do not have that in the amendment, but I have it in mind.

Senator BULKLEY. If that is not constitutional, what would you substitute for it?

Mr. MILLER. I think it is constitutional. I am no lawyer, but I have read the Constitution of the United States and have reflected on it, and I rather expect that when we get the decision of the Supreme Court in the *Humphrey case* it will be cleared up. I think that it

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should be written into the terms of the Federal Reserve Act, if you men really mean to set up a sound currency management in this country, that the Federal Reserve Board, when granted these powers, is to be independent in their exercise.

Senator GLASS. Would that necessarily legislate the Secretary of the Treasury and the Comptroller from membership on the Board?

Mr. MILLER. Yes. I would say this in respect to the Comptroller—though I do not want to get diverted; I want to proceed with the main matter—

Senator MCADOO. Perhaps it would be well to have them appointed as Federal judges are appointed—during good behavior. That is the term I believe, used with respect to the appointment of judges. You would not appoint them for life; you would appoint them for definite terms to hold during good behavior?

Mr. MILLER. Congress itself to be the judge.

Senator MCADOO. It has the power of impeachment unless we by statute set up some other method.

Mr. MILLER. I do not care what the method is; but, in my judgment, the Board should not be given these powers unless you are at the same time willing to confer upon it a status that is as impregnable against influence as it can possibly be made in law. And when I say that, I am talking out of the depths of my experience of 20 years in the Federal Reserve System. I would not ask the Congress to entrust us with these powers if it is not willing to give us the necessary independence in the exercise of them. I think it is going to be a very difficult thing at best; and only a body of men who are permanently interested in the thing, who make it their day-to-day and year-to-year responsibility, can do this job without damage to the country and possibly very serious damage, unless they are put in a position where nobody can interfere with the free exercise of their judgment and their sense of responsibility.

Senator GLASS. Or unless they are competent to do it?

Mr. MILLER. Yes.

Senator MCADOO. That is just the question.

Mr. MILLER. I know of no legislative formula by which that can be accomplished; but I will add, gentlemen, that it is amazing how good a performance you can get from men if they are in a position where they have to exercise a very quick and constant sense of responsibility. I think that will be the case in the Federal Reserve System. There would always be men there—and I think that is what the original set-up of the act contemplated—who have experience. You would get continuity. The older men have acquired a certain body of knowledge that gradually the newer men begin to absorb, and the sense of responsibility quickens intelligence and arrives at decisions that probably are as good as we could expect to get under our framework of government.

Next, I would earnestly recommend to your favorable consideration a provision for a retirement allowance for members of the Federal Reserve Board who attain the age of 70 years. It does not mean anything to me, but I am convinced that it would make a considerable difference in getting continuity of service on the Board.

Senator MCADOO. You mean, a retirement allowance analogous to that which is given judges?

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Mr. MILLER. Yes, sir.

Senator TOWNSEND. Would you compel retirement at 70 years of age?

Mr. MILLER. No; I would not—but I am not so sure about that; I am not so sure. That is a debatable question. I am inclined to think that age is not a conditioning factor in types of work where judgment, maturity, wisdom, and so forth, count. If it were more definitely an executive routine job——

Senator MCADOO. Or if it were manual labor, for instance?

Mr. MILLER. We would not think of such a limitation in connection with the Supreme Court and the Senate.

Senator MCADOO. I hope not, with respect to the Senate.

Mr. MILLER. Thank God, there are some men there who have grown to intellectual and spiritual maturity through long life and experience. I am not very far behind you, Senator, but I still think that I am of some use on the Federal Reserve Board. Any provision in that respect will satisfy me. I am not arguing for anything personal. I am arguing for what I conceive to be the good of the System.

Third. I would suggest, particularly if the title of "governor" is conferred upon the executive heads of the banks, that you change the set-up of the Board and that it be made the Board of Governors of the Federal Reserve System. If you confer this open-market authority or other similar authority upon the Board, it in fact becomes a board of governors of the System, electing its chairman or, if you prefer, having its chairman approved by the Congress. My own view is that we would have gotten a better performance in the past if the members of the Board had all stood on an equal footing with respect to one another.

Senator GLASS. I think the doctor misused the term there and said "Federal Reserve bank", instead of "Federal Reserve Board."

Senator MCADOO. You do not want the chief executive officer of the Federal Reserve banks to be given the title of "governor?"

Mr. MILLER. I have no objection to that.

Senator GLASS. What he means is that instead of having a governor of the Federal Reserve Board, the Board would be denominated as "a board of governors."

Mr. MILLER. Yes.

Senator MCADOO. I understand that; but I wanted to know whether, if that suggestion were adopted, you would exclude the use of the word "governor" for Federal Reserve banks.

Mr. MILLER. No, sir.

Senator MCADOO. I myself would want to do that, because it would avoid confusion.

Mr. MILLER. I had in mind drawing a distinction between the governor of a Federal Reserve bank and the governors of the Federal Reserve System.

Senator MCADOO. But that is confusing in the public mind. It is not so material, however.

Mr. MILLER. They have by usage the title of "governor." I see no objection to letting it go on. They will be called that. That is an immaterial point, from my point of view. I think the main thing is that you will build up the quality of independence in the Board and give it a more assured position for the exercise of its responsibilities if it be restated as a Board of Governors, electing its own chairman.

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I do not want to delay too much, but I do want to say just briefly that in the most serious issue in which the Federal Reserve Board was ever involved—the one to which you referred, Mr. Chairman—the Board found itself in the anomalous position that a majority of the Board were thoroughly convinced and of one mind with respect to the policy sought to be pursued, but their effectiveness was largely nullified by the fact that the Governor was not in step with his Board. He tried to do his best to implement the policy of the majority of the Board in which he did not believe. The Secretary of the Treasury was not in step with it, and in large part that policy failed of its full effectiveness and failed of an earlier adoption because of that. I have no question that if the Board had been in position then——

Senator McAdoo. What time are you referring to?

Mr. Miller. 1928 and 1929, notably 1929, right at the very moment when the episode occurred that Senator Glass has referred to. I was a member of the Board and was invited by a group of men to come up to New York and sit with some of the recalcitrants and was even promised that if I would they would come into agreement with the Board. I said, "That is not my business, that is the Governor's business."

Let me call attention in this connection to a fact or two. The Federal Reserve System has been in existence 21 years. In that time it has had seven governors—a startling rate of turn-over for a board charged with the vast responsibilities of the Federal Reserve Board. It is an average service of 3 years, despite the fact that among them was one Governor who served a term of 6 years.

It is not part of my purpose to suggest, nor do I regard it as proper except by way of just asking you to use your imaginations and guess a little why the office of Governor of the Federal Reserve Board is not conducive to longevity. Governors do not last long.

I also call attention to the fact that in that period of time the total number of appointive members of the Board has been 21, with only 4 that were ever reappointed. That is not conducive to independence. In my judgment, the membership has got to be made more attractive to a man who assumes membership in the spirit of accepting a great responsibility and who wants to dedicate his efforts to it and not be interfered with in the discharge of that responsibility.

So much, then, for building up the independence of the Board; and I repeat once more, before I leave it——

Senator McAdoo (interposing). Do you suggest the number who should compose the Board?

Mr. Miller. I do.

Senator McAoo. If you exclude the two ex officio members, that would reduce it to six.

Mr. Miller. I wanted to add this with respect to the Comptroller of the Currency, if I can do it without diverting our attention. I do not doubt—in fact, I expect that it is only a question of time when there will be a consolidation under some organization here in Washington, either the Federal Reserve Board or, if the Federal Reserve Board is put out of business, a successor organization under its general administration. That means particularly the office of the Comptroller of the Currency and, possibly, the F. D. I. C. I think it is

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doubtful and idle and premature to talk of unification of banking in this country until we have unified the agencies of administration that relate to banking, here in the Federal Government. I have become so thoroughly convinced of that that I know it must come. It is merely a question of time when it does come; and as chairman of the ground or site committee of the Federal Reserve Board I have tried to look ahead as well as I could and get ample space so that when that took place an additional building could be built near the Federal Reserve Board building in which these affiliated departments could be housed.

Senator McAdoo. Assuming such a consolidation of its activities—and I do not think the suggestion is without merit—what number would you have the Board?

Mr. Miller. I would suggest either seven or five. I am inclined to think that seven is none too large a number for a board that is going to deal with the problems that the Federal Reserve Board will have to deal with under this grant of powers. I think seven is none too large. I think that was the number on the original board, with two ex officio members—though I recognize that five also has a great deal to be said for it. If the board is experienced and well qualified for its job, five is a better number than seven. However, that is a thing upon which you men are more competent judges than I am.

I would be perfectly content, until consolidation takes place of these various banking and administrative agencies, to have the Comptroller continued on the Board, particularly as the present Comptroller has been deeply interested in Federal Reserve matters. He does not frequently attend the meetings, but he does attend, and whenever he does he has something helpful to suggest, and he has been cooperative to a remarkable degree. So that, while I think in principle, the Comptroller of the Currency should be eliminated, I do not see that there needs to be any haste, in view of my confident feeling that it is only a question of time when you are going to consolidate these various banking agencies under one supreme supervisory authority.

Now, with that out of the mind, here is what I propose by way of amendment to the open-market provisions of the Federal Reserve Act. I propose leaving the first two paragraphs of section 12 (a) exactly as they read now. I think that is essential. I think it is fair and reasonable that every section of this country in so vital a matter should, through its representative, have a voice in the determination of open-market policy. I object in toto to the narrow concentration of authority proposed in the Senate bill. I assume that the objections are so patent that no time need be spent by me in stating the objections to it. That is the form in which the open-market committee is reduced to a committee of 5, with only 3 Reserve Board members and 2 Reserve bank governors. From my point of view, there is nothing to be said in favor of it and only too much to be said against it. If we have in mind, that we keep the membership of the open-market committee as it is at present—12, one for each Reserve district—I would proceed to redefine the objective and also the procedures with respect to the authority of the Federal Reserve Board.

The objective I would redefine following the language of the existing act as closely as possible, but with certain differences, as follows [reading]:

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(c) The time, character, and volume of all open-market operations of the Federal Reserve System under section 14 of this act shall be governed with a view to supporting and reenforcing the credit and discount policies of the Federal Reserve System, when this may be necessary, in order to aid in the establishment and maintenance of sound banking, credit, financial, and economic conditions.

In other words, the open-market policy becomes a supplement to the credit and discount policy to be exercised as a method and a more effective method, something more in the nature of, we will say, surgical intervention, " in order to aid in the establishment and maintenance of sound banking, credit, financial, and economic conditions."

In my judgment, gentlemen, that is as far as you ought to go and as far, I think, as you can safely go in writing a formula into the Federal Reserve Act.

Senator Glass. From what are you reading now?

Mr. Miller. The amendment that I propose. Presently I shall come to the objective set up in the House bill; but what I have just read, to my mind, covers every reasonable requirement and carries in it a suggestion of the exercise of discrimination in the discharge of responsibility.

With reference to paragraph (d), this is what I propose as an amendment [reading]:

(d) In accordance with procedure prescribed by regulations of the Federal Reserve Board, the Committee shall from time to time consider, adopt, and transmit to the Federal Reserve Board resolutions recommending the policies which, in the judgment of the committee, should be adopted with respect to the open-market operations of the Federal Reserve System and stating the reasons for such recommendations. Such resolutions shall be subject to review, modification, and determination by the Federal Reserve Board and, if approved by the Federal Reserve Board, shall become binding upon all of the Federal Reserve banks, subject to such modifications as may be ordered by the Federal Reserve Board.

Senator McAdoo. Where do you refer to the power of initiation?

Mr. Miller. That is coming [reading further]:

The Federal Reserve Board, upon its own initiative and upon the affirmative vote of not less than four of its appointive members, may from time to time, on its own initiative, prescribe open-market policies for the Federal Reserve System.

Senator Glass. What reservation is there in the existing statute, except that any Federal Reserve bank not desiring to participate in a given open-market transaction may decline to do it?

Mr. Miller. What reservation as compared with this?

Senator Glass. I say, what reservation is there in the existing act as to that?

Mr. Miller. The Board, under the existing act, Senator, simply has power to approve or disapprove the recommendations of the Federal open-market committee.

Senator Glass. The open-market committee, on the contrary, Doctor, as you will recall upon thought, under existing legislation cannot engage in any open-market operations except under rules and regulations established by the Federal Reserve Board.

Mr. Miller. Yes.

Senator Glass. The only reservation at all being that any Federal Reserve bank which does not desire to participate in a given open-market transaction may, upon written objections, be excused.

Mr. Miller. Yes.

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Senator McAdoo. There is no power of initiation on the part of the Federal Reserve Board.

Senator Glass. No; I am talking about the existing act.

Senator McAdoo. That is what I say.

Senator Glass. Under the existing act the only reservation is the one that I have mentioned.

Senator McAdoo. Yes; but I mean there is no power of initiation.

Senator Glass Oh, no.

Mr. Miller. There is no power of initiation, and it is not clear that the Board has the right to say more than "yes" or "no" to proposals submitted to it by the Federal Open-Market Committee.

Senator Glass. The act textually says that the open market committee may engage in open-market transactions only upon rules and regulations adopted by the Federal Reserve Board.

Mr. Miller. Yes; but we have never construed, and I question whether it would be proper to construe it, and we have been advised that it would not be proper to construe it, that the power to make rules and regulations gives us power to annex authority not conferred by the act. We can regulate the manner, but we cannot say to them, "You shall not buy $500,000,000; you shall buy $200,000,000 or $700,000,000."

Senator Glass. No; that would be the initiation that you are advocating now.

Mr. Miller. I question whether we have the right to modify their recommendation. We have done it and they have resisted it at times. At the present time they do not resist so much.

Senator McAdoo. I do not think the Board by regulation, for instance, could alter their decisions, their open market committee decisions.

Senator Glass. They may only make decisions under rules and regulations adopted by the Federal Reserve Board.

Senator McAdoo. You are quite right about that, Senator. They can prescribe the method or manner of procedure by the open-market committee. I do not think the Board has any power to alter the method or decision of the open-market committee when it has acted within the rules of procedure prescribed by the Board.

Senator Glass. Of course not, when it has acted within the rules prescribed by the Federal Reserve Board. The Board cannot alter its decisions.

Senator McAdoo. Precisely.

Senator Glass. The only reservation that the Federal Reserve Bank has under existing law is to decline to participate in a given open-market transaction. In other words, if the Federal Reserve Bank of Atlanta or the Federal Reserve Bank of Minneapolis or the Federal Reserve Bank of Dallas, for example, mentioning some of the weaker Federal Reserve banks——

Mr. Miller. The smaller ones.

Senator Glass (continuing). Should in its wisdom determine that it is not able or that it would be distinctly to its disadvantage to participate in an open-market transaction initiated by the Federal Reserve Banks of New York, Chicago, and Philadelphia, it may decline to do so upon 30 days' written notice if at all.

Senator McAdoo. I am inclined to think as I consider this question—it is rather a new problem in my mind—that the point you make

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might be safeguarded if the power of initiation were given to the Federal Reserve Board, the powers that Dr. Miller suggested, by giving the Board power to excuse any Federal Reserve bank from participating.

Senator GLASS. You can do that at any time.

Senator McADOO. But I mean, you can expressly provide that the Board can excuse any particular bank or banks from participating if, in the opinion of the Board, it is advisable to do so. I think you could safeguard the position of those banks in that way.

Senator GLASS. Under existing law, by a very simple amendment which could be made—not according to Dr. Miller's idea, but according to my own—it could be adjusted by providing that any Federal Reserve bank may be excused from participating in an open-market operation by a vote of either a majority or two-thirds of the open-market committee.

Senator McADOO. Some safeguard like that might cover it; but what I think is quite important is that the power of initiation shall be lodged somewhere to excuse any bank from participating where upon a showing it seems wise that it should not be required to do so.

Mr. MILLER. It is done, as a matter of fact.

Senator McADOO. It is permissively done now, but you would like to have the authority, would you not?

Mr. MILLER. It is done as a matter of just sensible administration.

Senator GLASS. Yes; but administration is not always sensible. I can recall governors of your Board that were not sensible. They seemed to be ignorant of the banking business.

Senator McADOO. I agree with the chairman about that.

Mr. MILLER. What I want to call attention to in that connection, Senator, is with respect to Federal Reserve banks. Under the present set-up, an individual Reserve bank has the power not to participate, and there is a question as to how far it should participate in a transaction in which it is invited to participate as a result of the deliberations of the open market committee and the procedure of the Federal Reserve Board. But there is a grave legal question as to what power the Board has and what control in the saying of yes or no as to a matter that is submitted to the banks.

Senator GLASS. I do not see why that should be so, except—with apologies to all of you lawyers—that lawyers raise all sorts of questions that are in contravention of the plain language of the statute.

Mr. MILLER. For instance, Senator, I think it is clear that under the Federal Reserve Act as it is the Board has no legal authority to order a sale.

Senator GLASS. No. It was not intended that it should have.

Mr. MILLER. It ought to have the power, however, to modify an order.

Senator GLASS. It would have the power to adopt a rule and regulation, for example, that the Open Market Committee shall not engage in a transaction involving a given maximum amount, without the approval of the Board.

Mr. MILLER. I think the more important decisions that are made by the Open Market Committee, or the more important decisions of inaction, abstention from action, have got to be taken upon pretty broad grounds, a pretty wide survey of what is impending in the

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country at large. You cannot bottle up the effect of an open-market operation in the district in which it originates. There is no method of doing that——

Senator GLASS. I do not agree with that proposition at all. Nobody has ever been able to convince me that local transactions, for example, in the Dallas Federal Reserve District, have any effect whatsoever upon the financial transactions in the great monetary centers.

Mr. MILLER. Would you say that in the reverse, that a transaction that takes place in the great monetary centers, New York and Chicago, has no effect in Dallas?

Senator GLASS. Very little——

Mr. MILLER. Oh, yes.

Senator GLASS. Let me finish my remark. I say, very little under the general ordinary loans to the mercantile, industrial, and agricultural interests of that district; because I know perfectly well, and I have had it verified over and over again, that banks in a given district have their standard rate of discount which is always the limit of the statutory rate, and that they never depart from it except maybe in the case of a big privileged borrower.

Mr. MILLER. It may not, Senator, have any effect in many cases upon the rate of interest, but it will have an effect upon the ease with which you can get accommodation. Easy money in this country has had a far more sinister effect than cheap money.

Senator GLASS. Oh, yes.

Senator MCADOO. It may have a beneficial effect also?

Mr. MILLER. Yes; it all depends upon conditions, of course.

Senator GLASS. When the New York bank reduced its rate to the ridiculous figure of 1 percent, as it has done, or 1½ percent as it frequently has been, of course that momentarily enabled a big borrower in the Dallas district or the Minneapolis district to get accommodation at a better rate of interest than he otherwise would get.

Mr. MILLER. Yes; and he is very apt to be a speculative borrower, whose operations, Senator, will have distinct repercussions in the field of commerce and business.

Senator GLASS. But I am referring to the current general discount rate and the mercantile, industrial and agricultural interests of the country. They have a standard rate and they never depart from it, and it is always right up to the limit of the statutory rate.

Mr. MILLER. That is true and, I think, substantially true in considerable areas of the country. It is not true with respect to the bulk of borrowings.

Senator GLASS. I am going to stop arguing, because I am going to do my arguing on the floor of the Senate.

Mr. MILLER. I want to convince you of this, Senator. That is particularly what I am up here for. I want you to appreciate that I am speaking out of the depths of experience, and nobody is more profoundly concerned to protect and to defend the Federal Reserve System and the country from bad operations of the Federal Reserve System than I am.

Senator GLASS. Nobody knows that better than I do.

Mr. MILLER. I would not be proposing this if I did not think so; and I would not propose it under any conditions if I did not couple

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it with safeguards that I think will protect it and result in the country getting a very distinct benefit from it.

Senator McAdoo. It seems to me, Doctor, in discussing this particular question, and while the chairman's view about the local transactions is entirely sound and I agree with him about that, there are broad questions of national policy affecting credit throughout the country for which perhaps more adequate provision, regulatory or otherwise, should be provided in this new law. Open-market operations do affect the credit and financial structure throughout the entire Nation. Of course, they are felt less in one district than in another.

Mr. Miller. Less immediately.

Senator McAdoo. Yes; but they have repercussions.

Mr. Miller. Oh, they do; you are perfectly right about that.

Senator Glass. One of those policies involved the repudiation by the National Government, through congressional action, of its most sacred contract, characterized by the Supreme Court as "repudiation" and a "cheat." That is what it was, too.

Senator McAdoo. We are trying to avoid that the next time.

Senator Glass. Doctor, how much longer do you think you will require?

Mr. Miller. At the rate at which we are going we are not making progress very rapidly.

Senator Glass. Go ahead a while longer, anyhow.

Mr. Miller. All right, Senator. I just want to call attention, in connection with open-market operations, to a episode that may not be without interest. You referred to the episode of March 26 or 27, 1929. Do you know what precipitated that? The withdrawal of $50,000,000 from the market in Chicago by one of the largest banks there that had decided that it would cooperate in supporting the Board's program of getting control through direct pressure on speculative loans. It called $50,000,000 loans in the Chicago market, with the result that the pressure in New York was so immediate, so intense, that it brought on something in the way of a very considerable panic. That was what occasioned the intervention in the market of the gentleman who has been referred to.

Senator Glass. I agree that transactions in the largest metropolitan city have a repercussion in the second largest city.

Mr. Miller. They do, Senator. When money is active, there is an active market for what are called Federal funds.

Senator Glass. But that is no reason why you should strip all of the Federal Reserve banks completely of their jurisdiction and their judgments upon credits.

Mr. Miller. I have had all of that in mind. Let me call your attention again to the open-market formula that I have proposed here. It shall be "governed with a view to supporting and reinforcing the credit and discount policies of the Federal Reserve System."

These policies are made by the banks as well as the Board, "when this may be necessary, in order to aid in the establishment and maintenance of sound banking, credit, financial, and economic conditions."

As a matter of fact, I regard that as a pretty considerable limitation upon any careless or extravagant exercise of these powers when conditions do not clearly indicate them.

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Senator GLASS. Just exactly what is the difference between that and what the House has put into the bill?

Mr. MILLER. I want to come to that. There is an awful lot of difference. That is an excursion into Martian economics, lunar economics. This is an excursion into simple, common experience. That implies a world that is to be made over through the operation of the monetary mechanism of the country that, in my judgment, is just not attainable, and I think that should it be attained it would inevitably mean the destruction of the Federal Reserve System. But I shall have something to say about that later.

I propose a further paragraph [reading]:

(e) Each Federal Reserve bank shall purchase or sell obligations of the United States, bankers' acceptances, bills of exchange, and other obligations of the kinds and maturities made eligible for purchase under the provisions of section 14 of this act, to such extent and in such manner as may be required by the Federal Reserve Board in order to effectuate the open-market policies approved or prescribed by the Federal Reserve Board under the provisions of this section and each Federal Reserve bank shall cooperate fully, in every way, in making such policies effective.

And [reading further]:

(f) All actions taken by the Federal Reserve Board with respect to open-market policies shall be clearly recorded, together with a statement of the reasons therefor; and, if any member of the Board vote against such actions, such vote, together with any reasons therefor, shall also be recorded. In its annual report for each year the Federal Reserve Board shall publish in full all resolutions recommending open-market policies and stating the reasons therefor which were adopted by the Federal Open Market Committee during the year covered by such annual report, together with the full text of the contemporaneous record of all actions taken by the Board with respect to open-market operations and the reasons therefor and all dissenting votes and the reasons therefor.

I regard that as perhaps one of the most valuable and considerable limitations upon any careless exercise of the authority that I am asking that you give to a board that is made independent.

Senator GLASS. And only if it is made independent?

Mr. MILLER. Only. I stand by that to the bitter end. I do not want to see these powers given in any way that will lead to careless, hasty decisions or to any unintelligent or improper use. I think that is a very important safeguard.

You are a Virginian, Senator, and I want to recall to you what you already know but may not have in your mind at this moment—a remark made by a great Virginian of an earlier age, James Madison, in the debates on the establishment of the Treasury Department.

Senator GLASS. He is alleged to have written the Constitution that we once had.

Mr. MILLER. Correct—well, I think we still have it; but it is like the skin on a boy's body; it has got to grow as the boy grows.

A question was raised as to the nature of the safeguards that could be set up to insure that the Secretary of the Treasury would properly discharge his responsibility. I have never forgotten Madison's reply. He went through a number of things, and finally he came to this and said:

Finally, reputation. There is no species of property for which men have a more jealous regard than their good reputations.

I think that is one of the things that you men must rely upon in this act.

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I am not going to get through this morning, Mr. Chairman.

Senator TOWNSEND. Are you going to meet this afternoon?

Senator GLASS. I think it is a vital requirement that we hear such testimony as Dr. Miller is giving and as others have given and as others desire to give; but I am being pressed by the chairman of the committee to cut the hearings short and to report the bill.

Senator TOWNSEND. I do not think we can afford to cut Dr. Miller short in the midst of his testimony.

Senator GLASS. No; I do not want to. I want to hear all he has to say, and some other members of the Board also.

Can you come back at 2 o'clock, Dr. Miller?

Mr. MILLER. Any hour you suggest, Mr. Chairman.

Senator GLASS. Two o'clock?

Mr. MILLER. Yes.

Senator GLASS. Shall we meet here or over in the room of the Appropriations Committee?

Senator TOWNSEND. In the Appropriations Committee room, I would think.

Senator BULKLEY. Yes; I would rather meet over there.

Senator GLASS. Come back, then, please, at 2 o'clock in the Appropriations Committee room.

(Whereupon, at 12:20 p. m., a recess was taken until 2 p. m., to meet in the committee room of the Senate Committee on Appropriations in the Capitol.)

AFTER RECESS

The subcommittee resumed at 2 p. m., in the Capitol, on the expiration of the recess.

Senator GLASS (chairman of the subcommittee). We will resume. You may go ahead with your statement, Dr. Miller.

STATEMENT OF ADOLPH C. MILLER, MEMBER OF THE FEDERAL RESERVE BOARD, WASHINGTON, D. C.—Resumed

Mr. MILLER. The first thing I will take up this afternoon are those provisions of the Senate bill and of the House bill that contemplate a change in the status of the chairmanship and the governorship of Federal Reserve banks by consolidating the two. In other words, abolishing the separate position of chairmanship and combining it with the office of governor. And, likewise, certain changes in the tenure of office of various class C directors of Federal Reserve banks.

Senator GLASS. I would be obliged if you would furnish me with a copy of these proposed amendments.

Mr. MILLER. I will do so. What I now hand you is in the shape of an amendment to H. R. 5357 and S. 1715. Strike out everything commencing with line 19, on page 38 (S. 1715), through and including line 22, on page 40, and substitute the following:

Class C directors shall be appointed by the Federal Reserve Board, and one of them shall be designated by the Federal Reserve Board as chairman of the board of directors. The chairman shall be the highest official of the bank, shall preside at all meetings of the board of directors at which he is present, and may, at his discretion, exercise supervision over the bank and its officers.

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He shall be a man of outstanding and tested character and experience and shall be eminently qualified to give effective representation to the point of view of the public interest in all matters pertaining to the policies and operations of the Federal Reserve bank and shall consult with and be consulted by the Federal Reserve Board from time to time respecting such matters. He shall receive an annual compensation to be fixed by the Federal Reserve Board and paid monthly by the Federal Reserve bank to which he is designated. One of the directors of class C shall be appointed by the Federal Reserve Board as deputy chairman and shall preside at meetings of the board of directors in the absence of the chairman. In the absence of both the chairman and the deputy chairman the third class C director shall preside at meetings of the board of directors.

The last few lines read:

At each Federal Reserve bank there shall be a governor, who shall be the active executive officer of the bank.

He is described in the House bill as the "chief" executive officer [reading]:

The governor shall be appointed by the board of directors. He may be appointed by the Federal Reserve Board as one of the class C directors of the bank—

Instead of making it obligatory this would make it optional with the Board. [Continues reading:]

but, in such event, his term of office as class C director shall terminate when he ceases to be governor of the bank. For each Federal Reserve bank there shall be appointed annually, in the same manner as the governor, a vice governor, who shall, in the absence or disability of the governor, or during any vacancy in the office of governor, serve as the active executive officer of the bank. Whenever a vacancy shall occur in the office of either the governor or vice governor of a Federal Reserve bank, it shall be filled in the manner provided for original appointments; and the person so appointed shall hold office until the expiration of the term of his predecessor.

Effective ninety days after the enactment of the Act containing this amendment, the office of Federal Reserve agent shall be abolished and the terms of office of the present incumbents of the position as class C directors and chairmen of the boards of directors shall terminate; but they shall be eligible for reappointment, in the discretion of the Federal Reserve Board, as class C directors and chairmen. Hereafter the duties prescribed by law for the Federal Reserve agent shall be performed by such person or persons as the Federal Reserve Board shall designate.

No class A director shall serve continuously for more than one full term of three years, except that a class A director elected to fill an unexpired term may be reelected and may serve for the next full term. No class B director shall serve continuously for more than two consecutive full terms of three years each, except that a class B director elected to fill an unexpired term may be elected to serve the next two full terms of three years each.

The present bill provides that no director shall serve for more than 6 years.

Senator GLASS. And you provide that they shall serve how long?

Mr. MILLER. I recommend that the bank directors be permitted to serve only a single term of 3 years. That is in vogue in two Federal Reserve banks now, and it works well.

Senator GLASS. Suppose we were to enact a law that no Member of the House of Representatives should serve more than one term; what sort of legislation do you think we would have?

Mr. MILLER. Well, of course, this is not a legislative body. This is an operating, or, at the most, an administrative, body, and——

Senator GLASS (interposing). That is true; but I have heard it said repeatedly by members of various Federal Reserve bank boards that it takes a year for a member to know what it is all about.

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Mr. MILLER. That is true. That is the reason why, in contradistinction to the Senate bill and the bill as passed by the House, I have removed the restriction of 6 years upon class C directors. I look at the thing in this way: We do not want a specific banking influence to overawe the operations and decisions of Federal Reserve banks. That has been one of the troubles in the case of certain Federal Reserve banks. That was undoubtedly true of the Chicago district, where continuously from the inception of the System until, I think, 1931 the leading influence in that bank was the president of the largest bank in the city of Chicago, a class A director.

Senator GLASS. Was that George M. Reynolds?

Mr. MILLER. Yes; and that is not the only instance, but it is the most outstanding one.

Senator GLASS. Well, it is quite exceptional, is it not?

Mr. MILLER. It is not exceptional. There are many cases, but I think that one is exceptional, perhaps, in this way——

Senator GLASS (interposing). Exceptional does not always mean exclusive, but it is not the general practice, is it?

Mr. MILLER. It is not the general thing; no. But I think the position that was taken by the New York member banks at the inception of the Federal Reserve System that there should not be anything in the nature of perpetuity of control, or even a semblance of it, and that therefore there should be a change every 3 years, was and has been a very beneficial thing in the organization of that bank. And my recollection is that from the beginning of the System, or very soon thereafter, the Atlanta bank adopted the same system, and it has worked there well, very well; and I think we feel it in visiting those boards of directors when they are in session. You will see a notable difference in those banks where there has been a long continuance in the position of director by a leading banker of the district, who rather overawes the others. It may not be that he dominates the bank in any conscious way, but the other members show a tendency to defer to him on banking matters, and on matters that are not banking matters but which they think are banking matters, because he has positive views. So that I think that is a good restriction.

Now, when it comes to class B directors, I would not object to a longer term of service. It takes a good 3 years before a good class B director gets fairly oriented and is willing to speak up at meetings and take a position. And certainly he should be given a term of not less than 6 years. The advantage of giving a longer term to my mind would be this: I feel it most important that the class C directors should be the weightest and best men you can possibly get. I would put no restriction upon the length of their term of service. I would leave that to the discretion of the Board.

While it is true that some men have been continued in office in that position beyond what is altogether desirable, I think in view of the great responsibility that the Board is going to have under this act that that need not be feared for the future.

Now, in getting good class B directors, and particularly if you should feel disposed to let their term of service run to at least 9 years, the Board has the opportunity as a vacancy does occur in class C of directorships, or if it wants to make a change, to do so.

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And if there is a well-qualified and experienced man among the class B or business directors of a bank, whether he is a merchant, a farmer, or a manufacturer, they can pick that man.

Senator GLASS. And transfer him to a class C directorate, do you mean?

Mr. MILLER. Yes. That is what we did with Owen D. Young. He began as an elected director and then was selected by the Board as a class C director. If I had thought of it I would have brought down here this afternoon and introduced into your record a letter that Mr. Young wrote to the Board at that time, but the purport of it was that as a class C director he said he would feel an even greater sense of responsibility for the welfare of the bank than as an elected class B director, representing more or less the member banks.

I think in that way though the directors appointed by the Federal Reserve Board would be a minority in number, they would be a very strong influence, perhaps a dominating influence, as regards all of the weightier matters concerning the broader field of policy and the general public relations of their respective institutions. I advocate that, therefore, very strongly; and hope that as the legislation emerges there will be no restriction put upon the service of class C directors. We have had some men that under the operation of the law I think would have meant a very, very grievous loss to the Federal Reserve System if that were so. I know there are boards here in Washington, and I know there have been members on the Federal Reserve Board, that have felt it is desirable not to have strong men on Federal Reserve banks. But I feel the other way. I feel it is desirable to have very able men there, men who can put the Board on its mettle. None of our problems are 100 percent clear of solution or simple, and through contact and discussions I believe eventually will come sound determinations, as sound as you can expect to get from fallible human beings.

Now, as to the chairmanship: I think it is most important that the position should be kept alive, only however as chairman. Pursuing the thought a little bit further here is what I would say: That as men moved upward from the position of class B directors, supposing that you fill the class C directors from men who distinguished themselves as class B directors, I feel that there should be designated as chairman of the board of a bank a man of ripe experience, a man of wisdom, a man who is familiar with the problems, who knows his way around, and generally speaking that involves in my judgment a man of very much bigger mental caliber, and certainly of bigger stature as a man, than you can ordinarily expect to command for the position of active executive officer of a Reserve bank. I think his presence merely at directors' meetings, sitting at the head of the table, would do an immense deal to give elevation of thought and purpose and spirit to the meetings of boards of directors of Reserve banks.

I think there are in this country, in every district, men in the business world, men who have built up and developed great organizations and who have done it honorably as well as honestly, who have some sense of social obligation, who have something of the outlook of the man animated by a sense of public responsibility and of honesty, who can be found to be put in the chair of each

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of the Federal Reserve banks. I should like to see those men in the chair, and I think it would be one of the best guarantees we could possibly get for a better, broader, more publicly inspired administration of the banks.

Let me tell you here just a little instance and you can judge whether you want it on your record or not. There occurred a vacancy in the Buffalo Reserve Bank last winter. I happened to be on the New York committee, and in casting about for a man to fill the vacancy I came upon the name of Chief Judge Pound, who was just retiring from the New York Court of Appeals. I was satisfied that if that man were available, although he was not technically a banker, he would make a most admirable man to introduce into the bank at Buffalo, with a view to bringing him down on the board of the Federal Reserve Bank of New York when and if a vacancy should occur. I felt that a man of his distinction, wide experience, and outlook would be an admirable counterpoint to any petty or narrow banking point of view who would activate the meetings merely by his presence whether he said very much or very little or spoke only at times. I am reminded that the Federal Reserve institution, though not governmental, is vested with a type of serious public interest, and I should like to see that done.

They used to use the expression, in the case of the Bank of England, " passing the chair ", when men would gradually come along through experience and had qualified and made good would eventually occupy the chair of Governor of the Bank of England. I think a large part of the success of the Bank of England was due to that. It is a remarkable fact that ought never to be lost sight of, particularly in America at this juncture, though that institution is as private as the law could make an institution private, it has for at least three-quarters of a century been animated by perhaps the most vivid sense of public responsibility of any institution in the world, I do not care whether the institution is governmental or whether it is nongovernmental. It has been an institution of national service, operated and governed by men who are keenly alive to the importance of their powers and responsibilities and who are to be largely credited with the magnificent performance that Great Britain, and particularly the London financial market, has given all through a period of at least three-quarters of a century.

I see no reason why we should not undertake to open a path by which we can gradually emerge toward that goal in this country. My suggestion therefore is that this position of chairman be consecrated to that type of service now. I would have in mind in this thought that such chairman should be in no sense a functionary of the bank. He could be a man in active business life. He should have no routine functions. I have stated here " a compensation ", and what I have in mind is rather an honorarium, something or perhaps nothing. I think the men of the kind you want would feel themselves only too happy and greatly honored to be invited to step into a position of that kind of public responsibility even though they held no appointment technically governmental in its character. I think that at conferences with the Federal Reserve Board, and its conferences with them, they would be most helpful in every way, and that the public relations of the Federal Reserve banks in the several

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districts, as well as in the country as a whole, would be vastly improved.

Now, Mr. Chairman, are there any questions on that?

Senator GLASS. Dr. Miller, I think you have gotten to be right much of an idealist.

Mr. MILLER. You think I have?

Senator GLASS. I think you will experience a great deal of difficulty in finding men of that sort who would serve without compensation. But you may go ahead with your statement.

Mr. MILLER. Well, they have had that sort of men in some other countries, why not here?

Senator GLASS. Well, never mind. We will talk about it behind the bat.

Mr. MILLER. I will be glad——

Senator COUZENS (interposing). Let us go on with your next suggestion.

Mr. MILLER. The provision for compensation is there, and my thought is that it should not be made an inducement. I think you will find, gentlemen of the committee, that its occupant in time, and in no very long period of time, will come to consider it one of the greatest honors to be sought by American business men of distinction. There are in the circle of men I know or know of, a great many unassuming men but men of ability and broad experience whom I think could be induced to take a position of this kind and who would discharge the responsibilities splendidly, eminently, because they would feel it was an honor and something in the nature of a very much coveted recognition would develop out of it.

Senator GLASS. All right. Let us go on to the next proposition that you have to present.

Mr. MILLER. Now, I come to the proposition of the House bill, which is paragraph (b) of section 204, which reads as follows:

> It shall be the duty of the Federal Reserve Board to exercise such powers as it possesses in such manner as to promote conditions conducive to business stability and to mitigate by its influence unstabilizing fluctuations in the general level of production, trade, prices, and employment, so far as may be possible within the scope of monetary action and credit administration.

Senator COUZENS (interposing). Well, do you approve of it or do you not approve of it?

Mr. MILLER. I disapprove of it.

Senator GLASS. Well, you need not discuss it.

Mr. MILLER. All right.

Senator COUZENS. Are you going to offer a substitute?

Mr. MILLER. Well, I have already, but I have also prepared a substitute method of handling what I conceive to be the problem here in event that there was any likelihood of that objective being written into the Federal Reserve Act.

Senator GLASS. I do not think there is any. But if you have an amendment and will hand it in we will avail ourselves of it.

Mr. MILLER. I have an amendment here that is pretty completely thought out.

Senator GLASS. If you will let us have it we will take it under consideration.

Mr. MILLER. All right. Here it is.

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(Draft of May 27, 1935)

FEDERAL ADVISORY COMMITTEE

For the purpose of aiding in the establishment and maintenance of more stable economic conditions in the United States, there is hereby created a Federal Advisory Committee (hereinafter referred to in this section as "the Committee"), which shall consist of five members appointed by the President of the United States by and with the advice and consent of the Senate. The members of the Committee shall be chosen with particular regard for their qualifications for the discharge of the duties imposed upon them by this Act. Not more than two members of the Federal Reserve Board may serve at the same time as members of the Committee.

For the purpose of assisting the President in the selection of the members of the Committee, two lists of persons eminently qualified for membership thereon shall be prepared and submitted to the Federal Reserve Board on or before October 1, 1935. Each list shall include the names of not less than five nor more than fifteen persons and shall be accompanied by a memorandum stating the qualifications of each such person. One list shall be prepared and submitted by the American Economic Association and one by the twelve Federal Reserve banks, in accordance with procedure to be prescribed by the Federal Reserve Board.

After careful consideration and such investigation as it deems necessary, the Federal Reserve Board shall transmit such lists to the President, shall advise the President which persons among those named in such lists are, in the Board's judgment, best qualified for membership on the Committee, and shall add thereto any nominations of its own selection. In selecting the members of the Committee, the President shall give due consideration to such lists, the additional nominations submitted by the Federal Reserve Board, and the Board's views thereon, but shall not be required to select the members of the Committee from such lists or nominees.

Similar lists shall be prepared and submitted to the President in like manner and with like effect whenever any vacancy occurs or is about to occur in the membership of the Committee.

Of the five original members of the Committee, one shall be appointed for a term of two years, one for a term of four years, one for a term of six years, one for a term of eight years, and one for a term of ten years, and their successors shall be appointed for terms of 10 years each, except that a person appointed to fill a vacancy created otherwise than by the expiration of the term of a member shall serve for the unexpired term of his predecessor.

The members of the Committee (other than those who are at the same time members of the Federal Reserve Board) shall devote their entire time to the business of the Committee and shall receive salaries of $12,000 per annum, payable monthly, together with actual necessary traveling expenses, which salaries and expenses, together with all other expenses of the Committee, shall be paid by the Federal Reserve Board from the proceeds of assessments levied on the Federal Reserve banks in the manner prescribed by the Federal Reserve Act for defraying the salaries and expenses of the Federal Reserve Board: *Provided*, That the Committee shall annually submit a budget to the Federal Reserve Board, which shall be subject to the Board's approval.

With the consent of the Federal Reserve Board, the committee may utilize the services of members of the Board's staff; and, within the limitations of the budget approved by the Board, the committee shall have authority to employ and fix the compensation of such additional experts, assistants, attorneys, clerks, and other employees as may be deemed necessary to conduct the business of the committee. All salaries and fees of its employees shall be fixed in advance by the committee and shall be paid in the same manner as the salaries of the members of the committee.

Retired appointive members of the Federal Reserve Board may, in their discretion and with the consent of the committee, serve as ex-officio members of the committee, in addition to the five appointive members; but such ex-officio members of the committee shall have no vote and the aggregate amount of their retirement pay, plus any compensation received from the committee, shall not exceed $12,000 per annum.

It shall be the duty of the committee to study (1) economic, industrial, financial, and monetary conditions, the workings of the banking system and the Fed-

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eral Reserve System, the effects of United States Treasury operations, the laws relating to banking, and any other factors which, in its judgment, may affect the stability of general economic conditions, and (2) the methods of aiding in the establishment and securing the maintenance of more stable economic conditions in the United States. The committee shall report its findings from time to time to the Federal Reserve Board.

For the purpose of aiding in the establishment and securing the maintenance of more stable economic conditions, the committee shall also make recommendations to the Federal Reserve Board from time to time with regard to the open-market operations and discount rates of the Federal Reserve banks and the reserves required to be maintained by member banks of the Federal Reserve System. If adopted unanimously by the members of the committee holding office at the time, the Federal Reserve Board shall proceed to put such recommendations into effect, unless they be disapproved unanimously by all members of the Federal Reserve Board holding office at the time.

If the recommendations of the committee be not adopted by unanimous vote, a full statement of the reasons for such recommendations and full statements of the views of the minority members of the committee and the reasons therefor shall be communicated in writing to the Federal Reserve Board. After reviewing such recommendations and the reasons of the majority and minority for and against the same, the Federal Reserve Board shall set a date for a hearing at which the members of the committee shall appear. At such hearing each member of the committee shall be given an opportunity to state fully his reasons for or against the recommendations of the committee and shall answer all questions pertaining thereto propounded by the members of the Federal Reserve Board.

Following such hearing, the Federal Reserve Board shall again review the recommendations of the committee and, within a reasonable time, shall either approve or disapprove the recommendations of the committee, with such modifications as the Board may deem to be in the public interest. If the recommendations of the committee be approved by the Federal Reserve Board, the Federal Reserve Board shall proceed to put them into effect, with such modifications as it deems advisable.

The committee shall not make public any of its recommendations or findings or the results of any of its studies or any other information in its possession; but the Federal Reserve Board shall publish all findings and recommendations of the committee and statements of the Board's actions thereon, in the Board's annual reports to Congress in supplements thereto, or in the Federal Reserve Bulletin.

Upon the completion of the building which the Federal Reserve Board has been authorized to erect for its use, it may assign quarters therein for the use of the committee.

The Federal Reserve Board, the Federal Reserve banks, the Secretary of the Treasury, the Reconstruction Finance Corporation, the Federal Deposit Insurance Corporation, the Comptroller of the Currency, the Commissioner of Internal Revenue, the United States Tariff Commission, the Collector of Customs, and all other officers, employees, departments, bureaus, boards, commissions, independent establishments, and agencies of the United States are authorized and directed to make available to the committee any information in their possession which the committee may require for the performance of its duties under this act.

Well, Senator Glass, that pretty nearly finishes what I have to say.

Senator Glass. This is the amendment, do you mean?

Mr. Miller. This is an alternative solution for the problem that this paragraph which I was just reading to you from the House bill would impose upon the Federal Reserve Board. I do not want that, and if the Congress of the United States proposes to engage in the problem of economic stabilization I have a different solution to offer from that, that would protect an invasion of the Federal Reserve System from any share of responsibility of that kind beyond what is included in the formula I gave to the subcommittee this morning in connection with a revision of section 12a.

Senator Glass. Well, I do not think the Congress is going to do that. But, Dr. Miller, have you discussed the proposition of the pro-

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posed arbitrary right of the Federal Reserve Board to change the reserves whenever and to any extent that it pleases?

Mr. MILLER. No; not specifically, I think; only by a passing reference.

Senator GLASS. All right.

Mr. MILLER. You may recall that in 1916 or 1917 the then Federal Reserve Board prepared and requested that such an amendment to the Federal Reserve Act be passed, to confer upon us that power. I am certain as to the fact and the content, but am a little uncertain as to the date. I am not sure that it was made in 1916, but, at any rate, it had its inception in the Board in 1916.

We had a situation then where gold was coming into this country through vast purchases by the warring governments in Europe, and we felt there was great danger, and subsequent events demonstrated the truth of our fear, that the situation would get out of control. And we knew of no method at that time by which we could probably more effectively counteract it than by being able to raise the reserves.

Now, looking at the situation that will be left when this depression terminates, we will have an enormous amount of redundant money in this country, even supposing that there is no further monetary legislation increasing the already available or potential supply. And I do not think that the two and a half billion dollars of Government bonds that we hold would prove a very available method for counteracting any inflationary influence if and when it develops, and it will develop I do not for one moment doubt in my own mind. It is going to develop, all right. We have outstanding now almost two and a half billion dollars, certainly over $2,300,000,000, of excess reserves that in some way have to be recovered in part when business begins again to get its stride.

Senator GLASS. Well, they are only available for business purposes——

Mr. MILLER (interposing). They are available for——

Senator GLASS (continuing). In response to the demands under the existing law of commerce, industry, and agriculture.

Mr. MILLER. Under the terms of the new Banking Act of 1933 the Board is equipped with powers that it did not realize it had before to restrain the banks from the improper use of Federal Reserve credit used for speculative purposes. It has certain powers as well as responsibilities under the terms of the Securities and Exchange Act as well.

Senator GLASS (interposing). That touches securities on the exchange and not what we speak of as legitimate business.

Mr. MILLER. That is right. Beyond that you do what perhaps ought not to be overlooked, although I had not intended to raise the question in the hearings in which I have participated, of——

Senator GLASS (interposing). I think it is one of the most important, if not of more importance than the open-market question, if the Board here in Washington can do as it pleases with the reserves of the country, differentiating in the case of district from another district, and all that sort of thing. I think that is very important.

Mr. MILLER. Senator Glass, my doubt is whether it will ever be used.

Senator GLASS. Oh! My heavens alive, there has been more of that sort of legislation enacted, such as the N. R. A., the Frazier-Lemke

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Act, and innumerable other things, upon the supposition and in some cases upon the direct assurance that they would not be used, but they have been used and are being used, and misused at that, too.

Mr. MILLER. Well, I would suggest there that I doubt whether in any Federal Reserve set-up of which I have been a member, a power of that kind would be used, if at all, except under the pressure of pretty strong compulsion. I would suggest that it might be covered here again by requiring the affirmative votes of a certain number of members of the Board so as to make a test of the necessity to resort to that rather drastic means of control, to make it clear and beyond a reasonable doubt.

Senator BULKLEY. I should like to ask whether in the form as provided in this bill, and in the bill as it passed the House, you think it might have any effect of disturbing the equinimity of bankers, just to know that there is such a power on the part of the Federal Reserve Board.

Mr. MILLER. It might, but I do not think seriously. Our main difficulty in this country is not that we will restrain but that we will not restrain.

Senator GLASS. It is a power to begin with that would enable the Board to destroy the credits in one Federal Reserve district and expand credits in another.

Mr. MILLER. Well, I would not be at all averse to having it apply uniformly over the whole country if it is to apply at all. On the contrary, I think that would be the more logical way to do it.

Senator BULKLEY. And if a banker were to tell you he would be disturbed by it and would not know exactly what reserves to build up, you just would not believe him; is that it?

Mr. MILLER. It would not disturb me if I was a banker and knowing what I know.

Senator GLASS. But every banker has not your equilibrium. [Laughter.]

Mr. MILLER. It is going to require some compunction and some character, and I should say some courage, to raise the reserves of the banks of this country unless indications point clearly to its necessity. My fear would be that it might encourage the mistake of making the Federal Reserve Board feel that because it has a stick of dynamite it can pull out at any time it would not pull it out until it was too late to do anything with it. I mean that it might create a false sense of security.

Senator GLASS. Well, if that is all, Dr. Miller, we are very greatly indebted to you for your testimony. It has been very enlightening to us.

Mr. MILLER. There is one further thing I want to call your attention to that I have not mentioned so far, and that is the new position that the United States Treasury has in recent years come to assume as a factor in the money market, and that is something beyond anything in extent that we have ever had before. I have just looked up to see what the powers of the Treasury are to increase or decrease member-bank reserves and deposits. Mr. Thomas has made certain computations and assembled certain material for me. In the matter of increasing reserves it has the power now to issue $3,000,000,000 of greenbacks. And it has about 1,800,000,000 of stabilization funds with Reserve banks which it can use——

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Senator GLASS (interposing). Which it took from its owners.

Mr. MILLER. There would be two vast sources of inflation; and when you realize that things are moving in their ordinary way a dollar of reserve money multiplies itself to $10, and you can see what the Treasury could do there, that the Board would be helpless to counteract unless it is given some authority; and I confess that I view the future in that respect with at least perplexity. And it can issue more silver certificates. That again has the same effect as an open-market operation. It could also further devalue the dollar and spend the profits. That again would be an open-market operation. In other words, they have the power to go into the open market to an extent that makes Federal Reserve banks seem like a toy pistol alongside the modern revolving six-shooter.

The Treasury has the power, on the other hand, to decrease member banks' reserves. It can draw down its own balances at commercial banks and transfer the proceeds to Reserve banks.

Senator GLASS. Well, any private depositor has the power to do that.

Mr. MILLER. Except that he cannot deposit it in the Reserve banks?

Senator GLASS. No.

Mr. MILLER. He cannot get rid of it except by moving it out of the country. He can take it out in the form of currency and lock it up or take it out of the country. The Treasury can do the same thing with its trust-fund balances, to the extent that they are carried with member banks. And it can sell securities to the member banks or the public and place the proceeds on deposit with Federal Reserve banks.

These are very extensive monetary powers and could be operated to produce some startling things. Similarly the Treasury could increase the deposits of member banks without the knowledge or cooperation of the Federal Reserve banks, by spending money raised either by sale of securities to member or Reserve banks, by use of stabilization fund, by issue of United States notes, or by printing silver certificates against silver bullion already in the Treasury.

So that you really have two colossal sources of banking power in the United States, one being the Federal Reserve System, and the other being the Treasury.

Senator MCADOO. How was that?

Mr. MILLER. Senator McAdoo, I am explaining the enormous power the Treasury has to operate in the open market now, quite independently from the Reserve banks, and far more than the power that the Reserve banks themselves possess. It constitutes a problem in the future; and to my mind, if you want any realistic argument against this formula in the Federal Reserve Act, you have it there: that they can just pull the ground out from under us.

Senator GLASS. Do you know the origin of that formula?

Mr. MILLER. No.

Senator GLASS. Well, never mind. We will not go into that.

Senator COUZENS. Mr. Chairman, I think last Thursday or Friday Mr. Miller referred to some interference with the Federal Reserve Board, through political officeholders and bankers, and he stated, in response to a query I made to give us some examples, that he would be glad to give it to us in executive session. Now, if Mr. Miller is

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through with his statement for the record, I should like for the subcommittee to go into executive session and let us get some of that information.

Senator GLASS (chairman of the subcommittee). All right. The subcommittee will now resolve itself into executive session. Everybody will retire except the members of the subcommittee and Dr. Miller, and at the conclusion of the executive session we will adjourn until 10:30 tomorrow morning to resume our hearings in room 301 Senate Office Building.

(Thereupon, at 2:55 p. m., the committee went into executive session, and after a short time adjourned to meet at 10:30 a. m. Tuesday, May 28, 1935.)

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BANKING ACT OF 1935

TUESDAY, MAY 28, 1935

United States Senate,
Subcommittee of the Committee on
Banking and Currency,
Washington, D. C.

The subcommittee met, pursuant to adjournment on Monday, May 27, 1935, in room 301, Senate Office Building, Senator Carter Glass presiding.

Present: Senators Glass (chairman of the subcommittee), Bulkley, Byrnes, McAdoo, Townsend, and Couzens.

Present also: Senator Norbeck of South Dakota and Senator Nye of North Dakota.

Senator Glass. The subcommittee will come to order. We will be glad to hear from Mr. Edward Elliott.

STATEMENT OF EDWARD ELLIOTT, VICE PRESIDENT, SECURITY FIRST NATIONAL BANK OF LOS ANGELES, CALIF., REPRESENTING THE BANKERS ASSOCIATION OF SIX STATES, CALIFORNIA, ARIZONA, NEW MEXICO, OREGON, IDAHO, AND UTAH

Senator Glass. Be good enough to give your name and occupation to the official reporter.

Mr. Elliott. My name is Edward Elliott. I am vice president of the Security First National Bank of Los Angeles. I am representing the Bankers Associations of six States, California, Arizona, New Mexico, Oregon, Idaho, and Utah.

In appearing in behalf of the bankers associations of these six States, I beg to say that my representation runs to title I only of the bill, and it is only to title I that I wish to address my remarks. What I shall have to say will be confined to a discussion of section 101 of the House bill, subdivision 8, in which provision is made for the assessment upon banks for the Federal Deposit Insurance Corporation.

Senator Townsend. You are referring to the one-eighth of 1 percent?

Mr. Elliott. Yes, sir.

Senator McAdoo. Have you cited the page and line?

Mr. Elliott. I did not. It is subdivision 8 of section 101 of the House bill, page 11.

In the bill before the Senate and in the bill as it was originally presented to the House, the assessment provided for was one-twelfth of 1 percent upon total deposits with the right on the part of the Federal Deposit Insurance Corporation, under certain circumstances,

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to waive or remit one-half of the assessment. As the bill passed the House the provision was for an assessment of one-eighth of 1 percent of total deposits and the assessment was made mandatory.

The bankers associations of the six States which I represent have, I believe without exception, passed resolutions in opposition to the assessment provided in the House bill. They believe the assessment should not be mandatory and that it should not be an eighth. They believe further that such mandatory assessment of one-eighth is neither necessary from the standpoint of the Corporation nor desirable from the standpoint of sound banking.

Though the system under discussion has been spoken of as an insurance of deposits, and though the Corporation is called the Federal Deposit Insurance Corporation, the contribution to be paid by the banks can hardly be regarded as an insurance premium, as it is not based upon any actuarial figures. At best, any rate suggested may be regarded as an estimate of the amount that the banks can afford to pay. As a matter of fact, the insurance is now and must be for a considerable period of years largely a guarantee on the part of the Government rather than an insurance fund built up by contributions from the banks.

When it was suggested that an assessment of one-eighth of 1 percent of total deposits was not necessary from the standpoint of the Corporation, there was in mind the resources, actual and potential, of the Corporation and the possibility of these resources being sufficient to meet any calls that may reasonably be anticipated will be made upon the Corporation in the next few years.

There has been contributed to the Corporation by the Treasury of the United States and by the Federal Reserve banks approximately $300,000,000 and another $30,000,000 approximately has been contributed by the banks. The bill before you provides that the Corporation shall have the right to issue notes and debentures in an amount three times the sum contributed by the Treasury, the Reserve banks and the banks which are members of the fund, and inasmuch as the Treasury may buy the notes of the Corporation and may guarantee their payment as to principal and interest, the potential resources of the Corporation, should that provision be included in the bill as passed, would approximate $1,250,000,000.

Testimony before the House committee indicates, I believe, that thus far the income of the Corporation has taken care of all demands made upon it by reason of the failures of banks. In view of the large number of banks which were closed and not allowed to reopen in March 1933, and in view of the tremendous contributions made to the capital structure of banks through the Reconstruction Finance Corporation, it seems reasonable to conclude that the next few years should not witness many bank failures and, therefore, the actual funds of the Corporation plus its potential resources should be adequate to take care of all failures. If we are to anticipate that the failures, say, in the next 5 years will be in excess of one and a quarter billion dollars, then indeed the prospect for the country as a whole is a most discouraging one, but I for my part am not disposed to be pessimistic. I am hopeful that the soundness of the banking system will grow progressively better.

In the second place, the bankers' associations of the States I represent believe very strongly that the mandatory assessment of

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one-eighth of 1 percent of total deposits is most undesirable from the standpoint of the banks themselves. I would not have you believe that the view I am here expressing rests upon mere opposition on the part of the banks to insurance of deposits. As you gentlemen well know, there has been a difference of opinion among the bankers themselves in regard to the matter, but I think there is unanimity of opinion among the bankers of the States I represent that because of the present low earnings of the banks, an assessment of one-eighth of 1 percent of total deposits is entirely too high and will result in one of two things, either the payment of the assessment out of the capital funds of many banks or the withdrawal of many banks from the Deposit Insurance Corporation.

I am sure that all of us hope that the year 1934 was not a normal one from the standpoint of bank earnings, but so far as my information and experience go, earnings thus far in 1935 for the banks as a whole are lower than for the same period in 1934. My plea in behalf of the banks of these six States is based upon the abnormal conditions existing last year and this year, and the belief that a permanent rate of assessment should not be established when earnings are so abnormally low. It is true that in 1934 write-offs of losses were extraordinarily heavy and were largely accomplished through the issuance of debentures or preferred stock. There are, however, few who believe that the banks will not suffer further losses which must be taken care of and that one of the most urgent needs of our banking system at present is a building up of a permanent surplus and reserves. That this is the view of the framers of this bill is evident from the fact that this bill before the Senate and as passed by the House provides that all banks which are insured must set aside each year one-tenth of their net earnings for the preceding 6 months to surplus until the surplus shall equal the capital.

In support of the view I am expressing with regard to the low earnings of the banks in the States which I am representing, I want to present some figures with respect to the earnings and payment of dividends by the State banks. I am unable to supply the figures for the national banks, as I understand they have not yet been compiled for the year 1934, but inasmuch as the State banks constitute about two-thirds of the membership of the insured banks, I think that the figures I give for State banks will be representative of both the State and National banks in these States.

Senator Townsend. You are just speaking of the State banks in the six States to which you have referred?

Mr. Elliott. Yes; I think the percentage applies to the whole country, about 2 to 1.

In California there are 153 State banks, 66 of which paid no dividends on their common or preferred stock during the year 1934, 35 paid a dividend on the preferred stock only, while 52, or about 33⅓ percent, paid dividends on the common stock. In Idaho there are 35 State banks, of which 30 paid no dividends and only 5 paid a dividend on the common stock. In Utah there are 46 State banks, 32 of which paid no dividends on the common stock, 29 paid a dividend on the preferred stock, and only 14 paid a dividend on the common stock.

Senator Townsend. Is the preferred stock owned by the Reconstruction Finance Corporation?

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Mr. ELLIOTT. Yes. It carries a dividend rate of, I think, about 3 percent.

In New Mexico, there are 18 State banks, of which only 1 paid a dividend on its common stcok, while 8 paid dividends on preferred stock. I regret that the figures for Oregon are not available. The recent destruction of the State Capitol by fire destroyed the records which have not yet been recompiled, nor have I figures for Arizona in which there are, however, only seven State banks.

A summary of the earnings of the insured State banks of these six States shows for 1934 a net loss of over $16,000,000, while an assessment on total deposits at the rate of one-eighth of 1 percent would amount to $1,400,000. In other words, on top of the deficit in 1935, if like 1934, you would have an assessment of $1,400,000.

Senator McADOO. Have you any idea what amount in the deficit is represented by write-offs?

Mr. ELLIOTT. I have the figures, Senator McAdoo, supplied as to the net earnings of the banks, the recoveries, the charge-offs, and the net additions to or withdrawal from surplus.

Senator McADOO. Can you supply them for the record?

(The data referred to are inserted as follows:)

Statistics with reference to all State Federal Reserve member banks and State nonmember banks whose deposits are insured in the Federal Deposit Insurance Corporation, calendar year 1934

State	Number of banks	Net earnings	Recoveries	Charge-offs	Net additions or deductions to or from profits
Arizona	7	$252,000	$397,000	$362,000	$287,000
California	124	8,913,000	10,499,000	34,451,000	[1] 15,039,000
Idaho	35	388,000	323,000	657,000	54,000
New Mexico	17	64,000	120,000	301,000	[1] 127,000
Oregon	49	238,000	302,000	1,276,000	[1] 736,000
Utah	45	828,000	714,000	2,444,000	[1] 902,000

[1] Red figures.

Mr. ELLIOTT. Yes. What I want to urge upon you in the light of these figures is the fact that many banks, and this applies to national banks as well as State banks, and particularly the small banks, are not now earning any money in the six States that I represent; and the prospect for any immediate change in this situation is extraordinarily slight. The question, therefore, arises as to the soundness of a course on the part of Congress which would require a considerable number of banks, if they desire to remain insured, to make a contribution out of capital assets when the Government has been at such great pains through the Reconstruction Finance Corporation to strengthen the capital of the banks of the Nation by purchasing upward of a billion dollars of preferred stock and debentures.

In the light of the figures which have been here presented there is the basis for an argument in support of the view that the wise thing to do would be to suspend the assessment against the banks for at least a year with the purpose of allowing them to strengthen themselves either by adding to their reserves or by further writing off and writing down their losses and doubtful assets. Certainly there is convincing evidence that one-eighth of 1 percent of total deposits is far

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too high. One-half of that would be adequate for the corporation and far less harmful to the banks. One of the purposes of the insurance of deposits was to create confidence in the public in the banks, and I think it is generally admitted that this purpose has been very largely accomplished. It hardly seems wise now to pursue a course which would result in weakening the banks in which you have sought to create confidence.

Senator McAdoo. What would you suggest should be done—specifically—to have a reduction to one-twelfth of 1 percent or one-sixteenth of 1 percent?

Mr. Elliott. I should like to make this clear, that I am not speaking for my individual bank in this situation, nor am I speaking primarily for the large banks. I am speaking primarily on behalf of the small banks out in the country districts that are having a very difficult time making enough money to take care of normal losses under these conditions. My suggestion here is not any rate, but a suspension of any assessment for 1 year.

Senator McAdoo. Suppose that were not done; what is the maximum that you are prepared to say should be assessed for 1 year?

Mr. Elliott. One-eighth of 1 percent is the amount set by the House. One-twelfth of 1 percent was recommended as adequate by the chairman of the Board of the Federal Deposit Insurance Corporation. I think the banks that I represent certainly feel, and I believe they have so expressed themselves almost unanimously, that even one-twelfth is more than they should be required, under these conditions, to pay; and if you are going down the line, perhaps one-sixteenth.

Senator McAdoo. Suppose it were either suspended or made very low for the first year; then what would you say would be a reasonable percentage to ask after that?

Mr. Elliott. I would say, Senator McAdoo, that under normal earning conditions most banks in the country could perhaps afford to pay one-eighth of 1 percent, though that is a rather high assessment.

Senator McAdoo. You spoke of the mandatory provision to which you object. What is your idea about that?

Mr. Elliott. I do not think you ought to keep piling up year after year without any limit.

Senator McAdoo. You mean, you would leave it to the Federal Deposit Insurance Corporation?

Mr. Elliott. Some discretion in them to determine that.

Senator McAdoo. It has been suggested here that when the fund reaches $500,000,000 the assessments shall automatically cease until there should be an impairment, if any, to the extent of 25 percent, after which the assessments would be automatically resumed until the deficit had been restored.

Mr. Elliott. That would be a total fund of $500,000,000, not a contribution of $500,000,000 from the banks. If you retain in the bill the provision which will allow the Corporation to issue notes and debentures to three times the contribution by the Government and the bank, it seems to me that $500,000,000 which would then produce a fund of $2,000,000,000, under all ordinary circumstances should be adequate to meet even the most unusual conditions.

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Senator McAdoo. You mean, under extraordinary circumstances?

Mr. Elliott. Even under extraordinary circumstances.

Senator Glass. That would be upon the assumption, however, that the Corporation is going to issue debentures?

Mr. Elliott. Yes.

Senator Glass. Would it not be well to avoid the issuance of debentures?

Mr. Elliott. I hope we will never have occasion to do so, if that is what you mean, Senator Glass.

Senator Glass. Mr. Elliott, do you happen to know how many banks are now being propped up by the Reconstruction Finance Corporation and to what extent in money they are being propped up?

Mr. Elliott. No. The capital or notes issued amounts to about $1,000,000,000. Some of that has been repaid; the exact amount I have not now in mind.

Senator Glass. Yes; some of it has been repaid; but is it not a fact that a great deal of it has not been repaid and that the Reconstruction Finance Corporation owns the principal assets of those banks?

Mr. Elliott. I think there are relatively few banks in which the Reconstruction Finance Corporation owns a majority of the stock or even 50 percent of it. There are very few cases in which the preferred stock equals the common stock. But they do own, of course, a very substantial interest in the banking structure of this country and have a very important position in it.

Senator Glass. And for the loans made they have taken the cream of the assets of these banks; is not that so?

Mr. Elliott. I am not speaking about any loans. For the preferred stock they do not take any security.

Senator Glass. That is practically a loan.

Mr. Elliott. But they do not take any security for it.

Senator Glass. No; but it is practically a loan excepting in the instances of a few banks.

Mr. Elliott. It would be very helpful to the banks if it could be described or characterized as a loan, because then we could deduct from our income-tax returns as interest instead of dividends, the amount we pay on our preferred stock.

Senator Glass. A very large amount of money was loaned to these banks and the cream of their assets taken as security. Is not that a fact?

Mr. Elliott. Well, I am not in possession of the facts sufficiently to make a statement as to that, Senator Glass.

Senator Glass. I ask you these questions because you were doubtful as to whether we should have another year of bank failures.

Mr. Elliott. I am still of the opinion that in view of the tremendous contributions to the capital of the banks made by the Reconstruction Finance Corporation, plus something that I did not mention, namely, the contributions of stockholders which have been very considerable, running into several hundreds of millions of dollars, if we have anything like a return to normal conditions within a year or two, I do not think we will have heavy bank failures again.

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Senator McAdoo. The write-offs of doubtful assets and the charge-offs of loans have put the banks in a very much stronger position than they have been in for many years?

Mr. Elliott. And there is a prospect, of course, of eventually having considerable recoveries of a large part of their assets which have been charged off.

Senator Glass. We are very much obliged to you, Mr. Elliott.

(The witness withdrew from the committee table.)

Senator Glass. Is Mr. Ward in the room?

Mr. Ward. Yes; Senator.

STATEMENT OF LOUIS B. WARD, DETROIT, MICH.

Senator Glass. Will you be good enough to give your name?

Mr. Ward. My name is Louis B. Ward. I am from Michigan. My home is in Pontiac, Mich., and my office is in Detroit.

Senator Glass. We have under immediate consideration Senate bill 1715, but there has been offered in the Senate by Senator Nye a bill that, as I understand it, he will offer as a substitute for the Senate bill if and when reported, Senate bill 2162, in which it was incidentally stated that Father Coughlin was interested and which he helped prepare; and at the suggestion of members of the committee I extended to Father Coughlin more than 10 days ago an invitation to appear here. I have understood from you that he did not find it convenient to come.

Mr. Ward. I wanted to make a statement on that, Senator.

Senator Couzens. Before you start your statement, will you tell us your experience and background to indicate your knowledge of the banking business?

Mr. Ward. I am primarily a student. My occupation, Senator, is that of a business counsellor. For 14 years I have counseled business in Detroit, and that is my occupation today. I come before you, after approximately 25 years of study, an academic study. I never worked in a bank, never stood behind a cage, never counted much change in my life. I have taught constitutional history. My presentation to you gentlemen of the committee——

Senator Bulkley. Have you been an independent business counselor, Mr. Ward?

Mr. Ward. Yes; for a number of years, and I have been with an organization for other years as counsel to the automotive industry.

Senator Couzens. Have you been employed by the General Motors Co.?

Mr. Ward. I have been employed by General Motors, Fisher Body, the interests of Packard, Hupmobile, Graham-Paige, Chrysler, Libbey-Owens-Ford, Champion Spark Plug, and practically all the large accounts of the automotive industry; and I am today representing here the National Union for Social Justice whose program of 16 principles involves not only banking, but general economic problems facing this country, and my work for years has been the study of those problems. I do not appear before you as a banker.

Does that answer your question, Senator?

Senator Couzens. Quite well, I think.

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Mr. WARD. The National Union for Social Justice and Father Coughlin are tremendously appreciative of the invitation extended by Senator Glass some 10 days ago. I received a copy of that letter which I requested from Senator Glass office. On getting in touch with Father Coughlin on Sunday I told him that a wire had been sent to him. I was mistaken; it was a letter. That letter has not reached his desk up until this morning. I am very sorry for that and so is Father Coughlin. He would have liked the courtesy of replying to it. It is probably in some mail bag in his building. He on Sunday night extended his appreciation to the Senator's invitation, and as soon as he receives a copy of this letter, Senator, he will, of course, write you immediately.

He arrived in Detroit on Sunday and I talked to him on Sunday night before his broadcast, and he was unable to get here today. In a certain sense it is well that he did not get here. He is tremendously interested in this legislation; but what you gentlemen just witnessed—the photographers stepping into the room and taking pictures—I believe would divert attention from the legislation to the personality.

He has asked me to appear in his place. Our witnesses will be very few. The National Union for Social Justice has requested Senator Gerald P. Nye and Congressman Martin L. Sweeney to introduce the so-called "Nye-Sweeney bill", a central banking bill. Our witnesses will consist of Mr. George LeBlanc, whom I have asked to be here the first thing in the morning. Mr. LeBlanc has been president of two New York banks, has been for 37 years in the Street, and he is a counselor at no. 1 Wall Street today. He was senior vice president of the Equitable Bank, and we rely upon Mr. LeBlanc for the comments of a banker on this bill. We recognize full well that we cannot ask the bankers to appear here in favor of a central banking bill.

The second witness is Mr. Robert M. Harris, of the New York Cotton Exchange, a man who has been a stockholder and, I think, the largest stockholder, in one of the banks in Texas, an owner of agricultural land, and his interest is in the merchandising of the agricultural product primarily, and that is his interest in the exchange.

I have asked Mr. Edward E. Kennedy, the national secretary of the Farmers' Union, to comment on this legislation from the standpoint of the farmer.

Our own organization has now 8,500,000 members, every one of whom has signed his name to 16 specific principles of social justice, and all of whom stand solidly behind six pieces of legislation emanating out of the Seventy-fourth Congress. Those are the Thomas Patman bonus plan, recently defeated; the Frazier-Lemke farm-refinancing bill, the Nye-Sweeney central-bank bill, the Wagner-Connery labor-disputes bill, the Thomas-Massingale cost of production plus a profit bill, and the Wheeler-Rayburn public utilities holding company bill.

Illustrative of the fifteenth principle of our National Union of Social Justice is the Nye bill to prevent profiteering in time of war.

For the information of the committee I ask that these 16 principles be introduced into the record for the reason that they substantiate my position as a witness before this committee, not as a bank spe-

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cialist, but as a lobbyist in favor of and lobbying for that type of legislation.

Senator GLASS. That may be inserted in the record.

(Preamble and principles of the National Union for Social Justice referred to and submitted by the witness as here printed in full as follows:)

PREAMBLE AND PRINCIPLES OF THE NATIONAL UNION FOR SOCIAL JUSTICE

Establishing my principles upon this preamble, namely, that we are all creatures of a beneficent God, made to love and serve Him in this world and to enjoy Him forever in the next, and that all this world's wealth of field and forest, of mine and river has been bestowed upon us by a kind Father, therefore, I believe that wealth as we know it originates from the natural resources and from the labor which the sons of God expend upon these resources. It is all ours except for the harsh, cruel, and grasping ways of wicked men who first concentrated wealth into the hands of a few, then dominated States, and finally commenced to pit State against State in the frightful catastrophes of commercial warfare.

With this as a preamble, then, these following shall be the principles of social justice toward whose realization we must strive.

1. I believe in the right of liberty of conscience and liberty of education, not permitting the state to dictate either my worship to my God or my chosen avocation in life.

2. I believe that every citizen willing to work and capable of working shall receive a just and living annual wage which will enable him to maintain and educate his family according to the standards of American decency.

3. I believe in nationalizing those public necessities which by their very nature are too important to be held in the control of private individuals. By these I mean banking, credit and currency, power, light, oil and natural gas, and our God-given natural resources.

4. I believe in private ownership of all other property.

5. I believe in upholding the right to private property, yet of controlling it for the public good.

6. I believe in the abolition of the private-owned Federal Reserve Banking System and in the establishing of a Government-owned central bank.

7. I believe in rescuing from the hands of private owners the right to coin and regulate the value of money, which right must be restored to Congress where it belongs.

8. I believe that one of the chief duties of this Government-owned central bank is to maintain the cost of living on an even keel and the repayment of dollar debts with equal value dollars.

9. I believe in the cost of production plus a fair profit for the farmer.

10. I believe not only in the right of the laboring man to organize in unions but also in the duty of the Government which that laboring man supports to facilitate and to protect these organizaions against the vested interests of wealth and of intellect.

11. I believe in the recall of all nonproductive bonds and thereby in the alleviation of taxation.

12. I believe in the abolition of tax-exempt bonds.

13. I believe in the broadening of the base of taxation founded upon the ownership of wealth and the capacity to pay.

14. I believe in the simplification of government, and the further lifting of crushing taxation from the slender revenues of the laboring class.

15. I believe that in the event of war for the defense of our Nation and its liberties, there shall be a conscription of wealth as well as a conscription of men.

16. I believe in preferring the sanctity of human rights to the sancity of property rights. I believe that the chief concern of Government shall be for the poor, because, as it is witnessed, the rich have ample means of their own to care for themselves.

These are my beliefs. These are the fundamentals of the organization which I present to you under the name of the National Union for Social Justice. It is your privilege to reject or accept my beliefs, to follow me, or repudiate me.

CHARLES E. COUGHLIN,
Royal Oak, Mich.

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Mr. WARD. The idea of a central bank is precisely 6 years older than the convention which framed the Constitution of the United States.

In the month of May 1781 Pelatiah Webster wrote a pamphlet which he circulated among the people of the States asking that there be called a convention of people to revise the Constitution, which was then, of course, the Articles of Confederation. Madison spoke of this Pelatiah Webster as " an able though not conspicuous citizen "; and that is precisely the point of the National Union for Social Justice—not to emphasize the conspicuous names in America, but to attempt to throw before the people certain economic reforms that have usually emanated from the people.

Webster, in his pamphlet, after discussing the fiscal system of the United States under the Second Continental Congress, suggested as one of the chief remedial provisions that a central bank be established because, and I quote:

the authority of Congress at present is very inadequate to the performance of their duties and then this dictates the necessity of their calling a continental convention for the express purpose of ascertaining, defining, enlarging, and limiting the duties and powers of their constitution.

It was this pamphlet of Pelatiah Webster that so influenced the thought of men that the very idea of the present Government of the United States was predicated upon the theory of a central bank first advocated in 1781, and the convention of 1787 was directly built upon that idea.

In 1787 the Fathers met in a convention, and it was Charles Pinkney who on Tuesday, May 29, of that year submitted article VI of his plan of union, which read [reading]:

The Legislature of the United States shall have the power to borrow money and emit bills of credit; to coin money and regulate the value of all coins and fix the standard of weights and measures.

Significant in this early draft are the words " emit bills of credit." Significant, likewise, is the idea of regulating the value of money and fixing standards of weights and measures. Money was to be regulated, but the standards of weights and measures were to be fixed. Money was something to be created by the Government, while the standard of weights and measures was to be fixed by law.

Money in those days was not confused with wealth, for then as now wealth might only be created by the unremitting toil of man expended on natural resources. But money is not wealth. It is a method of distributing wealth. It was a function of sovereignty; and Charles Pinkney recognized it when he wrote article II of his plan submitted on that same day, Tuesday, May 29, 1787, in these words [reading]:

No State shall emit bills of credit nor make anything but gold, silver, or copper a tender in payment of debts.

I would be tempted to follow the course of this power over money throughout the debates of the Federal Convention, but the distinguished chairman of this Committee said on Friday that he was being pressed for time on these hearings. But I really believe that if each Member of Congress read the Federalist and read Madison's Notes on the Convention, the idea of a central bank would

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so impress itself that it would not need the tremendous propaganda that I think it needs today.

I want to recall Elbridge Gerry's remarks in that convention on June 13, 1787. It was Gerry who restated the maxim regarding money, that the people should hold the purse strings. I want to call to the committee's mind that Gouverneur Morris was opposed to the issuance of paper money or bills of credit, as was Pierce Butler, on the ground that—

> if the credit of the Nation were good no such issuance were necessary, and if the credit were not good the issuance were unjust.

I also want to recall what James Madison said in his desire for the issuance of money to be preserved under the new Government.

Gouverneur Morris had argued that the many interests would oppose the plan of government if paper emissions were not prohibited.

George Mason had a mortal hatred for paper money, but was unwilling to tie the hands of the legislature. Now I quote Madison in respect to Mason:

> He observed that the late war could not have been carried on had such a prohibition existed

that is, without the issuance of paper money.

Today the committee finds a wide-spread propaganda against this Government issuing money; and I believe it is well to look back to the debate of the fathers and find them crediting the winning of the Revolution by a Government issue of currency. John Randolph, of Virginia, notwithstanding his antipathy to paper money, would never agree to strike out the words "empower the Government to issue", because he said that he could not foresee the occasions which might arise.

James Wilson opposed the right of Congress to emit bills of credit, as did Pierce Butler. But the important opinion on the entire subject was that of James Madison himself, who wrote [reading]:

> This vote in the affirmative by Virginia (the vote by which the specific permission was not given Congress) was occasioned by the acquiescence of Mr. Madison, who became satisfied that striking out the words would not disable the Government from use of paper notes, as far as they could be safe and proper.

The argument of Mr. Madison is tied up with the nature of sovereignty.

Under article I, section 8, clause 5, of the Constitution, Congress is empowered "to coin money and regulate the value thereof of foreign coins", and under the eighteenth clause of article I, section 8, Congress is empowered to "pass all laws necessary and proper to carry into execution the foregoing provisions."

The Fathers put squarely in the Constitution of the United States two important powers: The power to tax and the power over the money of this country. The Fathers placed the power over money in the hands of Congress, the power to coin money and regulate its value, and they prohibited this power to the States in this language, by section 10 [reading]:

> No State shall enter into any treaty, alliance, or confederation; grant letters of marque and reprisal; coin money; emit bills of credit; make anything but gold and silver coin a legal tender in the payment of debts.

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There is no need to point out to this committee the elementary fact that 74 Congresses have been called into session and every one of them has put solemn thought and endless labor upon the problem of taxation, with commission after commission and great economic study on a tariff, for example, with endless effort on the internal revenue as represented by the excise duties and sumptuary laws, with the initiation of an amendment to the Constitution to permit the income tax, and with the new intricate measures covering new processing taxes.

The tax problem has had 154 years of thought. If we contrast this with the power of Congress over money, we would be surprised. Yet 10 centuries before Christ the city-states of Greece, Athens, and Sparta, recognized that the power over money is the most important single asset of sovereignty. Imperial Rome in later centuries farmed out the taxes, but the coin of Caesar was never permitted to go into private hands.

But the Government of the United States, though denying to any State the power to emit bills of credit—in other words, the power to issue paper money—consistently has permitted the State banks to issue paper money from the earliest days down to 1862.

The Government of the United States, with the power placed in the hands of Congress by the people under the Constitution has abdicated its power over money and permitted the private banking interests of this Nation to usurp the earliest and greatest attribute of sovereignty—the power over money.

From the foundation of our country down to 1862 private banking exercised the prerogative given by the Fathers to Congress, and the States which were refused the right of issue had to witness a State bank incorporated under its authority exercising a power that that sovereign State was denied.

But Congress, by a 10-percent tax on State bank issues, recaptured its prerogative and then there grew up in this Nation the kind of money which has dominated the trade and commerce of the country throughout the recent decades, until now 95 percent of our business is conducted with a new kind of money, undreamed-of in the days when the 55 men drafted the Constitution, and unchallenged by every Congress that has met from the Civil War to the present day.

I refer to the ability and power of a bank to enter upon its ledger a debt and against the debt grant the right of withdrawal. I refer to our demand deposits against which there need be but a 10-percent reserve in currency, so that it becomes the right of the people, the privilege of the people, to pass through the wicket of a bank a promissory note together with people's securities in stocks or bonds or mortgages and against that promissory note with, of course, the security behind it, issue to the extent of the loan, checks which have become the money of the Nation.

What is the present situation in America where we have, unquestionably, the richest-developed Nation in the world; where we had an evaluation in the year 1920 of $488,000,000,000 of national wealth; where we have in 1930, after a decade of so-called "boom" an evaluation of $369,000,000,000, and where in 1935 no economist in the country would evaluate America at over $200,000,000,000 of national wealth?

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Our farms have depreciated from $78,000,000,000 in 1920 to 57,000,-000,000 in 1930 to $37,000,000,000 in 1934. That means that a farm, the average farm, was evaluated at $12,000 in 1920, at $9,000 in 1930, and a little less than $6,000 in 1934.

There is little question in the mind of anyone that a man owning a $12,000 farm in 1920 had the right to a $6,000 mortgage on it. The decade of the so-called " prosperity " in the twenties never gave cost of production to the American farm. The farm debt actually increased and the value of the property dropped one-fourth.

By 1934 the entire property had depreciated to $6,000, and 10 years more of such decimation of values will bring the total value of our farms in America down to the present face of the first mortgage upon them, $8,500,000,000.

Dr. Adolph Miller testified here last Friday. His charts and his testimony represent a splendid background for this study. He told this committee how the present Federal Reserve System decreed in 1924 the slump which is indicated in the automotive industry by the chart which I now show you. There [indicating] is the story of the automotive industry from 1913 to 1931. Here [indicating] is the year 1919, where production was held up continuously. Here is your splendid drive straight up [indicating], and here [indicating] correspondence to Dr. Miller's chart with a drop in 1924.

Here is Dr. Miller's second chart [indicating] with a drop in 1927, and here is your market and here is your depression, straight down [indicating].

And that is a reaction that can be pictured in the home.

Senator Bulkley. What is this—a total of all passenger cars?

Mr. Ward. Yes; and it is backed by the individual companies. The rise and fall of prosperity, independent of management, by the first chart, and of course qualified by the next. One of the distinguished members of the committee knows so well why the automotive industry failed in individual cases. That chart is a picture of the largest single manufacturing industry in this country [exhibiting].

I do not want to take the time of the committee, but I want to show the members of the committee that in the automotive industry 1926 reached the high point in invested capital, and then it tapered off. I want to show the net profit in the automotive industry and the manufacturers' bonuses for the war period. Production was down. Here [indicating] is the war, with the net profit, and there [indicating] is the way the profits rose in the automotive industry.

Senator Byrnes. What year is the peak?

Mr. Ward. 1919 is the peak. We have the net profit in relation to sales of all companies. Here are the sales in the war period [indicating]. Here is the bonus to American industry as reflected by the industry that I have been interested in for 14 years [indicating].

Here is a gross income chart. The capital invested is declining. Eighty-five percent of the people are in the low-price field. It shows that automobiles are a popular thing, for the people that own cars costing $3,000 amounts to 0.28 of 1 percent.

Senator Bulkley. What do you consider the low-priced field?

Mr. Ward. Below $750—the Ford, Chevrolet, and Plymouth.

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I think that these charts, for which I wired Sunday night, are most interesting to some members of this committee. Here is 61.5 percent of all sales going to people with less than $3,000 income.

Senator BYRNES. How do you ascertain that fact?

Mr. WARD. I might say, Senator, that the study cost thousands of dollars in its completed form. They are bought on time. They want to know what Ward does, and what is his income, before they grant the credit. You see, we have 23,000,000 motor vehicles, and 30,000,000 families. We know what kind of people do not own cars. The rest of them do. So it follows the income classes.

Senator GLASS. What kind of people do not own cars?

Mr. WARD. Well, there are a few in America.

Senator GLASS. Those in the almshouses?

Mr. WARD. That is about it. California and the District of Columbia lead, and there are a couple of States in the country that do not own cars.

Senator BYRNES. What did you say about California and the District?

Mr. WARD. One car to every three persons. There is the Federal pay roll in one place, and the retired wealthy in the other. The District of Columbia did not catch California, however, until the last few years. In Kentucky, North Carolina, and South Carolina the ratio is 1 to 10; Mississippi, 1 to 16 people. There is 1 car to every 4 persons in this group of States [indicating], and with this number of millions of cars it becomes an interesting study from the financial standpoint.

The point I wanted to make with the charts was that I enjoined Dr. Miller's testimony tremendously, because, without touching his field, in the field in which I work, there was not a single point in his statistical information where I could not bow my head and say " That is reflected. I know what that is in business."

Dr. Miller told this committee how the present Federal Reserve System decreed in 1924 the slump there indicated in the automotive industry. He testified that the present Federal Reserve System went into its open-market operation in 1927 to start an inflationary process reflected in the automotive industry with the line I have indicated, and the doctor was not questioned in public on what the Federal Reserve did in 1929 in open-market operation, to account for the collapse. He told you that he was against the commodity dollar, for there on his chart was an almost even line and level of commodity prices during which period profits were not distributed but were used in speculation, in the wildest speculation that this country ever knew.

My charts happen to show the withdrawal of capital from the automotive industry before the period of its greatest sales.

Gentlemen, we are suffering in this country, I believe, from a paucity of money——

Senator BULKLEY. Mr. Ward, what happens when capital is withdrawn from the automotive industry? Are automobile factories converted to other use?

Mr. WARD. There have been, Senator, some 565 groups that have gone into the manufacture of automobiles, and there are today approximately 13 companies operating. Five hundred and forty, let us say, of the 565 have disappeared, because of their inability to manufacture cars, because they did not have the brains for that

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highly competitive business, as the senior Senator from Michigan can also confirm. There are a few of them that succeeded. In 1921 I think there were 171 manufacturers of passenger cars in the country, and today, if you will look at that information, which is 2 years old, you will find that three of them do 90 percent of all the business in the country—Ford, General Motors, and Chrysler. Three out of those 565 have made a substantial success. Two have been down to Jesse Jones this year to bail them out. That accounts for five. The rest are dividing 5 percent of the business.

Senator BULKLEY. When that capital is withdrawn, are the factories devoted to other purposes?

Mr. WARD. Yes, sir. They just become——

Senator BULKLEY. Of no value at all?

Mr. WARD. I think Fisher's had 49 factories for automotive bodies when I first knew the account. They have five operating today. That is accounted for by technological development, plus duco, plus what Dr. Miller pointed out, the eternal march to reduce the cost of production through greater efficiency, and dismissal of labor; and those that cannot follow, fall by the wayside and leave us, in that magnificent industry, three dominating it to the extent of over 92 percent. Many of the rest are unable to get credit. One of the great ones always had it himself. Two others went to the people with stock, and the rest are dependent on bank loans in part. Then, when a situation such as 1921 comes along—I think there is a profit chart that answers that question here. [Referring to chart.] Here is the depression of 1921. General Motors lost $38,680,000; Chrysler, $3,200,000; Packard, $3,400,000; Willys-Overland, $13,000,000; and Peerless and Graham-Paige lost.

Here is your depression, gentlemen [indicating on chart]. In 1929 the net profit of the automotive industry was $424,000,000. They decreed a contraction of call loans and shot the prosperity in this Nation, and in 1930 the profit drops to $200,000,000. The next year, 1931, it drops to $21,000,000—a loss of $460,000,000 in 2 years. You can trace everything there right on Dr. Miller's charts.

Senator COUZENS. What, in your opinion, would have altered that situation?

Mr. WARD. An understanding of the money question, differentiating money from wealth. Let men go on and create the real wealth of the Nation by the labor of men against the national resources and the manufacturing, and let money, which is not wealth, but which is a method of distributing wealth, issue forth from the Government of the United States, and not be in the hands of the private bankers for its control. I do not say that as an arbitrary, quick answer, and I do not say it is a panacea. The fact that we are backing 16 principles and not 1, I think, ought to be suggestive of the fact that we are not interested in panaceas.

Senator COUZENS. Do you make any discernment between money and credit?

Mr. WARD. I include in money the credit money of the demand deposits in the banks, which is pure fiction money, which is the right concept of money, in the sense that it is a purely created thing, and the free issue of that type of money carries on 95 percent of our transactions. That is in the hands of the private banker, who can expand it and contract it at will.

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On that question, I have here the best essay on money that I ever read, consisting of four pages. This is an issue of the New York Herald Tribune, called "The Financial Section of a Newspaper", edited by C. Norman Stabler, and sent out to the advertising agencies. I do not think there is a man in the United States who has not a debt of gratitude to the organ of Ogden Mills for contributing the best four-page essay on money that I ever saw. He opens this little book with the wording "preference", showing that (reading):

Sixty-six percent, or 656 of the 994 members of the New York Stock Exchange who responded to the question "What morning New York newspaper do you read regularly?" mentioned the New York Herald Tribune.

He goes on to show the publicity value of this little book. It is addressed to:

Students in schools and colleges, many of whom have had no immediate contact with the financial world and consequently are not thoroughly acquainted with Wall Street parlance, are realizing the necessity of the coming debtor versed in the ways of those institutions in lower Manhattan from whose rooms are directed the flow of credit and commerce to all sections of the globe.

He is going to send the college to school in Wall Street, through the medium that 67 percent of the New York Stock Exchange uses. He shows the art of publicity in this question you gentlemen are dealing with. One of the items is entitled "The Week in Finance", by Edward H. Collins, giving the people the idea that the bankers' convention proved a good show from the news standpoint, but a none too happy occasion for the bankers themselves. "It should have been their great opportunity for a concerted demonstration against the administration's banking heresies—for an appeal to sound public judgment against attempts to sabotage the banking system—but they failed utterly to make anything of the opportunity."

That is the point of view of this against the administration. That is on the news page.

Senator Bulkley. Mr. Chairman, I ask that that four-page essay on money be printed in our record at this point.

Mr. Ward. I offer it, and thank you for the suggestion.

Senator Glass. If there is no objection, it will be done.

Mr. Ward. I want to say that it is the best we can find on the secret of money.

(The matter referred to is here printed in full as follows:)

(Note.—This comprises pages 26, 27, 28, and 29 of the attached pamphlet.)

Our Monetary System

A BRIEF DISCUSSION OF ITS ESSENTIAL ELEMENTS AND MECHANISM

(By Edward H. Collins, associate financial editor New York Herald Tribune)

The modern banking system exists primarily to provide and regulate the supply of money.

There are three general classifications of money in use today. These are: Real money, representative money, and deposit money (or credit). Roughly speaking, they represent successive historical steps in the development of the present monetary system.

The distinguishing characteristic of real money is that it is freely received, not because it bears the seal of the State nor because it is exchangeable for some other form of money, but because of its own value. In most of the civilized world the supply of real money, for more than half a century, has

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been gold coin and bullion. Before the World War gold coins were widely used as pocket money throughout the more prosperous portion of Europe and in western United States. They could have been employed elsewhere in this country, but a preference had developed for the more convenient paper money. In the West adherence to gold coins was a carry-over from the old days when, during and after the Civil War, paper money had fallen into disrepute.

In the 14 years before the war the European Continent showed some slight tendency toward the increased use of paper money. However, the central banks were, for the most part, forbidden to issue paper currency in small denominations, hence the chief reliance of the public was on gold and silver[1] coinage. In England the lowest denomination of Bank of England notes was £5, about $25. The prohibition of smaller denominations of paper money in Europe seems to have grown out of a desire to protect the man of slender means from loss in case the issuing bank failed to meet its obligation.

It is possible that the whole civilized world would soon have come to the use of the more satisfactory paper money by this time in the natural course of events; as it happened, however, the exigencies of the war made such a course compulsory. Both in the United States and the rest of the world gold was impounded immediately at the outbreak of hostilities. The reason will be seen presently.

Representative money, the second of the three general classifications, is traceable to the goldsmiths, the first private bankers of Europe. People used to leave their money—that is, their gold or silver coins or bullion—with the goldsmiths for safekeeping, and the goldsmiths used to give them in return written acknowledgments, or receipts. These acknowledgments, since they represented claims on specific amounts of gold or silver, soon became widely acceptable in place of money.

Then the goldsmiths made a simple, but epochal discovery. They discovered that only a small percentage of the holders of such receipts ever wanted their gold at one time. They thereupon started the practice of issuing receipts in excess of the amount of bullion which they held, lending these surplus "bank notes" out at interest. They not only added a new and profitable field of banking to their original function, but at the same time laid the foundation of the modern bank-note issue.

Though the principle of issuing money redeemable in gold was sound so long as adequate gold reserves were maintained to accommodate those persons who might, from time to time, wish to convert their paper into gold, it was naturally subject to abuse.

The tendency was to issue as many notes as possible, since these notes were lent out at interest. So bad were these abuses that in most countries the privilege of note issuance early came under close State supervision, and today it is reserved generally to the central banks. Nor are even the central banks permitted to issue notes to their heart's content. So long as the countries of their domicile are on the gold standard they must not issue so many that the convertibility of the notes can be seriously questioned. There are numerous methods of assuring such convertibility. In Great Britain, for example, the Bank of England may issue up to £240,000,000 of notes secured by Government paper, but beyond that every pound note must be backed 100 percent by gold. In this country the law is that the Federal Reserve System must maintain a 40-percent gold reserve; that is, $40 in gold for every $100 Federal Reserve notes outstanding.

Whatever the mechanism employed, the purpose of maintaining an adequate reserve of gold behind the note issue is always the same. It is to guarantee that the currency will be redeemed in gold at the holder's option. This exchangeability of a country's currency at all times for its gold equivalent is what we have in mind when we say that a country is on the gold standard.

(At the time this article is being written—in September 1933—the United States is, temporarily at least, off the gold standard. As a result of the banking difficulties which culminated on inauguration day, March 4, in a Nation-wide banking moratorium, the Government announced that, in order to conserve the country's gold reserves, gold would not be paid out for currency or for export abroad. Similar action had been taken a year and a half earlier, Sept. 20, 1931, by Great Britain as a result of foreign "runs" on the gold reserves of the Bank of England. A number of lesser nations followed the action of Great Britain.)

The reader may ask: If our currency is issued by the Federal Reserve banks in the form of Federal Reserve notes, how is it that one of the bills in my pocket

[1] This was, as will be seen below, a form of representative money.

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bears the statement that it represents 1 silver dollar and a legend to the effect that the Seventh National Bank, of Wilkes-Barre, Pa., will pay the bearer $5 on demand The answer to these and similar questions that might be asked is this: Although the Federal Reserve note, issued by the Federal Reserve banks and backed by a gold reserve of not less than 40 percent, is the backbone of the currency today, our system is still cluttered up with the remnants of earlier stages of our monetary development and abortive monetary experiments. Silver certificates, "Treasury notes of 1890", United States notes, Federal Reserve bank notes (not to be confused with Federal Reserve notes) and national-bank notes. It is not possible to discuss the origins and status of all these outmoded forms of currency here. For present purposes it is necessary only to point out that although they have been permitted to remain in circulation, their amounts may no longer, except in the case of national-bank notes and Federal Reserve bank notes, be further increased. The Secretary of the Treasury is compelled by the law of March 14, 1900, to keep all kinds of money at parity with all other kinds, so that these miscellaneous forms are all ultimately redeemable in gold while the country is on the gold standard.

In addition to bank notes there is one other form of representative money. That is what is known as "token money", and comprises the subsidiary coinage which is used for the smaller everyday business transactions—the nickels, dimes, and quarters with which we pay our subway fare and for our movie seats. Token money is coined by the United States Mint on order of the Treasury when and as needed. Token coins, unlike the gold coins that circulated more or less freely before the war, is not real money because the actual value of the metal that it contains is less than the face value of the coins. The latter circulate by custom and as a matter of convenience even though they are not accepted as legal tender in unlimited amounts.

The third type of money that we have is what is known as "deposit money" or "credit." It is represented by the bank check, drawn against a bank deposit, and in the business world of today it far surpasses in volume and importance the representative money employed in hand-to-hand business transactions. In normal times, it is estimated, upward of 90 percent of all domestic business settlements are made by means of checks. This being so, it is important that we should understand clearly the source of this form of "money."

Many persons have a notion that a commercial bank is an institution which is set up with a certain amount of capital, and that its deposits are brought in in the form of cash by its customers, to be drawn against by check as needed. It is true that some deposits do come to the bank in that measure; but if that were the only source of deposits our monetary system would consist today of only about $10,000,000,000—the amount of its gold and currency—instead, as it does, of more nearly $444,000,000,000.

The vast majority of the bank deposits of the country are not brought in to the banks but created by them. For example, a storekeeper wishes to stock up for the Christmas trade. He goes to his bank and makes a loan, giving the bank his note, payable at such a time as, presumably, the goods shall have been disposed of to his customers. Now, the storekeeper does not draw down the proceeds of his loan in cash. What happens is that the bank credits him with a deposit in that amount, and he gradually writes checks against it as he needs it. It is in this manner—through the extension of business loans—that the bulk of our deposit money or credit comes into being.

Just as there is a limitation placed on the amount of representative money (Federal Reserve notes) that the central banks may issue, so is there a limit on the amount of deposit money that may be created by commercial banks. Member banks in the Federal Reserve System must maintain average reserves with their district Federal Reserve bank equal to 10 percent of their deposit liabilities.

Let us see, now, how the modern banking system has taken a given amount of real money—gold—and enabled it, as a monetary reserve, to do a great deal more than it could have done in the way of work had it been continued as a circulating medium.

Since, under our laws, currency can be issued against a 40-percent reserve of gold, it is clear that whereas $1 in gold in circulation is just a dollar, $1 employed as reserves permits the issuance of $2.50 in currency. But the use of deposit money, or credit, makes it possible to stretch our gold much further. For, obviously, if it is only required that member banks carry a 10-percent reserve against deposits $10 in "money" of this sort can be created out of every $1 in gold.

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But even this is not the complete picture. The mobilization of our gold in the Federal Reserve banks has added still further to the work that gold can do. To understand how this comes about, however, we must turn a moment to an examination of the mechanism by which the member banks do their banking with the district reserve banks.

Essentially they do it much as one of their own customers does business with them.

For example, if George Jones needs cash, he goes to his bank and draws out some that he has on deposit. But, suppose he wants cash but has none at the bank. In that case, assuming, as we must for purposes of analogy that his credit is good, he borrows at the bank, the latter setting up a deposit against which he may write checks. (See the discussion above of deposit money, or credit.)

A member bank in the Federal Reserve System needing more currency does precisely the same thing. If it has a deposit balance at the Federal Reserve in excess of the 10 percent required as reserve against the deposits of its customers, it simply draws down what it needs in the form of currency, reducing its reserve balance by that amount. Otherwise, under certain restrictions which need not be gone into here, the member bank borrows from its regional bank by rediscounting with it some of the discounted notes that it holds for its customers.

When a member bank does not need currency, but wishes to expand its own loans (deposits) it may likewise borrow at its district Reserve bank. The only difference in this case is that it withdraws no currency; its reserves are simply marked up on the books of the Reserve bank by the amount of the loan.

Let us see what has happened now, so far as increasing the usefulness of the gold dollar is concerned. The Reserve bank, it is clear, can "create" reserves for the member banks just as the latter can "create" deposits for their customers. How does this work out mathematically? Well, the Reserve bank must keep a reserve of 35 percent in gold[2] against its deposits, or $1 in gold against every $2.85 in deposits. But for every dollar of those deposits—since they represent the reserves of the member banks—the member banks may create deposits of $10. Therefore, in theory at least, $1 in gold in the vaults of the Federal Reserve System may, when used as a reserve against the latter's deposits, provide the basis for $28.50 in deposit money, or credit, in the member banks!

From the foregoing it will be seen that under our banking system the Federal Reserve banks provide the ultimate limits of monetary expansion—using money in its broader sense of both currency and credit. It remains to say a word about two mechanisms with which the system exercises some degree of control in addition. One of these mechanisms is the so-called "rediscount rate", loosely referred to at times as the bank rate; the other is the mechanism known as "open market" operations.

It has been observed above that when member banks lend heavily (thus creating deposits in the same amount) they turn to their district Reserve banks and borrow in order to keep their reserves up to the legal limit. By raising or lowering its rediscount rate, i. e., its charge for such loans, the regional bank can, and does, act either to encourage or discourage such borrowing.

The open-market operations consist in buying or selling Government securities in substantial amounts in the open market—in other words, from those dealers who act as a clearing house for this type of security. When such a dealer is paid for the Reserve's purchases he presumably deposits the check with a member bank. Since this check is a check on the Reserve bank it serves to build up the member bank's reserves and thus to add to its lending (deposit creating) power. Hence, a policy of open-market purchases on the part of the Federal Reserve System has the same general purpose as a low rediscount rate; that is, the purpose of stimulating lending. It will be at once clear that a reversal of this policy—heavy sales of Government securities by the Federal Reserve—would have the opposite result, hence would be regarded, along with the establishment of a high rediscount rate as evidence of a "tight money" policy—a desire to curtail, rather than expand, the supply of bank credit.

Senator Glass. Do you think the New York Herald Tribune would like to be responsible for the New York Stock Exchange in 1928 and 1929?

[2] Or lawful money.

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Mr. WARD. No, my good Senator. I think that the New York Herald Tribune, in an honest hour, sent to its advertisers an appeal on the strength of the paper in the Street, and somebody, not guided by the hand of propaganda, proved that he knew something of the money question. He hit it on one page, from the people, and they published it in four pages, which is the finest essay on the monetary system that I have ever read, and I have cracked the books for 25 years.

Doctor Miller told you he was against a commodity dollar, and his chart was an almost even line and level of commodity prices, during which period profits were not distributed but were used in speculation, in the wildest speculation that this country ever knew.

I want to devote a few minutes to Alexander Hamilton, because Alexander Hamilton is my best authority for the Nye-Sweeney bill.

Senator GLASS. Do you think so?

Mr. WARD. I do.

Senator GLASS. I noted that you failed to quote Alexander Hamilton in his statement that the ownership of a central bank should unquestionably be in private hands, and that if it should be in the Government's hands only a miracle could avert disaster. Have you that quotation there?

Mr. WARD. I am not quoting that one, Senator. [Laughter.]

Senator GLASS. Excuse the interruption. Go ahead.

Mr. WARD. That is perfectly acceptable.

I am quoting Alexander Hamilton on the money question. He wrote to Governor Clinton on May 4, 1783, favoring a central authority to gather the creditors of the central Government into a corporation of a central bank which would contribute "an increased circulation without which the people would be disabled from paying the taxes for want of the sufficient medium."

Gentlemen, we are suffering in this country from a paucity of money, and one of the distinguished members of this committee disagrees heartily with me, and says "Ward, we have practically the same amount of money in circulation today that we had during the last decade."

I beg to differ with the Senator, who has more money than I will ever dream of; but the fact is that we had 23 billion dollars in 1929, in demand deposits, in check-book money, in bankers' credit, pure fiction money, and 3 billion dollars of real money in the banks, behind which there was only 10 percent, under the law, in currency and reserve. This 23 billion was issued against a 10-percent reserve, and, of course, the securities that the borrower tossed in through the wicket.

Chrysler stock was selling at $3 under the name of Maxwell at the beginning of the decade and rose to 140. All any man in America did was to shove it through the wicket of a bank, accompanied by a promissory note, and get a dollar and a half in the early twenties or $70 a share toward the end of the decade.

He made a loan and was credited with a deposit. The security was there and against this security he was given the right to withdraw and twenty-three billions of this kind of money was issued by the private banking concerns of this country and existed in the form of demand deposits in the year 1929.

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That kind of money does 95 percent of the business of America and when that kind of money is withdrawn from circulation, when the private banks of this country call their loans, then the owner of that security must pay back to the bank not in the counterfeit check-book money, the fiction money of the banker.

The gold and silver and coin and bullion and Federal Reserve notes and Treasury notes and certificates, issued under the authority of Congress will be the only kind of money the bank will take in repayment of such a fiction-money loan.

The bankers of this country demanded the repayment of these promissory notes in cash, and the only way to raise cash is to sell the security.

It doesn't take a Federal Reserve expert, nor a banker, nor a monetary authority to explain to the people of this country what happens when deflation sets in. Chrysler stock was up from 3 to 140; General Motors from 15 to 150, with the stock split time and time again, and then was devaluated until both sold well below $10 per share.

The $22,000,000,000 of demand deposits in this country shrunk to $15,000,000,000. This was a shrinkage of over $7,000,000,000 in the actual money of this country, the credit money, the money which is in the control of the private banker.

When this type of money disappears there is only one thing for a nation to do and that is, replace it by actual money, if you want business to keep going.

Such a thought is considered radical; such a thought is considered inflationary; such a thought brings forth the press of the Nation with its special writers on the continental currency of our Revolution, forgetting that the Revolutionary Fathers won the war, and the only kind of money available was a pure fiat, irredeemable paper currency with nothing but the full faith and credit of the people behind it, and forgetting that the fathers were inspired to write the Constitution by Pelatiah Webster's pamphlet on a Central Bank.

Senator GLASS. Did they not win the war on the coin that France loaned us to pay our troops off, in order to get them to Yorktown?

Mr. WARD. Well, they had $7,000,000 of foreign money, and it was at 10 percent interest. It had a great deal to do with it.

Senator GLASS. But it was the first money that the continental troops had seen for nearly 2 years, was it not?

Mr. WARD. That is true, but they stood at Valley Forge with nothing but the paper, and Howe was in Philadelphia with the gold, and the two were competitive. There was luxury in one, with everything for the Army. There was no shortage of food. Howe ate, and he ate well, on the gold. Washington starved on the paper. I will admit that freely. But the point is that they used the only kind of money there was to use, pure fiat money.

Senator GLASS. I did not ask the question in a controversial sense.

Mr. WARD. I know that.

Senator GLASS. But in a historical sense.

Mr. WARD. And I would give full credit to the foreign loans, and also recall that it was 10-percent interest, and also recall that they were repaid.

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The writers in the newspapers and magazines of the country retell the story of the Confederate currency, as though the South had any gold or silver base to which they could attach currency. It issued in its hour of need the same kind of currency Russia issued after the revolution; the same kind Germany issued after the war; and the same kind that France issued after the revolution, and which every nation in the world will continue to issue if driven to economic destruction by the decimation of values through war or economic distress.

Gentlemen, we want to realize, if we are interested in this money question, that when you pick up the paper and get Andy White's book on French assignats, or the Saturday Evening Post, with the cartoons on the German marks and the rubles, and all the bunk on printing-press money, that they make no comparison in these instances with a nation that had billions of gold and silver bullion in a Treasury, free or unfree, 9 billions of it, against which 5⅓ billions are issued in this country.

Sometimes I sit in the gallery of the Senate and watch the proceedings with tremendous interest. I listen to discussions about rubles, French assignats, Confederate currency, and Continental currency. I do not think any of you gentlemen are guilty of passing bad checks, but I imagine that if death faced you and you thought you might be able to cover if you got a few miles away, you might issue a rubber check. These nations that were destroyed—France, after the revolution—issued the only kind of money there was to issue.

Senator GLASS. The South did not have any Crown lands, and did not seize all the church property as a basis of its issue of currency. That is what France had to start with.

Mr. WARD. That is correct. But is not that money always to be expected in an hour of need? There is no comparison with the country today.

Senator GLASS. It did not do much good.

Mr. WARD. No.

Senator GLASS. I used to play with band boxes full of it after the war.

Mr. WARD. The point I want to make is this: Money is not wealth. It is merely the means of wealth distribution, and it is the function of the Government to issue the money of a country.

Senator GLASS. Mr. Ward, let me clear up one point in my mind, if you will?

Mr. WARD. Gladly.

Senator GLASS. You are opposed to checking accounts?

Mr. WARD. No; I am not. I am coming to that point of 100-percent deposit. I believe money is not wealth, and it should not be confused. Therefore, as an attribute of sovereignty, the Government should issue the money. Private bankers have usurped the power of Congress to coin and issue money and regulate its value. The real money of the country today is the check-book money, doing 95 percent of the work. We had 22 billions of it available in 1929. We lost 7 billions of it in the depression. We have today uncontrolled credit money inflation, and uncontrolled credit money deflation, with the intellectuals of the country cursing printing-press money. We need

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to recapture, or reassert the congressional power over money. We need to take the function of issue away from the banks and put it in a central bank of the United States, which shall have the power over the money and currency of the Nation. This power over currency and money controls the lifeblood of the Nation. It is the means of the concentration of wealth into the hands of the few.

Senator GLASS. Mr. Ward, would it be convenient for you to come back at 2 o'clock, in the Appropriations Committee room?

Mr. WARD. Gladly.

Senator GLASS. The members of the committee have to respond to the call of the Senate.

Mr. WARD. Gladly, sir. Thank you.

(Whereupon, at 12 noon, the subcommittee recessed until 2 p. m.)

AFTERNOON SESSION

The subcommittee resumed its session, at 2 o'clock p. m., at the expiration of the recess, in the committee room of the Senate Committee on Appropriations, United States Capitol.

STATEMENT OF LOUIS B. WARD, DETROIT, MICH.—Resumed

Senator GLASS. You may as well proceed with your testimony. It is difficult to get all the Senators here on time. We will read it and examine it. Before you proceed, however, I want to hand a telegram to the official reporter from Father Coughlin, to be placed at the beginning of your testimony to supplement what you said about his inability to be present. Do you care to see it?

Mr. WARD. Yes; thank you, Senator.

(The telegram referred to and submitted by Senator Glass is here printed in full, as follows:)

ROYAL OAK, MICH., *May 28, 1935.*

Hon. CARTER GLASS: Deeply appreciate your letter of May 18, which was opened just this minute. Mr. Ward will testify for the National Union and is delegated to speak for me. Serious circumstances at home prevent my being absent for sometime.

Cordially yours,

CHARLES E. COUGHLIN.

Mr. WARD. To resume, the problem of production has been solved in America. Again I refer to the testimony of Dr. Miller, who shows by his chart that year after year the cost of production is and should be lower. Yet we find a condition where 59 percent of the wealth of this Nation is concentrated in the hands of 1 percent of the people; where 26 percent of the wealth of this Nation is in the hands of an additional 3 percent of the people; and where only 15 percent of the wealth of this Nation is distributed over 96 percent of the people.

Picture 100 men lined up in formation. One man carries 59 percent of the wealth, three men follow him carrying 26 percent of the wealth, and the 96 that follow have only 15 percent of the wealth.

Picture it another way—a little group represented by 300,000 families in America having an average wealth of $393,000. Then there are 900,000 families whose average wealth is $57,000. Then a third group represents 28,800,000 families, the teeming masses of labor and agriculture, with a total average wealth of only $1,042 per family.

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The Nye bill, S. 2162, attempts through monetary control to provide for the just distribution of the abundance with which the beneficent Creator has blessed us.

Senator BYRNES. What is the source of the information that you are now giving? Where did you get those figures from?

Mr. WARD. It is a combination of a study of income-tax returns on the one hand, together with statistics of the United States Government, in addition to the tremendous data selected with reference to the class that has nothing, out of the relief studies and the unemployment studies of the country. And when we say 59 percent, that is the best obtainable information that we have. Those figures are thrown with the figures of the National Industrial Conference Board of New York City whose figures are used by our Bureau of the Census; and the National Industrial Conference Board, Senator, has the only wealth census that I know of in the country. When I refer to the Census Department they in turn refer me to the National Industrial Conference Board. That is our stnadard source.

This bill attempts to restore to the Federal Government the control over all forms of money, over coin, currency, and credit. The Nye bill would take out of the hands of private individuals the power to inflate and deflate, and the power to value and devalue our national wealth. The answer lies in the proper distribution of our wealth by maintaining the purchasing power of money at a fixed and equitable level.

Our aim is to restore the value of property to just levels, and our bill likewise provides a means of regaining the lost billions of evaluation between the 200 billion we have today and the 488 billion of national wealth we had in 1920. It is the same property. It is revalued at the 200 billion.

Since 1760, the dawn of the industrial revolution, men have addressed their minds to the solution of the problem of production. That problem is solved—solved to the extent that men complain of surpluses. There are organisms high in the councils of this Government that would throw back into the face of the Creator the gifts He has given us. These men set about to destroy our real wealth in cotton, in wheat, in hogs and cattle, just as the private banker destroyed credit in 1929. These men refuse to develop the natural resources. They permit, for example, the St. Lawrence River to rush headlong and unharnessed to the sea, lest an abundance of power be developed, or economical access be available to our land-locked central West.

On the parallel problem of distribution of wealth, no effort is being made except by the Communists or by the Socialists, and by a handful of progressive minds who recognize that God blinds the eyes of reactionaries to the possibility of bloody revolution. In the literature of France no one predicted the French Revolution. In the literature of Russia no one of the old royalty dreamed of revolution.

To the true conservative, he who wishes to conserve the American heritage, the just distribution of wealth is wholly as important as its production. Literally millions of minds have contributed to the solution of the problem of production, and there are only 531 minds in all America directly charged with a true solution of the problem of the distribution of wealth. These are the Members of Congress who were given, under the Constitution, the power to coin money and reg-

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ulate the value thereof and of foreign coin, and who have permitted this power to go squarely into the hands of the private bankers.

I do not believe in panaceas, but I do believe that the money question is the most important question, the most momentous question of the hour.

I would like to quote Hamilton again. Hamilton was faced with the question of placing the taxing power in the hands of the States in the year 1787. He was faced in that same year with a foreign debt of over 7 millions of dollars, borrowed from Europe at 10-percent interest. Hamilton said, and I quote him:

> We are willing to grant the money but not the power required from us. Money will pay our debts; power will destroy our liberties.

These are good words to remember today.

The power over money when left in other hands, other than Congress, will and has destroyed our economic security. Hamilton knew the function of money. He said, and I quote him directly:

> The paper money of the State of New York in most transactions is equal to gold and silver; that of Rhode Island is depreciated to 5 for 1; that of North Carolina to 2 to 1; that of South Carolina may, perhaps, be worth 15 shillings in the pound.

In his speech upon the impost grant—and I quote from the Federalist—he said:

> The legislature having thought an emission of paper advisable, I consider it my duty as a representative of the people to take care of its credit. The farmers appeared willing to exchange their produce for it. The merchants, on the other hand, had large debts outstanding. They supposed that giving a free circulation to the paper would enable their customers in the country to pay, and as they perceived that they would have it in their power to convert the money into produce, they naturally resolved to give it their support.
>
> These causes combined to introduce the money into general circulation, and having once obtained credit, it will now be able to support itself.
>
> The chief difficulty to have been apprehended in respect to the paper was to overcome the diffidence which the still recent experience of depreciating paper had instilled into men's minds. This, it was to have been feared, would have shaken its credit at its outset; and if it had once begun to sink, it would be no easy matter to prevent its total decline.
>
> The event has, however, turned out otherwise and the money has been fortunate enough to conciliate the general confidence. This point gained, there need be no apprehensions of its future fate, unless the Government should do something to destroy that confidence.
>
> The causes that first gave it credit still operate and will, in all probability, continue to do so. The demand for money has not lessened, and the merchant has still the same inducement to countenance the circulation of the paper.

I picked up today a 10-dollar bill, national currency, secured by United States bonds, deposited with the Treasurer of the United States of America. Underneath those words it says, "or by like deposit of other securities. The Federal Reserve Bank, St. Louis. Ten Dollars."

There was a question asked of Mr. Morgenthau, the honorable Secretary of the Treasury: What other securities? It was asked by a United States Senator, the coauthor of this bill; and the answer of the Secretary of the Treasury was to the effect that it would be very difficult to find out what securities.

"Are Insull securities behind that particular note?" was the specific question; and the honorable Secretary answered that he could not tell except after an exhaustive survey.

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No one questions the circulating value of that 10-dollar note. What we question is that when Father Coughlin or the National Union goes before the people of the United States asking that Congress assume authority over the currency of the United States we find the private banking system that secures its currency by bonds of the United States on which the United States pays interest, and we find on one Federal Reserve note that this is redeemable in gold on demand at the United States Treasury, and we know that it is not. The rest of the sentence is " or in gold or lawful money at any Federal Reserve bank "; and there is an open public distinction on where you redeem that type of currency. That is redeemable in gold. There is no fiat money there. That is 100-percent gold redemption. If you walk into the Treasury or if you walk into the Federal Reserve bank, it is redeemable in another one of the same type—gold or lawful money.

Senator GLASS. The lawful money is redeemable at the Treasury in gold.

Mr. WARD. This [indicating] is lawful money.

Senator BULKLEY. It used to be.

Senator GLASS. I mean, it used to be, of course. I have stated all along that we are on a fiat basis now.

Mr. WARD. What we stand for is simply——

Senator BULKLEY. I do not see the point that you are making about that. Of course that is not good now; that redemption clause does not hold good.

Mr. WARD. But when it was good, it was good, Senator, in gold at the United States Treasury, and if you went to the bank it was good in paper money.

Senator MCADOO. If they chose to give you paper money.

Mr. WARD. But this is the redemption feature of this money. It is redeemable either in gold or in lawful money.

Senator BULKLEY. What is the point? I do not see what you are driving at.

Mr. WARD. It is redeemable. There is the idea of redemption to distinguish it from fiat money. The idea is that it would be redeemable in metallic money, gold and silver, to distinguish it from paper.

Senator BULKLEY. Of course, it used to be redeemable in gold, before we went off gold.

Mr. WARD. At the Treasury.

Senator GLASS. Or gold or lawful money at the bank. But the lawful money, in turn, was redeemable in gold. The reason for that, or the mechanics of the thing was, that banks did not care to carry so much gold. The Treasury had the gold. So they gave them lawful money, and if they wanted gold they could go and get it. I have no doubt they could have gotten gold at the banks, too.

Mr. WARD. There is no criticism of that whatsoever. The only thing we ask is that that prerogative of issue be recaptured by the Government of the United States.

Senator MCADOO. May I ask you a question now?

Mr. WARD. Yes, Senator.

Senator MCADOO. You say you want the prerogative recaptured?

Mr. WARD. Yes, Senator.

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Senator McAdoo. All money in this country is now issued by the United States, of course. It is a Government obligation to pay on demand the face of the note, either in gold or in lawful money——

Senator Bulkley. Except the national-bank currency which is about to be retired.

Senator McAdoo. But even that the Government of the United States is back of. It is secured with Government bonds back of it. Now, to what extent do you mean that the Government shall recapture the prerogative, since it is exercising its prerogative to issue paper money?

Mr. Ward. This morning, Senator, I tried to emphasize the fact that 95 percent of the money was not currency, but was credit money, deposit money, pure fiction money, that does the work of this country, and I have now gotten into this slight comment upon currency.

Senator McAdoo. You mean, bank checks? Is that what you are driving at?

Mr. Ward. Yes.

Senator McAdoo. Would you have the bank-check currency replaced entirely with Government issue of money?

Mr. Ward. Absolutely, 100 percent behind those deposits, secured precisely in the same way——

Senator McAdoo. I am just trying to figure out in my own mind how that can be done. I am only trying to develop your idea. When you take $100,000 of bank-check currency of the United States and use it in all business operations, how could you supplant that altogether with currency?

Would not that slow down business transactions enormously?

Mr. Ward. I do not think so, Senator.

Senator McAdoo. For instance, as it stands today, I earn my salary I hope. At any rate, the Government sends me a check. I deposit that in a bank. Somebody sends me a bill for a pair of eyeglasses, or some evidence of old age, and I pay it. Suppose it is $9.20. It is a very great convenience to me to be able to write a check for that amount and send it in the mail instead of paying it in currency.

Mr. Ward. I would not interfere with that for anything in the world.

Senator McAdoo. How would you supplant the bank check with currency?

Mr. Ward. In this way, Senator: That type of deposit through the wicket of the bank represents money in commerce and industry. We have no criticism; no attack. It is the normal, natural, economic, business way to proceed. But when the Senator deposits that money which he has earned, the thing that we object to is having that real money used as a 10-percent basis for the issue of credit out of a bank and to permit that bank to take that $10,000 and make it the basis of a $100,000 loan.

Senator Bulkley. Do you think banks ought not to loan money?

Mr. Ward. I certainly think they should lend, but I do not think banks should have the ability to create money.

Senator McAdoo. You mean the bank can borrow $100,000 from somebody?

Mr. Ward. No; I mean that they can create on the basis of your $10,000 cash a $100,000 loan and issue to anyone who hands them a

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promissory note and the proper security, Senator, against the securities of the borrower $100,000 in credit or check money.

Senator McAdoo. Provided, of course, they get the security for it?

Mr. Ward. I say, against security.

Senator McAdoo. The borrower has to supply securities that are satisfactory to the bank?

Mr. Ward. Yes.

Senator McAdoo. If he did not do that, what other method of getting money from the bank is available, if any?

Mr. Ward. The unsecured only. That is the real way that deposit money is created. It is money; it is real money issued against the securities of the people; and they usually charge around 6 percent for it. Ninety percent is created money. The Government does not participate in that creation; it does not provide for that type of credit. It is in private hands. It is a function of sovereignty.

Senator McAdoo. I may be dense, but I want to see if I can grasp your idea, of course.

Mr. Ward. Maybe I am abstruse.

Senator McAdoo. You say the bank can issue $100,000 of credit against a $10,000 deposit. Let us assume for the sake of the discussion that that is true. They can only issue credit to that extent, provided somebody borrows the money and because the bank accepted security for it, whether it be that man's personally endorsed note or collaterally secured note or what, so long as it is, in the judgment of the bank, a satisfactory security for the amount.

Mr. Ward. That is correct.

Senator McAdoo. The bank then lends you $100,000 and it goes to your credit in the bank and you can draw checks against that?

Mr. Ward. That is correct.

Senator McAdoo. If that process were not followed, how would the borrower otherwise be able to get the $100,000? I mean, how could the Government's intervention enable him to get it in some other way that would be satisfactory?

Mr. Ward. I am leading right into that directly as I go along, Senator. If you want the answer immediately——

Senator McAdoo. I think it would be well if you would just give it here in answer to the question.

Mr. Ward. The Government of the United States has floated already some 30 billions of bonds, and it has sold those 30 billions of bonds, though there never is over 6 or, at most, 7 billion dollars in actual money, currency, existing in the country. That 5 billion and a quarter, or 6 billion a while ago, is not in circulation.

Senator McAdoo. The currency is not?

Mr. Ward. No; we know that. We know that of $5,400,000,000 actual money in this country the banks themselves have about $670,000,000, approximately, at the last statement of the Comptroller or the Federal Deposit Insurance Corporation.

Senator McAdoo. Where is the rest of it?

Mr. Ward. The $670,000,000 is not in circulation and it is not loaned. It is till money. There is in the country approximately $1,000,000,000 in the hands of storekeepers. That money cannot be kept in circulation in the sense of not being needed for change and for day-to-day transactions. In another sense it is money that is in circulation, getting back to the bank and into the hands of the people.

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Senator McAdoo. It is bound to circulate.

Mr. Ward. We have in the homes of the people, roughly, another billion of dollars——

Senator McAdoo. On that point I am rather interested in knowing how you arrive at the amount that is in the homes.

Mr. Ward. You have the A. & P. in this country; and when I did a little work on that account they were doing $400,000,000 a year business. They were just coming up, doing a cash business with the home over the counter. There are 23 million motor vehicles running, and it is very difficult for even the distinguished Senator to drive from Washington to California without paying cash.

Senator McAdoo. I know that that is a correct statement.

Mr. Ward. That is one that is admitted. Credit is given some. Garfinckel, perhaps, with his trucks may have credit with a filling station. Maybe we can throw away three million as not doing a cash business. But here is an industry that has come up in the last generation. It did not need any cash expenditure for the horse and buggy. Twenty-three million of them, and the cash expenditure approximates $250 per year per car. Say that car goes 8,500 miles. That cash has a turn-over. It does not all stay in the hands of the gasoline station attendant, naturally. But those are the large items. New York City had a million transients a day in the last decade. The hotels in the country are doing a volume of $900,000,000, which is largely cash where I have been.

Senator McAdoo. How do you deduce from that that $1,000,000,000 is in the homes?

Mr. Ward. Because I approached it that way, and I approached it by labor and wages——

Senator McAdoo. You mean, it is just an arbitrary estimate of your own?

Mr. Ward. If you want to call it that way—an arbitrary estimate. I know there is five billion and a quarter of that currency. I know that you cannot find over $670,000,000 in all the banks of the country. Therefore $4,800,000,000 is outside the banks. Who has the $4,800,000,000? Foreign travel is one check on it Laborers, who do not have bank accounts—what they earn is another check on it. The service fee on bank accounts has reduced the number patronizing the banks.

Senator McAdoo. We know, in any event, that we have got more than four and a half billion dollars of currency in circulation in this country outside of the Treasury. We know that.

Mr. Ward. Five billion four hundred million.

Senator McAdoo. About 5 billion 300 million dollars of currency in circulation outside of the Treasury. That is what we commonly call circulation in the hands of the people, because it circulates among the people. I was just interested in your estimate of $1,000,000,000 as being in the homes. Of course if it is in the homes, unless it is hoarded, it is a part of the circulating medium.

Mr. Ward. I admit that.

Senator McAdoo. I do not yet see how you meet the question I asked upon which the discussion arose as to how you would supplant, through governmental intervention, the bank credits which the individual now procures, when the only way in which he can borrow

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money is to borrow it from a bank or an individual who has it or from somebody who has it——

Mr. Ward. They would issue currency.

Senator McAdoo. If they issue sufficient currency to do that, you would expect that the individual would borrow the money direct from the Government? Is that the idea?

Mr. Ward. No; I would not expect that. I would take the $30,-000,000,000 worth of Government bonds now in the country, which I think the distinguished chairman suggested, 60 percent of those in the hands of the banks, or $18,000,000,000 of United States Government securities on which the people are paying interest in the banks, to be used as a basis for the printing of enough currency to back the demand deposits in the banks 100 percent. There is no interference there with the check-book privilege. It is 100 percent reserves; and the function of that is to stop a bank taking your $10,000 in currency, actual money, and building it on the 10 percent reserve theory and principle to $100,000 check-book money, $90,000 of which was created by the banks and by the printing press.

Senator McAdoo. It was not created by the bank. It is created by a bank getting adequate security.

Mr. Ward. Absolutely.

Senator McAdoo. The extension of credit.

Mr. Ward. That is correct.

Senator McAdoo. What I am trying to get through my brain is how you are going to find a successful substitute for that method of doing business with a bank. I repeat, I am only trying to develop your idea so that I can grasp it. I am wondering how the mere issue by the Government of all this currency would affect the question of credit extension through a bank.

Mr. Ward. Well, if I have the securities and go to my bank with a hundred-percent deposit, the banker has all the ability in the world to grant me credit on those securities in the form that they then are. I may have a municipal bond—or no matter what it is, he has an endless supply for a long time to come of governments to turn into cash to back that type of loan.

Senator Couzens. Assuming that to be true, just what effect would that have upon the Government? If I approach a bank and offer them $100,000 worth of security, your idea is that they should give me $100,000 worth of printed money, currency?

Mr. Ward. Yes; certainly.

Senator Couzens. So instead of getting a check-book credit that you are talking about, I get $100,000 in Federal Reserve notes or Government notes, or whatnot. Just what difference does that make, so far as the effect upon the commerce of the country is concerned.

Mr. Ward. All right, Senator. We start with the year 1929, as an example, with $22,000,000,000 in deposit money. We have behind that deposit money $2,200,000,000 in currency, and, of course, behind that deposit money is the security of the borrower. That currency circulates in this country just the same as that type of money.

Senator McAdoo. You mean check currency?

Mr. Ward. Yes. A minor distinction. But there is 95 percent of the business of the country in this minor money. In 1929 the bankers decided on a contraction. The only thing they had to do

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was to call loans; but for every loan that is called an equal amount of money disappears out of circulation. For example, in the depression they called $7,000,000,000 worth of this check-book money. They reduced the currency of the country precisely $7,000,000,000.

Senator McAdoo. You mean the check-book currency?

Mr. Ward. Surely; the money of the Nation, check currency, credit money of the Nation. That had the effect that everybody in this room is conscious of and that the automotive industry can chart, as I showed the committee this morning, the collapse of business; that some banker can at a predetermined date decide to extend credit and take in securities, and against those securities grant the right to withdraw; and that right to withdraw is the basis of this check-book money once again.

If the banker in 1929 decided to contract, he has not only his capital and surplus that were put into the business, he has had also the currency that is deposited, and against those three items he has predicated 22 billions of check-book money.

There never was $22,000,000,000 in this country. What we would like to do, of that hundred-percent deposit, is to have that banker who owns $18,000,000,000, perhaps—and that is the Senator's figure the other day—of United States bonds, coupon interest-bearing tax-exempts—take them and turn them in for the issue of currency against them.

Senator McAdoo. You would retire the bonds by issuing currency; is that the idea?

Mr. Ward. Yes. That money does not go into circulation. It goes into the banks.

Senator McAdoo. If you issued $18,000,000,000 of currency and retired an equal amount of interest-bearing bonds, of course, the currency would not bear interest?

Wr. Ward. That is correct.

Senator McAdoo. If you did that, you say the currency would not go into circulation?

Mr. Ward. It would not. It would replace security that is there today. That hundred percent deposit would be just stepped up, the cash reserves, from 10 percent today to 100 percent then.

Senator McAdoo. All right.

Senator Bulkley. That would make the hundred percent reserve all right, would it?

Mr. Ward. Yes.

Senator Bulkley. Loans outstanding are only about $18,000,000,000 today?

Mr. Ward. Yes. The deposits dropped from 22 to 15.

Senator Bulkley. What about the loans?

Mr. Ward. Those are the demand deposits. They dropped from 22,000,000,000 to 15,000,000,000 in the depression. We lost seven and a fraction billion dollars.

Senator Bulkley. Are you talking about all banks or national banks?

Mr. Ward. All the banks in the Federal Reserve System. We built deposits, including time deposits, to $58,000,000,000 in 1929. We have got the same wealth in this country, and we devalued everything and destroyed that money, and we are where we are.

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Here we have an individual bank, a member of the Federal Reserve System, permitted under our law to create money, check-book money, and a 10-percent reserve system. An individual member bank in time of depression has orders to go to the Government of the United States and seek relief from the R. F. C. In turn the R. F. C. loaned to the banks in this country nearly $900,000,000 in capital subscription, loaned in the form of subscription to preferred stock and aside from any loans of the assets of these banks.

We have the Central Bank of the United States of America. It is the Reconstruction Finance Corporation. It is limited to the function of loans. It has bailed the railroads out of bankruptcy; it bailed the banks out of bankruptcy and the insurance companies out of bankruptcy. Over in another department we have the Comptroller's Office with its power of regulation and examination of national banks. We have the Federal Deposit Insurance Corporation; and if I heard correctly before I went on the stand this morning I heard a banker ask this committee to reduce or to waive insurance of deposits for a couple of years, so the banks could——

Senator McAdoo. To reduce the payment of premiums for a year.

Mr. Ward. To one-twelfth or one-eighteenth for a year. We have the Home Owners' Loan Corporation, and we have the Federal land banks and endless governmental banking functions. Over in the Treasury we have nine billion in monetary stocks, and we still have the Constitution and we have the power of Congress coining and regulating the value of money. There is no reason in the world why we cannot combine all of that into a central bank.

With those rather extended remarks I want now to discuss the Nye-Sweeney bill.

The bill creates a central bank, known as the Bank of the United States of America ". Section 2 makes this bank the agency of Congress, with the function of issue and the function of controlling the value of money and the value of foreign moneys, as is directly outlined under the Constitution as a power of Congress in section 1, article VIII, clause 5.

The bill places the sole jurisdiction over the monetary stocks and moneys and the public credit of the United States in the hands of this bank. The bill makes this bank the central depository of all reserve funds of all banks under the jurisdiction of the United States.

The bill makes the bank the fiscal agent of the United States Government, and since the drafting of the bill the circulating-note privilege of national banks having been repealed, the sentence may now be omitted—the last sentence in section 2.

Section 3 attempts to set up an independent Board of Governors for the Bank of the United States. The committee has heard the testimony of Dr. Adolph Miller to the effect that pressure from two sources is continuously evident in the management of the Federal Reserve System.

In response to the request for information on the part of the senior Senator from Michigan, Dr. Miller suggested an executive session of the committee so that he might reveal the facts respecting the pressure from New York in times of inflation, and from the Treasury in times of deflation.

The public may well understand pressure that comes from New York, though the details are obscured in the manipulation of the

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money and credit of this country by the New York bankers and the members of the Federal Reserve Board, but political pressure from the Treasury of the United States on a Federal Reserve bank, generally in times of deflation, is little understood by the people. The fact that it exists along with the pressure from private banking interests makes one thing obvious—there is needed an independent board of directors of the Central Bank of the United States, free alike from the pressure of political influence and free from the domination of the New York bankers.

May I say here that I have no sympathy with the philosophy so current in the press of the Nation nor in the philosophy of the Manufacturers Association or the United States Chamber of Commerce or the American Liberty League or the American Bankers Association, that Government should keep its hand out of business.

The sovereign power to tax puts the Government into every business in the Nation. Business has come to Washington since the year 1818 at least, and from 1832 continuously, in behalf of protective tariffs for business.

The greatest banker in America was interested in government, as he secured our entrance into the World War for the protection of the credit of Great Britain whose fiscal agent he was.

The building industry wanted a housing act; the textile industry desires to shut out Japanese goods; the American match industry wants to compete with both Europe and Japan. Not only business but labor wants the Government to step in, and agriculture wants the Government to step in or out. The point is that this special please against Government activity is always on the part of those who profit most if left unregulated and to their own devices, and this is the case with the private banking interest of America who only exist because there is an R. F. C., the Government Central Bank today, which has bailed them out of difficulty.

The Nye-Sweeney bill attempts to set up an independent board, and for independence this board is modeled after the Senate of the United States, with equal representation from each State. The true wealth of this Nation is distributed over 48 States, but the concentration of money and credit is in the great banking centers of the country.

If the Congress of the United States truly seeks to divorce the power of money and credit from the great financial centers of this country, which have brought us where we are, one key is found in recognizing that banking is a service, and money is a method of wealth distribution, and money under our present private reserve system becomes the basis of credit, and the allocation of this credit follows the money reserves.

It is well to have on the board of directors of this Central Bank of the United States men who know the economic resources, the industrial situation, the labor situation, and the agricultural situation in every one of the 48 States, and we have suggested a board of 48, one from each State, elected for a period of 12 years, and upon election to be divided into classes so that one-sixth retire every 2 years. We have taken our language directly from the Constitution of the United States, as that Constitution originally set up the Senate of the United States. This is a board of directors elected

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by the people. It is this method of choosing the electors that will undoubtedly come under the attack of the enemies of this bill, or perhaps friends of the bill.

You will hear immediately that it is unconstitutional. You will hear that Congress cannot delegate any power to an elective board. You will hear that the President alone has the appointive power, by and with the advice and consent of the Senate.

You will hear immediately these criticisms, that the Senate is well supplied with great constitutional lawyers. The opinions of two of them were solicited, and they both suggested that they thought the plan was constitutional. It is merely, however, an attempt to secure independence; and perhaps a more certain way is to provide for the appointment by the President, by and with the advice and consent of the Senate, of one member from each State, trusting that only one-third will serve during any one administration. A board of 48 is not a large board. There are over 100 directors of the 12 Federal Reserve banks today. There are 531 Members of Congress theoretically legislating on banking, and over and above these regulations the Federal Reserve Board; and then there are 2,500 members of 48 State legislatures with authority over State-chartered banks; and the commercial State bank is just as much a party to check-book counterfeit currency as the national bank is.

In other words, gentlemen, we have over 3,000 minds with authority over banking in this country, and this bill aims at reducing that number to 48 directors of the central operating bank.

I will not pause at the details of salary, except to say that if the Board is to be independent its personnel must be rewarded; and, as Dr. Miller says, the career of banking must be the aim.

The Nye-Sweeney bill provides for the divorcement of the directors from all industry and financing, and the bill provides a liberal pension after 70 of $1,000 a year for each year of service as a director, up to a maximum of $12,000.

The board of directors under the Nye-Sweeney bill elects an executive committee of 7 to an executive board of the bank, and then the entire board of 48 appoints a president and vice president and other executive officers, examiners, economists, and banking experts as may be needed. The principal office of the bank would naturally be Washington, D. C., with branches in each of the several States.

Section 5 of the bill provides that all the currency of the United States shall be the issue of this central bank.

The senior Senator from Ohio asked Dr. Miller repeatedly for an expression of his opinion why the Government of the United States should not own the Federal Reserve Banking System. This question had been asked before of others by the committee. The question has been repeatedly dodged by such answers as: "Ownership is not important; it is the control, the administration, the men, that are important."

Certainly there is a profit in the Federal Reserve System. Originally Congress provided that 6 percent be paid and that a dividend be cumulative with all excess profit split 50–50 between the Government and the surplus of the Federal Reserve banks. The Government's share was in lieu of franchise tax. The act of 1933 amended this provision and put all profit over and above 6-percent cumulative into a surplus fund for the private bankers.

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There is a hidden profit that goes with every right of issue to any bank.

When France called her currency in to revalue it, out of 81,000,000,000 francs, 20,000,000,000 had been lost.

What happens when a *Lusitania* sinks or a *Titanic* goes down at sea?

What happens when Chicago burns or San Francisco has an earthquake?

What happens when the Dillingers hide their loot and then are shot down?

Or the feeble-minded throw hoarded currency into the stove?

The hidden profit from lost money was approximately 20,000,000,000 francs in France or one-fourth of the total currency issue.

With $5,400,000,000 in currency supposedly "in circulation" in this country, the lost item alone would more than pay for the Federal Reserve bank stock, and if the truth were known the banks that own the stock—those of them that are now in receivership—may be found to be owing Jesse Jones far more than its face value today.

Section 8 provides for the purchase of the capital stock of the 12 Reserve banks and branches and agencies at the paid-in value of stock and 6 percent per annum interest from last dividend period. The section further provides the full and complete and absolute and unconditional ownership of the Federal Reserve banks in the hands of the people of the United States.

In answer to the question asked previous witnesses, may I call to the attention of the committee that the witnesses have merely emphasized that the important thing was the Board and not the ownership, and if the ownership is deemed not important, why then there is no reason whatever not to vest it in the hands of the people of the United States.

Section 10 declares that all banks doing a commercial banking business within the United States, all banks which have demand deposits, to be engaged in interstate commerce and subject to Federal jurisdiction; and section 10 bring these banks within the central banking rules and regulations.

There are many very thoughtful men who sincerely believe that the banker of this country cannot absorb many more billions in Government securities. They foresee proximate catastrophe in a 5- or 10-point drop in Government bonds.

They realize that such a 10-point drop in bond prices would bankrupt every bank in the United States should not the R. F. C. come to their rescue with a billion or more in additional loans.

Thoughtful men realize that further Government aid of this kind will destroy private banking in this country.

So the central banking principle and the issuance of currency to retire the Government debt take on a different aspect in the light of the present crisis. Central banking and expansion of the currency in the minds of many thinking men provide the only salvation for private enterprise in our capitalistic nation.

In this light, too, the interstate commerce clause, which by inference in recent Supreme Court decisions has been made to appear as a menace to free individual enterprise, appears as the one avenue to setting up a national control of banking which well may become the sole safeguard of private enterprise in the field of banking.

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Clause b of section 10 writes into the bill the 100-percent reserve principle. In other words, it provides that every bank shall keep on deposit in the bank of the U. S. A. notes to the full 100 percent of demand deposits. It is this provision alone which builds the competitive monetary system to that of the United States of America. It is this provision that is just as important at this time as it was in 1862 to tax out of existence the circulating privilege of the State chartered banks.

It is this provision that requires that demand deposits shall be held in trust for the benefit of the depositors and not merged with or become a part of the assets of the bank, thus leaving the depositor a creditor, as the law leaves him today. It is this provision that reverses the whole theory of modern demand-deposit banking and permits a new day, where banking becomes what the people think it is, namely, a place to deposit your money and to withdraw it when one wants to; a place where money may be deposited and the title to it transferred by order, not merely the creation the lawful money reserve required against credit money.

Clause c of section 10 provides that the Central Bank shall purchase part of the debt of the United States and other public debt, and against it issue currency to the amount of the demand deposits of the country. The public debt at the end of this fiscal year will be approximately 34 billion dollars; the State debt is approximately two billion and one-half; the municipal and local Government debt is approximately 20 billion dollars.

Congress has lately authorized the United States debt to go as high as 45 billion. One of the greatest questions facing this Nation is, Who owns the debt?

The individual and the corporation are most solicitious about their creditors.

The committee knows that the banks of the country own 60 percent of the present United States Government debt. We know that insurance companies, endowment funds, schools, and universities own other billions, but a great question facing the country is, Who owns the remaining billions of United States Government bonds that are tax exempt, the ownership of which must be the source of opposition to many of our legislative policies—for example, the bonus. It must be the source of opposition to any expansion of the currency; of opposition to any central-bank idea or other so-called "inflationary measures"; or the opposition to the use of silver; or lower interest rates on farm mortgages; or any monetary or banking reform whatsoever.

This bill provides a use for Government bonds and a market for the Government bond, and permits the central bank to own a large percent of the United States debt and against it issue currency, not for circulation but to be placed in the vaults of the member banks, dollar for dollar behind every dollar of demand deposits.

With regard to the regulation of the value of money, section 11 of the bill permits the Bank of the United States to buy or sell gold, silver, and foreign exchange in the financial markets of the United States, and this power is granted to the central bank, as the agency of the Congress of the United States, in order to carry out the constitutional provision incorporated in article I, section 8, clause 5, "to coin money and regulate the value thereof and of foreign coins."

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Section 12 puts supervision under the control of the central bank and puts the Comptroller of the Currency under the authority of the central bank.

Section 13 provides that the central bank shall have the full statistical data essential for a sound monetary system.

How do we find the cost of living today? We go to the Bureau of Labor Statistics. What do they know about it? Why, in 1918 they made a study, and the 1918 study is corrected from year to year by use of index numbers. It is passed on to every governmental department, it is used by the American Federation of Labor.

The basic statistical information was gathered 17 years ago, in the interval we have had 2 panics and 4 administrations. It is rumored they use over 700 commodities in establishing the price level, and the American people are so impoverished that the 96 percent of them who average $1,000 of wealth per family don't participate in 70 commodities, much less 700.

The central bank should have all the facilities for obtaining and compiling authentic data without depending upon politically appointed department heads for such vital information. If there were an independently controlled central bank today, free from political interference on the one hand, free from the private banking influence on the other, and a Senator or a private citizen wanted to know what was contained in the Dr. Beckman report, paid for by the people's money that Senator could have access to that report before it was politically doctored and then even suppressed to deny to Congress the truth.

Section 14 provides a mandate on the central bank to secure stable purchasing power of money on an equitable price level. The Republicans in 1920 placed in their platform the pledge to reduce the cost of living. They did it—they fulfilled their pledge; they withdrew from the circulating medium of the United States $1,900,000,000 in the 18 months that followed the inauguration of Mr. Harding, but they were not content with this. From February 1, 1921 to April 1, 1921, the demand deposits of the banks of the country were reduced $627,934,000.

The committee heard the testimony of Dr. Miller. And by 1923, when conditions had been built up considerably after 1921, the Federal Reserve feared prosperity and its open market depressed things for 1924, and that is reflected in that automotive industry study.

In 1927 it was time to rig the great bull market. The farm had been depressed since 1920; the building industry was shot from 1926 on, but with great production, together with modern efficiency, the price level could be kept low and the huge profits were directed not to the payment of a just and living wage for labor, not to the return of cost of production to the American farmer. They were poured into a speculative market and we boasted of bank deposits of 58 billion by 1929.

The banker was controlling the Federal Reserve Board in that period of inflation and it was left to the Treasury to influence that Federal Reserve policy in the period that followed. Why, the Government itself was induced to borrow itself out of trouble by the issuance of tax-exempt bonds, so that a debt which after the war had been reduced to 16 billion, which during the war was never over

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26 billion, is now, at the end of the fiscal year, 34 billion, and permitted to run to 45 billion.

Section 14 provides suitable purchasing power of money by permitting the central bank to purchase the debt of the United States until there are 100-percent reserves behind demand deposits; and lest our fiscal policy be predicated upon debt, the central bank may control the price level, if necessary, by paying extraordinary and then the ordinary expenses of Government by currency issue until the average commodity price level reaches the index of the Bureau of Labor Statistics for 1926. Then the board of directors is charged with determining a true and equitable commodity price level and to regulate the volume of the currency so as to maintain such a level.

In the present Federal Reserve Act there is provision for the issuance of currency 2½ times the gold reserve. The United States Treasury has 9,000,000,000 of monetary metal in its vault. This can support, unchallenged by any modern banker who has supported the privately-owned Federal Reserve System—this 9,000,000,000 can support the currency issue of $23,000,000,000.

This is not fiat money; this is not an irredeemable paper money; this is not any more printing-press money than is any Federal Reserve note ever issued mere printing-press money.

Senator BULKLEY. Would it be redeemable in gold?

Mr. WARD. The same as your Federal Reserve notes.

Senator BULKLEY. Federal Reserve notes are not redeemable now.

Mr. WARD. No.

Senator BULKLEY. Your money would not be redeemable?

Mr. WARD. I am just showing the possibility of that metallic base under the Federal Reserve principle of 2½ to 1.

Senator BULKLEY. But the Federal Reserve principle was to have it redeemable in gold.

Mr. WARD. Yes.

Senator BULKLEY. Of course that has been departed from.

Mr. WARD. Yes.

Senator BULKLEY. You do not adopt the principle of having it redeemable in gold at all?

Mr. WARD. No; nor do I recommend the 23 billion. I simply say that there is the bullion base, and there is the principle of the Federal Reserve, and that with the two, I say that any man who shrieks "printing press money"——

Senator BULKLEY. Let us see if you do not recommend the 23 billion. Did you not say that it would take about $18,000,000,000 to take up these bonds?

Mr. WARD. Yes.

Senator BULKLEY. And there is about 5 billion out already?

Mr. WARD. Yes. That comes to 23 billion.

Senator BULKLEY. And you do not recommend that?

Mr. WARD. Wait a minute. This 18 billion is not in circulation at all.

Senator BULKLEY. I understand that.

Mr. WARD. Fine; if you understand that 18 billion is where it is; absolutely, yes; I will recommend 23 billion.

Senator BULKLEY. And as much more as needed?

Mr. WARD. Certainly, for that commodity price level of 1926.

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Senator BULKLEY. Do you have to stop printing currency when the commodity price level changes?

Mr. WARD. Yes; until you finish your new study, Senator. This arbitrary 1926 level is accepted all over the country, on 1918 figures. We want the central bank to study the commodity price level, the relationship to debt, private debt, and the volume of business done. Do not go over to the Department of Labor and pick out a study of 1918, 17 years ago, with a series of index numbers, and look at the year 1926 and say to America, "Thus far you can go, and no further." I do not know where it should be. I only know that the study should be made, and I predicate that solely upon the fact that we had a study.

Senator BULKLEY. Do you favor buying any other Government bonds except those that are in the banks?

Mr. WARD. Yes. I am coming to that right this minute.

Senator GLASS. The $23,000,000,000 to which you refer, and vastly more than that, is available now if business revives and business interests demand it, isn't that true?

Mr. WARD. There is an unlimited amount available to them in check-book money of the private bankers, credit money.

Senator GLASS. Aside from that, counting the gold reserve, and counting that extraordinary provision of the law which returned us to a bond-security currency, a vast number of billions of dollars are available if business should revive and demand it.

Mr. WARD. Of course, the only thing I cannot say yes to is "if business revives." Yes; if business received the credit that it needed there would be use for vast numbers of billions of dollars which are available under the present credit system.

Senator GLASS. I would not have put it that way—if business received the credit that it needed. Well, yes; the credit that it needs. I would accept your phrase. But not the credit that it desires.

Mr. WARD. I would not urge that. With regard to the Beckman report, I pestered six Senators to get that Beckman report.

Senator COUZENS. Tell us what that Beckman report is.

Mr. WARD. Dr. Beckman, of Ohio.

Senator COUZENS. What did he do?

Mr. WARD. He came down and used the people's money in the Bureau of the Census to get a survey of the needs for small industry for credit.

Senator BULKLEY. Did you get the report?

Mr. WARD. Never. I do not think the senior Senator from Michigan would object to my making this statement: They sent two guards over to the office of Senator Couzens with it finally, with the statement, "What do you want it for? We cannot release it."

Dr. Beckman is a fine scholar. He went out and got these facts, and the facts were bad for the "new deal." The people spent their money. The New York Times printed the conclusion, which was released by somebody who made a mistake in the Department, the day the report was out. We can get the conclusion. They will give you those 20 pages. The nearest we ever came, through the efforts of six distinguished Senators, was to get, under guard, a report brought into Senator Couzens' office, but he could not copy it. He could look at it.

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Senator BULKLEY. Do you know what it shows?

Mr. WARD. Yes; it shows that small industry had piled up in orders, good orders that they could not fulfill for lack of credit, a demand for $2,000,000,000 worth of credit not available from a private bank in this country, and not available from the Reconstruction Finance Corporation.

Senator BULKLEY. About what date was this?

Mr. WARD. I came down in January, and I would say approximately the first of February. Then they went over the report and doctored the report, Senator, to change some of it. Then they released the statement that it was released prematurely by a clerk. The trouble with the report is that it was the truth.

Senaor GLASS. Who are "they"?

Mr. WARD. Roper's department—Dr. Roper, or whatever should go with it for the record. That report is just unavailable, and there is a bill covering that, to try to bring it out in the House. Representative Kopplemann, of Connecticut, has introduced a bill. We had the same thing in Michigan, with the Reconstruction Finance Corporation. We set up 36 agencies, and I had a request to try to get $10,000 back from the Reconstruction Finance Corporation, privately subscribed in Detroit, Mich., for the industrial-loan department. The Reconstruction Finance Corporation wired the Chamber of Commerce of the city of Detroit, Mich., to gather together a good board to study loans to industry, and to loan the Government money. Certain men threw $10,000 in there. They elected a good business man, I guess—Mr. J. Walter Drake—head of it, and they collected applications for millions of dollars' worth of loans to small industries, and among those industries was the Detroit Steel Products Co., with United States Government orders on its books, and no money to manufacture. They took these applications for loans over to the Government-owned bank in Detroit to see if they were good banking risks. Those that were approved they brought down to Washington. After spending $16,000 of private money in the city of Detroit, it was decided that there was no money out of the Reconstruction Finance Corporation for small industry.

Senator BYRNES. What was the $16,000 spent for?

Mr. WARD. Office expenses and investigation.

Senator COUZENS. Who decided that there was no money?

Mr. WARD. The Reconstruction Finance Corporation, Senator.

Senator COUZENS. Is there a record of that decision anywhere? I never saw it.

Mr. WARD. I have a file on it. I came down twice, Senator, to see if we could get any action.

Senator BULKLEY. The Reconstruction Finance Corporation claimed that they could not get applications for good loans.

Mr. WARD. Dr. Beckman, of Ohio, Senator, is the best man to answer that. He found excellent loans where they needed $2,000,000,000 to start industry on orders that were in.

Senator BULKLEY. Did he find specific cases where the Reconstruction Finance Corporation had refused to go along with them?

Mr. WARD. Yes; and with the Reconstruction Finance Corporation, the private bank.

Senator BULKLEY. What is that?

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Mr. WARD. And also the private bank. It was a complete picture. His report is a very fine report.

Senator BULKLEY. I would be interested to see it.

Senator COUZENS. Do you know him?

Senator BULKLEY. No; I do not know him.

Mr. WARD. Senator, I would be more than interested in having you see it. I want to see it. I cannot see it. Senator Couzens came nearer getting it than anyone. He got it inside his office.

Senator BYRNES. What you mean, Mr. Ward, is that this report covered cases where this gentleman said that certain corporations had applied to banks and could not secure loans and then applied to the Reconstruction Finance Corporation?

Mr. WARD. And could not secure loans.

Senator BYRNES. And could not secure loans.

Mr. WARD. And business was halted for the lack of money.

Senator GLASS. Mr. Ward, what do you think banks are in business for?

Senator BYRNES. The question in each case presumably depended upon the judgment of the banker and the Reconstruction Finance Corporation officials as to the collateral offered.

Mr. WARD. That is correct.

Senator BYRNES. You do not know anything about the collateral offered to the bankers or to the Reconstruction Finance Corporation?

Mr. WARD. Oh, no.

Senator BYRNES. That is what you would like to know.

Mr. WARD. Oh, no; I do not know that, and I do not know the details of the report. I have the 20-page summary. The New York Times published that.

Senator BULKLEY. You would presume that detail would show in the report?

Mr. WARD. Oh, yes. That is the report, and they have used Dr. Beckman's study.

Senator GLASS. I just asked the simple question, what do you think a bank is in business for except to lend money on sound collateral security?

Mr. WARD. There are other minor incidental objectives of a banker. The Senator knows far more than I will ever know about it. They do not just go into the business of lending money on good security.

Senator GLASS. I thought they did. I thought that was what they were chartered to do.

Mr. WARD. I know; but that would not account for some of their activities in calling loans on good security, knocking the market down, or raising a bank stock to $1,200 or $1,400 a share, from $200. We had many objectives of Michigan bankers.

Senator GLASS. Of course, if they are in the stock-gambling business or the securities-gambling business they would do things of that sort. I am talking about legitimate banking.

Mr. WARD. I am from Michigan, and it is a very difficult thing to have any exact information on that subject in the last few years.

Senator GLASS. You do not think there is any legitimate banking out there?

Mr. WARD. There is some. We have a few old savings banks.

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The United States Treasury has nine billions of monetary metal in its vault. This can support—unchallenged by any modern banker who has supported the privately owned Federal Reserve System—this nine billion can support the currency issue of $23,000,000,000.

This would not be fiat money. It would not be irredeemable paper money, nor printing-press money, to any greater extent than the Federal Reserve notes issued today.

Senator BULKLEY. What would it be redeemable in?

Mr. WARD. Senator, this 2½ to 1 should be used with the full recognition of its historic significance. The goldsmiths of Europe learned that their customers did not come back the same day, and they were smart individuals. They figured out a percentage, and if they had enough to meet those that did come in for their gold, with the gold receipts, that was sufficient.

Senator BULKLEY. That is very familiar to all of us, but what I am trying to get at is what you are proposing in this bill. You just said it would not be irredeemable paper; and I am asking you, if it is not irredeemable, what would it be redeemable in?

Mr. WARD. I did not say it would not be irredeemable, Senator.

Senator BULKLEY. I misunderstood you, then.

Mr. WARD. I said it would not be any more irredeemable than the present Federal Reserve notes.

Senator BULKLEY. It could not be any more irredeemable than the present Federal Reserve notes.

Mr. WARD. I was just comparing them. I will stop there.

Senator GLASS. It could not be any more irredeemable, and the probability is that they would not finally put you in jail if you were caught with any of it. But if you are caught with any gold now, they would fine you and put you in jail.

Mr. WARD. This merely means giving the sovereign power of the United States the same prerogative that the United States gave the private banker in 1913. But lest the purchase of the debt of the United States and the issuance of currency to equal demand deposits provide some physiological reaction in anticipation of higher prices, though such action puts not one penny of money in circulation, and lest further issues of currency raise the price level above that prescribed in section 14, then Congress can retire all excesses of currency through taxation.

Mr. Warburg came before the committee to testify that no government would have the courage to stop a boom. But Mr. Warburg didn't complete the most important thought for the people of the United States, and that thought is this: That no government would have the courage to start a depression.

I am not here for or against the Eccles bill. I do not believe that the committee invited a hearing on this bill at this time, as a means of killing the Eccles bill.

You have here the testimony of the Secretary of the Treasury that he is of that school which believes in a central bank. You have Mr. Eccles himself, presenting a bill to Congress while he needed confirmation as Governor of the present Federal Reserve Board.

In the consideration of the Nye-Sweeney bill, naturally we can't get the bankers of the country to come here and testify in favor of

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it. It will be universally ridiculed, and, as it gains public respect, the attitude will change and it will be tolerated, and then there will occur that third phase, which Woodrow Wilson said was the fate of every reform measure. It would be embraced with a view of so manipulating it that there would be no reform possible.

I would as soon ask the Egyptians to go easy on the slaves in the matter of making bricks as I would ask the bankers of America to endorse this bill. I would as soon ask Caesar to emancipate the galley slaves as I would ask the modern banker to give up the privilege of counterfeiting money.

I would as soon ask a feudal baron to permit his serfs to transfer land in fee simple as I would ask Wall Street for an objective consideration of this bill. The bill is drafted, and it will follow the course of all legislation which passes, and that is modification.

This Nation has waited upon Congress since 1789 to use the power given it under the Constitution to coin money and regulate the value thereof and of foreign coins.

Through the medium of the radio and through great public mass meetings, the people are being informed, and the people ultimately win every battle they set out to win.

It took 6,000 years before human slavery, man's ownership of his fellow man, disappeared.

It took 9 centuries at least of recorded history before the Constitution of the State of New York finally abolished the feudal tenures which had lasted down from the old Dutch patroon of the rent wars of 1842.

It took from 1765, with the Stamp Act, to 1781 at Yorktown to give us political independence, but they didn't have the radio in those days, and they didn't have the telegraph.

We ask that this subcommittee, which is being pushed to bring out a banking bill, substitute the Nye-Sweeney bill for the Eccles bill, and you will need no deposit insurance; you will need no political control over banking, and you will have no private banker control over money.

I ask the sincere and honest deliberations of this committee, according to its intellectual lights, before the four billion eight hundred million is added to the national debt; before there is a possibility of the Government bond market breaking and the banks forced to run again to Jesse Jones to bail them out.

I want to thank the committee again for the courtesy extended Father Coughlin, and that courtesy will be acknowledged to the millions who listen to him.

I should like to offer for the record an analysis of banking and money by the New York Herald Tribune.

Senator GLASS. That may be done.

(The matter referred to is here printed in full as follows:)

AN ANALYSIS OF BANKING AND MONEY BY THE NEW YORK HERALD TRIBUNE

In 1933 the New York Herald Tribune published a little book of 60 pages entitled "The Financial Section of a Newspaper."

The book was edited by Mr. C. Norman Stabler, financial editor, and additional copies are advertised as available for $1 each by addressing the New York Herald Tribune.

The book was obviously prepared for the advertiser, because in a foreword, under the title "Preference", we learn that 66 percent, or 658 out of 994

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members, of the New York Stock Exchange who responded to the question, "What morning New York newspaper do you read regularly?" mentioned the New York Herald Tribune, while 65 percent reported that they read the Herald Tribune among Sunday newspapers; all of which is prepared as proof of a substantial preference over other newspapers, both week days and Sundays.

In the introduction to this book, I find the following language:

"Students in schools and colleges, many of whom have had no immediate contact with the financial world and consequently are not thoroughly acquainted with Wall Street parlance, are realizing the necessity of becoming better versed in the ways of those institutions in lower Manhattan from whose rooms are directed the flow of credit and commerce to all sections of the globe. It is for this latter group, principally, that this elementary discussion on how to read the financial pages is published."

On page 25 there is reproduced a portion of an article entitled, "The Week in Finance."

The author, Mr. Edward H. Collins, associate financial editor, bemoans the fact that the American Bankers' Association in their 1933 Chicago convention should have held a "concerted demonstration against the administration's banking heresies, and should have put forth an appeal to sound public judgment against the attempt to sabotage the banking system."

But Mr. Collins laments the fact that the bankers made nothing of their opportunity, for the administration stole their thunder by sending Jesse Jones, Eugene R. Black, and James F. T. O'Connor to capture the headlines.

THE BANKING SYSTEM FOUNDED ON TRICKERY

On the next page, page 26, Mr. Collins describes "Our Monetary System."

In the opening sentence, his topic thought is: "The modern banking system exists primarily to provide and regulate the supply of money."

The Constitution of the United States, article I, section 8, clause 5, places this power over money directly under the Congress of the United States.

Mr. Collins, in his article, distinguishes three kinds of money: "real money, representative money (or currency), and deposit money (or credit)."

With respect to currency, in a few brief sentences, he traces the origin back to the goldsmiths of Europe and what he calls the epochal discovery of those goldsmiths to the effect that the holders of their receipts never wanted their gold at the same time. So the dishonest practice of issuing receipts in excess of the amounts of bullion on deposit, and the lending out of these excess bank notes at interest, Mr. Collins terms "The foundation of the modern bank-note issue."

It was the greed for interest on these notes, unsecured by bullion, that lead to abuses so bad that most countries started the supervision of the privilege of note issue.

RULES FOR AN ELASTIC FORM OF CURRENCY

Mr. Collins then explains the Federal Reserve regulation of $40 in gold for every $100 Federal Reserve notes outstanding.

Then Mr. Collins analyzes the third type of money which is deposit money or credit money. In the second paragraph on page 28 he gives the reader the popular conception of bank deposits and follows it in the third paragraph by the true facts regarding the bank's ability to create money.

Later on he states that a dollar in gold is just a dollar, but a dollar employed as a reserve, permits the issuance of $2.50 in currency.

I quote Mr. Collins:

"But the use of deposit money, or credit, makes it possible to stretch our gold much farther. For, obviously, if it is only required that member banks carry a 10-percent reserve against deposits, $10 in money of this sort can be created out of every $1 in gold. But even this is not the complete picture", says Mr. Collins. "The mobilization of our gold in the Federal Reserve banks has added still further to the work that gold can do.

"The Federal Reserve does with member banks precisely what the member bank does with the customer. The Reserve bank must keep a reserve of 35 percent in gold or lawful money against its deposits, or $1 in gold against $2.85 in deposits, but for every $1 of these deposits, since they represent the reserve of member banks, the member banks can create deposits of $10."

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Now, finally, this is what Mr. Collins has to say and this I truly believe is the most important single proposition before this country today. I quote:

"Therefore, in theory at least, $1 in gold in the vaults of the Federal Reserve System may, when used as a reserve against the latter's deposits, provide the basis for $28.50 in deposit money, or credit, in the member banks.

"From the foregoing it will be seen that under our banking system the Federal Reserve banks provide the ultimate limits of monetary expansion of using money in its broader sense of both currency and credit."

I ask that Mr. Collins' 4-page article be introduced into this record. It comes from the assistant financial editor of the New York Herald Tribune, that prides itself on influence—67 percent in "The Street." It is the finest short article on our monetary system that it was ever my pleasure to read. It openly admits that there are three kinds of money: The metallic base; the currency of circulating issue, born in iniquity on crookedness; and, thirdly, the actual money in the country which is deposit money, which is fiction money, which is banker-controlled money—the real printing-press money in the country, which doesn't need even the Bureau of Engraving and Printing to process it, which only needs a job printer to run off blank checks and promissory notes to be filled in by anyone in the country to whom the private banker allots credit.

This is money which, according to Mr. Collins, has an ultimate limit of $28.50 for every dollar of gold in the Federal Reserve System.

This is not bankers' money, because the banker has contributed only the capital and surplus. This isn't depositors' money in the sense that it originated by the depositor shoving currency through the wicket of a bank.

This money is available on the security of the borrower who can cash in his real property or his securities at the will of the private banker who alone decrees the allotment of credit in this country—the banker who can and does decree every expansion and every contraction of credit—the banker who throws you into depression at will and whose power over this country represents in his control of money and credit the control over the lifeblood of this Nation.

WE HAVE A CENTRAL BANK

Gentlemen, it is rapidly occurring to everyone in public affairs that we have a central bank.

On February 2, 1932, there came into actual operation a central bank of the United States under the title of the Reconstruction Finance Corporation. From that day until December 31, 1934, the R. F. C. authorized the following:

Loan banks and trust companies, $2,263,000,000.
Building and loan associations, $102,000,000.
Mortgage loan companies, $425,000,000.
Credit units, $622,000.
Federal land banks, $399,000,000.
Federal intermediate credit firms, $9,000,000.
Joint stock land banks, $21,000,000.
Agricultural credit corporation, $6,000,000.
Regional Agricultural Credit Corporation, $178,000,000.
Livestock, $14,000,000.
Railroads, $457,000,000.
Total, under section 5, $4,031,000,000.

In Table 8 of R. F. C., Report to Congress, Document No. 139, a report for the fourth quarter of 1934, 7,327 banks and trust companies had received loans of $2,263,000,000; 5,164 of these loans were granted to banks and communities of less than 5,000,000 people.

I submit the table for the record.

Table 9 in Mr. Jones' report shows that on December 31, 1934, approximately $865,000,000 represents the loans on and purchases of preferred stock and purchases of capital notes and debentures of 5,457 banks and trust companies. This $865,000,000 is 26 percent of the capital stock of all the banks reporting to the Federal Deposit Insurance Corporation.

In the R. F. C., we have a central bank owned by the United States which, in turn, directly owns capital stock to the extent of 26 percent of all the capital of the banks of the country.

We have, under the Constitution, the power of Congress to coin the money and regulate its value, and yet so far we have not been honest enough to combine under the constitutional power the functions of the R. F. C., the Home Owners' Loan Corporation, the various farm credit agencies, the work that

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should be done in extending credit to small industries, such as is being proposed under the Koppleman bill.

We have the tremendous problem of financing the extraordinary expenses of Government, particularly as covered by the Work Relief Act.

Just as the Federal Reserve was deemed necessary in 1913, so 22 years later there is need as never before since 1781, when it was first proposed, a central bank of the United States of America.

Mr. WARD. I have here a little summary showing how the 108, or 102 who are on the Federal Reserve directorates today—there are a few vacancies—are cast.

(The statement referred to is as follows:)

A BOARD OF 48

The Federal Reserve is headed by a Board with two ex-officio members, the Secretary of the Treasury and the Comptroller of the Currency, and six appointed by the President, by and with the advice and consent of the Senate.

The 12 Federal Reserve banks have, according to the last report, 102 directors, representing 40 States and the District of Columbia. There are, of course, the 12 governors in addition.

Here is management of a System represented ordinarily by 108 directors, 8 members of a central board, and 12 governors; 128 represent the banking interest of the country and 8 represent the administration.

The following list indicates the membership on the boards of the 12 banks, arranged by weight of membership:

State	Members	State	Members
Pennsylvania	9	Maine	1
Texas	9	Connecticut	1
New York	8	Rhode Island	1
California	7	Delaware	1
Massachusetts	5	Maryland	1
Ohio	5	South Carolina	1
Illinois	4	New Hampshire	1
Minnesota	4	Florida	1
Missouri	4	Alabama	1
Virginia	3	Louisiana	1
Georgia	3	Iowa	1
Wisconsin	3	Kentucky	1
North Carolina	2	Arkansas	1
District of Columbia	2	Tennessee	1
Mississippi	2	South Dakota	1
Indiana	2	North Dakota	1
Michigan	2	Montana	1
New Jersey	2	Colorado	1
Kansas	2	Oregon	1
Oklahoma	2	West Virginia	1
Nebraska	2		

The following States have no membership on the 12 Federal Reserve bank directorates:

Vermont, Arizona, Utah, New Mexico, Nevada, Washington, Wyoming, and Idaho.

Mr. WARD. I have a summary prepared here, covering my statement, which I will ask permission to insert in the record. The chairman has asked me to be as brief as possible, and with the consent of the committee I will just leave that summary of points.

(The statement referred to is as follows:)

AN INDEPENDENT BOARD

The committee has heard the testimony of Dr. Miller. The banker doesn't want the politician in, and the people don't want the banker or a politician in.

Instead of 128 men directing the destinies of our monetary system, we should establish an independent board, one from each State, appointed for long terms of years.

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They don't have to be bankers any more than the Senate of the United States has to be constituted of bankers in order to be able to draft banking legislation.

The experts brought us where we are, and the bankers brought us to our lowest state.

The independent board is the thing, operating under Congress. A board that will make monetary control a career; a board that will be given authority and responsibility.

SUMMARY

Gentlemen, I want to now summarize the presentation of the Nye-Sweeney bill for social justice.

I believe that for the first time in American history a bill is suggested which is intended to correct the most glaring evils of the American monetary system.

The Nye-Sweeney bill attempts to put into effect the true and real intent of money.

It hopes to transform and correct the wrong notions as to the place and work of money, which notions have prevailed since the introduction of the modern banking system.

The following are the theses, which should be challenged by every independent mind of Congress; and if there is anything wrong about any of them, the error should be brought to light.

Point 1.—The monetary banking system came as a usurpation of the sovereign right of the Government to coin and regulate money.

Point 2.—The creation of a counterfeit checkbook money furnishes competition to the money of the United States, is only an extension of the plan of the goldsmiths to circulate gold receipts, and is on its face the usurpation of the sovereign power to government.

Point 3.—The introduction of this counterfeit checkbook money, competition to our national currency, was not an open usurpation, but rather as a usurpation introduction as a "trade secret" discovered by the goldsmiths and handed on "in the trade" to their modern successors, the bankers.

Point 4.—The people do not understand this subtle move or usurpation of the sovereign power over money, since it came in in such a way as not to attract any attention to it or any suspicion of it.

Point 5.—Nevertheless, it is a real, though at first unsuspected, usurpation of the Government's prerogative to coin and regulate the value of money. The bankers now consider this usurpation a vested right. The rank and file of the people, until lately, did not comprehend the real point at issue and have until now paid little or no attention to it.

Point 6.—The present banking system, with its creation of a system of credit money, and operating under the Federal Reserve Act, puts the power over money and credit in the hands of the bankers and gives them the power to create depression or decree prosperity at will. Such power over money and credit is sanctioned by law under the present Federal Reserve Act.

Point 7.—In recapturing the money power by the people and placing that power under Congress, where it belongs, the theory is attacked by such as Banker Warburg, who said in his testimony on the omnibus bank bill, "The Government would not have the courage to stop a boom"; but the converse of Banker Warburg's statement is the important thing for America: "Neither would the Government have the courage to start a depression." The boom is stopped by calling more loans, and the depression is caused by calling loans and stopping credit.

Point 8.—The Nye-Sweeney bill aims at correcting this monstrous injustice. It would take out of the hands of private bankers this power over prosperity and put it into the hands of the Government the control of money and credit, to be administered for the good of all. Since credit performs at least 95 percent of the business of America, the power over it should rest only with the Government.

Point 9.—The argument that the Nye-Sweeney bill will put credit and its allotment into the hands of the politicians—well, this objection applies with equal force to every power which "we, the people" of the United States, have given to Congress in the 18 powers enumerated in the Constitution.

Point 10.—The production problem of the country is solved. The only way to create wealth is the starting of toil and labor on the natural resources of the Nation. This creates the wealth. Money is the means of distributing that wealth, and the creation of money is in private hands today, is the means of concentrating wealth into the hands of the few, and the creation and destruc-

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tion remain the property of the private banker. If placed under the control of the Government, the power over money and credit would be administered for the good of all.

Point 11.—A depression is caused in only one way; that is, by the banks calling in loans and refusing further credits. Such contracting of credit takes out of circulation a huge amount of the checkbook money of the banker; and though it is legalized counterfeit money, it operates the same and to the same advantage as genuine Government money.

Point 12.—Depressions are inevitable because they occur here in the richest Nation in the world under a provident God and not an improvident God; they are therefore the work of men. The thing to find out is, who are the men that cause them?

Point 13.—The Nye-Sweeney bill will prove it by the means of attacking the problem of interest. The Government is paying a billion a year for interest and approximately 6 hundred million of this goes to the private banker who absorbs practically 60 percent of the national debt. The public and private debt of this Nation is far in excess of 2 hundred billion dollars and actually is greater than the national wealth. Five percent is a low average interest rate. Interest runs from the point of $2.70 average for the financing of the Government to as high as 240 percent a year which the poor pay to the personal loan. The national interest bill is 10 billion dollars a year, or practically 25 percent of the entire national income. This is a millstone around the necks of the people.

Point 14.—All the banks of the Nation will be asked to absorb the 4 billions of Government bonds under the Public Works Act. All the banks have 700 million dollars today in cash in their possession; this 700 million is needed for till money. They can't even loan that to the Government, so what happens. They enter upon their ledgers a credit in exchange for Government bonds, carrying approximately 3-percent interest in exchange for which they give the Government the right to withdraw. Without departing with the slender cash, they now create money and the sovereign power of the United States pays the 75 million dollars a year, so-called "interest" for the use of the usurped right to coin money.

Point 15.—Now if the control of credit was under the Government, why should the Government charge interest for check-book money, the free circulation of which in adequate amounts brings prosperity to the country. Wouldn't it be absurd for the Government to penalize the borrowers whose check-book money brings about prosperity? But the banker under our present system can exact tribute from the borrowers who help to make prosperity. Would it not be to the advantage of the Government, that is, to the advantage of the people, to have at all times enough money in circulation to meet all needs? And by money we mean currency and credit, or check-book money.

Senator BULKLEY. Does the National Union have any message to deliver to us with respect to its determination to defeat any Senator who does not see this thing in the way the Union does?

Mr. WARD. No.

Senator BULKLEY. You would rather have us give sincere and honest consideration to it?

Mr. WARD. I think that was the language, Senator.

Senator BULKLEY. I hope the National Union is going to take that view, because the other view, in my opinion, is just nonsense, and it is very harmful to the cause.

Mr. WARD. I will regard very attentively that judgment, and appreciate your thoughtfulness in giving it.

Senator BULKLEY. I stick to that pretty strongly, for reasons which you probably know, and I hope, at the same time that you thank Father Coughlin for his courtesy to us and for the very interesting and excellent and thoughtful statement you have made, that you will also convey the other message, not in any spirit of antagonism at all, but simply as a statement of principle.

Mr. WARD. You have all been most courteous. Are there any questions?

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Senator GLASS. Apparently not. We are glad to have had your statement.

Mr. WARD. Thank you.

Senator GLASS. There are two bankers from South Carolina who had asked to be heard this afternoon. Mr. Beattie.

STATEMENT OF F. F. BEATTIE, PRESIDENT FIRST NATIONAL BANK, GREENVILLE, S. C.

Senator GLASS. I believe you are connected with the First National Bank at Greenville, S. C.

Mr. BEATTIE. Yes, sir.

Senator GLASS. You know the bill we have under consideration.

Mr. BEATTIE. I understand, sir, that I am appearing on the Eccles bill, the banking bill of 1935.

Senator GLASS. Yes, sir.

Mr. BEATTIE. Mr. Chairman and gentlemen of the committee, I desire to say for your information that I am president of the First National Bank of Greenville, S. C. The bank has resources in excess of $6,000,000. I have held my present position for nearly 20 years. The bank has been in existence for more than 60 years. I take pride in saying that it has been able to stand upon its own merits and has neither requested nor accepted any aid or favors from the Government, even during the great depression through which we have been passing.

Greenville, S. C., is a town of about 30,000 people, situated in the Piedmont section of the State. The chief industries of the community are farming and cotton-textile manufacturing. I desire to say also that South Carolina is overwhelmingly Democratic in politics. I have voted the Democratic ticket consistently throughout my life and many years ago served as a Democratic member of the General Assembly of South Carolina. I say this to assure you that I am free from political prejudice in the matter concerning which I appear.

I appear, gentlemen, to protest earnestly against the passage by Congress of title II of the Banking Act of 1935, which act is now before you for consideration. I am of the opinion that title II of this act gives to this administration and to such administrations as may follow enormous and unprecedented control over the resources of the Federal Reserve System. I think that it is a most dangerous power which this bill seeks to create—dangerous not only to those interested in banking, but to the very liberties of the people of America. It is well recognized that a government desiring dictatorial power seeks first to seize control of the credit machinery of a nation. Given the dictatorial control of credit, governmental power over the destinies of a people may easily become supreme. I think also that the open market features of the bill confer powers which may easily lead to currency inflation such as has been experienced since the World War by Germany and other European powers, using the same methods. I cannot believe that this Nation is willing to take the chance of such a disastrous experience.

I desire to say, gentlemen, that I am of that school of thought which believes that the business of banking in this Nation is already unduly controlled and regulated by Government. Such control is

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now far more vigorous and rigid than exists in other enlightened nations of the world. The banks of this Nation are already so controlled by laws and regulations as to substantially retard their operations and cripple their proper functions, from which communities suffer. A condition has thus been brought about in the banking business where new capital refuses to come into this business and young men are reluctant to choose the business of banking as a career.

It may be proper to ask here, with all respect, who owns the Federal Reserve System? Whose money is invested in the Federal Reserve System? Certainly the Government does not own it and has no money invested in it. The Federal Reserve System is owned entirely and completely by the member banks of the System and through these member banks by many thousands of American citizens who have invested their money in the capital stocks of the member banks. Yet this bill would place the Federal Reserve System with its enormous resources under complete governmental and political control, without the investment of a single Government dollar. Where a strong government is dealing with the property of its citizens, which it may desire, government ownership of the property desired may not be necessary, if the government is willing unfairly to seize without compensation the perpetual use and control of the desired property of the citizens. If there is to be a central bank in this Nation, governmentally and politically operated, of which I do not approve, I think that in all fairness to the owners of the Federal Reserve System, the Government should own and operate it with its own money and not with money invested in good faith by its citizens. If the banks of the Nation are to be operated as the post offices are now operated, they should be governmentally owned and paid for.

I beg to repeat here that I do not advocate Government ownership and political control of banking. I am of the opinion that any system of banking under political control is dangerous in the extreme, whether it be the Federal Reserve System as contemplated by this bill, or whether a new central bank governmentally owned be created by Congress to supplant the Federal Reserve System.

Senator Bulkley. What alternative do you favor as opposed to governmental control?

Mr. Beattie. My opinion, sir, is that the Federal Reserve System, as originally created, under the control of a Federal Reserve Board, with the powers then conferred, and with the Secretary of the Treasury and the Comptroller of the Currency removed from the Board, would meet my ideas.

Senator Bulkley. You think the present system is all right if we take the Secretary of the Treasury and the Comptroller of the Currency off the Board?

Mr. Beattie. With the powers conferred upon the Board by the bill as originally enacted. In other words, I am an advocate of the Federal Reserve System as it was organized, speaking generally, The objection that I have is that the Comptroller of the Currency and the Secretary of the Treasury being on the Board tends to give some political control, which I think it would be wiser not to have. I think the further removed the Federal Reserve Board can be from

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political domination or control or interference, the better for the banking business of the country.

Senator BULKLEY. Mr. Miller testified last week that world conditions have so changed that we are bound to have a greater measure of management with respect to currency and banking matters than we had some years ago. I was wondering whether you thought the set-up was adequate to cope with that.

Mr. BEATTIE. I do, sir. I assert, in all earnestness, that sound banking and politics will not mix.

Gentlemen, I want to say here that, as I stated a moment ago—and I did so purposely—many years ago I had some little political experience myself before I went into the business of banking, and I thoroughly understand and appreciate the urge that comes upon a man holding political office to seek the influence of someone above him in politics—what an urge there is there to do something which he should not do, to the extent that his judgment is likely to be warped or overridden if he is under political influence or interference.

Senator BULKLEY. Do you think the present Federal Reserve Board is free from that?

Mr. BEATTIE. I think it started off that way, sir. I think in recent years—possibly within the past 2 years—there has been some evidence that there might be political control there.

Senator BULKLEY. Mr. Miller quite firmly testified that there is political influence going back a good deal more than 2 years.

Mr. BEATTIE. Of course, Mr. Miller speaks with authority. My knowledge is limited, and obtained only from general impressions made by reading in the daily press. I thought, however, that up to 2 years ago there was little political interference or control. That was my opinion.

I assert in all earnestness that sound banking and politics will not mix. Political banking is disastrous, whether it be in a local community or on a national scale. The simple reason for this, I think, is that the ability to say " no " firmly and courteously when that word is required is an absolute essential of sound banking; and politicians, thinking about the chief or the boys back home, often have difficulty in pronouncing this simple word. The only way that a bank or banking system can be kept free from political pressure and control is through a board of directors who hold no political office and who have no political aspirations, and manned by executives of the same caliber.

It is interesting to remember, gentlemen, what a great and successful effort was made by Congress at the time of the creation of the Federal Reserve System to keep the System free from political interference and control. I need not recall to your minds that this was during the administration of a great Democrat, Woodrow Wilson; and that another great Democrat—your chairman, now the senior Senator from Virginia, the Honorable Carter Glass—was the leader of the successful fight. Under the Federal Reserve Act as thus created the Federal Reserve System was to be governed by impartial and experienced men far removed from the turmoil and pressure of politics and intent upon giving to the Nation a banking system serving the legitimate and proper banking needs of agriculture,

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commerce, and industry. Throughout the years the Federal Reserve System has fulfilled its mission well.

Now a determined effort is being made which will destroy that System as created. This bill, if passed, will spell its doom.

The Federal Reserve System, as it exists, has been the envy of the world. It is the child of a Democratic administration. It is now being attacked by those who should be its protectors. Should a Democratic administration now destroy the Federal Reserve System, then the Democratic Party will be classed with those vile creatures of the earth who devour their young.

Senator GLASS. We are very much obliged to you, Mr. Beattie.

STATEMENT OF L. M. WIGGINS, PRESIDENT BANK OF HARTSVILLE, S. C.

Mr. WIGGINS. Mr. Chairman and gentlemen, I testify before you not as a banker nor an economist nor as one " qualified by education or experience or both to participate in the formulation of national economic and monetary policies." I represent the viewpoint of industry, agriculture, and commerce in South Carolina and, to a lesser degree, banking; being president of a small State bank, which is a member of the Federal Reserve System.

With reference to title I of the proposed banking bill, I am in full accord with its provisions, and urge its prompt adoption, with the exception of one provision. I present the serious objections on the part of bankers and business men in our State to the provision in title I that will discontinue on a fixed future date the insurance of deposits in banks not members of the Federal Reserve System. Although it may be a desirable ultimate objective to have every bank of deposit in the United States a member of the Federal Reserve System, it is a practical impossibility for many of the small banks and cash depositories in our State to meet reasonable membership requirements and to survive the loss of revenue which would follow membership in the Reserve System. The only alternative to the discontinuance of banking facilities in many of our small towns and communities would be a restoration of wide-spread branch banking. South Carolina has sustained such serious losses in the operation of branch banks in the State that it will be many years, if ever, before this type of banking will have the confidence of the people. We believe that the farmers and business men of small communities have the right to provide and use banking facilities so long as the institutions set up are soundly administered and profitably operated, even as that right is enjoyed in the larger centers of population.

Senator GLASS. Did you have branch banking or chain banking?

Mr. WIGGINS. We had one main bank in the city of Charleston, with branches all over the State—46 of them, I believe.

Senator GLASS. Were they exactly branches of that bank, or were the smaller banks owned by that bank?

Mr. WIGGINS. They were branches of that bank.

Senator COUZENS. Did they fail?

Mr. WIGGINS. They failed, and the depositors, up to now, have received 10 percent of their deposits.

Senator BYRNES. The Western Carolina Bank, with 12 branches, failed.

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Mr. WIGGINS. Yes; it failed. The South Carolina National Bank, with three branches, failed.

Senator COUZENS. Your State law permits branch banking?

Mr. WIGGINS. Yes, sir.

Senator COUZENS. Anywhere in the State?

Mr. WIGGINS. Yes. The profitable operation of many of the smaller banks in our State under the requirements of Federal Reserve membership would be impossible. We, therefore, urge upon you the postponement if not the present abandonment of the proposal to require banks which have their deposits insured to become members of the Federal Reserve System by a specified date.

Senator COUZENS. What do you think of the proposal to require all those with more than half a million dollars worth of assets to come in, and exclude those below that amount?

Mr. WIGGINS. I think that would be all right. In fact, I know of no bank in our State of that size that is not a member.

Senator GLASS. What do you think of the proposal to defer the matter until 1938, according to one suggestion, and 1940, according to another?

Mr. WIGGINS. My idea, sir, is that at the present time it would be pure speculation to determine a future date, considerably in the future, for that to be brought about.

Senator BYRNES. What will be the effect upon your State banks and cash depositories to which you refer if they are not given time?

Mr. WIGGINS. I did not quite get the question.

Senator BYRNES. If the present plan is carried out, what would be the effect upon those cash depositories?

Mr. WIGGINS. Most of them will have to go out of business.

Senator COUZENS. Because their earnings are not enough or because their assets are not good enough?

Mr. WIGGINS. Because their earnings are not enough. Their assets are good.

Senator BYRNES. The earnings come from the amount they charge for cashing checks.

Mr. WIGGINS. That is true. They are principally capitalized at very small amounts. They are prohibited from lending money. They are safeguarded with every provision for soundness, and they must make their earnings out of various charges which the community is willing to pay.

Senator COUZENS. Do I understand you to say that they do not lend any money?

Mr. WIGGINS. No, sir.

Senator BYRNES. They opened just after the bank holiday to serve the communities.

Mr. WIGGINS. That is true; when capital was so limited that it was impossible to organize an ordinary bank we established a system of cash depositories.

Senator COUZENS. Without capital?

Mr. WIGGINS. No, sir. They have a small capital—$10,000 in some cases.

Senator BULKLEY. Do they invest deposited funds?

Mr. WIGGINS. No, sir; not without the permission of the depositor. They can invest their own capital, but not the deposits.

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Senator BYRNES. Are there many counties having no bank operating, and relying entirely upon cash deposits?

Mr. WIGGINS. There are not many entire counties, but my recollection is that there are 27 cash depositories in our State, and approximately 130 banks.

Senator COUZENS. Are these 130 banks mostly members of the Federal Reserve?

Mr. WIGGINS. Only the national banks, and four State banks.

My principal comment is on title II. I shall not attempt to discuss in detail the provisions of this title because this already has been done, and ably, by others who have preceded me. I shall attempt only to give you the viewpoint and conclusions of men from my section of the country who represent a fair cross section of agriculture, industry, commerce, and finance.

We regard the major and underlying purpose of title II of the Banking Act of 1935 as a perversion of the Federal Reserve System from the sound principles on which it was founded and a deliberate attempt to appropriate to the Government the banking reserves of this Nation, with the result that they may be used as the means for promoting the financing of governmental needs with a minimum checks and with a maximum of political control, by whatever administration happens to be in power.

Under the recent emergency conditions, the Federal Reserve System, through an urgent necessity which may possibly be justified, turned over to the Government a large part of the reserves of the banks of the Nation and through them the reserves of the depositors in the banks throughout the Nation and accepted in return the obligations of the Government. The great concern today should be the restoration of the liquid reserves of the Federal Reserve System and the divestment of its holdings of Government securities, rather than an attempt to institute a program whereby these reserves could be utilized still further to finance a mounting Government deficit. We urge upon you the desirability of returning the Federal Reserve System to its proper reserve and banking functions as soon as possible.

The Federal Reserve System, which was designed primarily to hold the liquid reserves of the Nation, to provide an elastic currency and furnish a " democracy of credit " that should meet the needs of agriculture, commerce, and industry, becomes, under the emphasis given in title II of this act, in effect a political department of the Government whose chief concern is " in the formulation of national economic and monetary policies " rather than in the operation of a sound reserve banking system to meet the needs of agriculture, commerce, and industry. The individual Reserve banks are practically stripped of any independence by this act and the directors of the Reserve banks representing banking, agriculture, and industry become in practical effect little more than an advisory body. The personnel of the Federal Reserve Board, now selected with some regard for a " fair representation of the financial, agricultural, industrial, and commercial interests " of the people of the United States, will, under the proposed set-up, be limited to persons well qualified to participate in the formulation of national economic and monetary policies.

The concentration of power in the hands of a small group, largely political, constituted with practically no legal limitations or restric-

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tions, as will be given by this title to the Federal Reserve Board, is foreign to our conception of the principles of democratic government. Such a grant of power is unparalleled in our country, except in times of war or grave national emergency, and should be safeguarded by law so as to retain in the hands of Congress the power to regulate the value of money. The broad invitation given to the Federal Reserve Board under the powers granted under this bill, to engage in monetary manipulation and to try out economic theories on a gigantic scale through the use of the reserves of the bank depositors of the Nation offers possibilities of mistakes that may invite financial chaos in this country. It is possible—whether it does it or not, the power is there—for the Federal Reserve System, under the provisions of this bill, to become a bouncing board, against which Government securities, without limitation as to amount or maturities, may be tossed to produce an unending return stream of paper credit to provide for mounting Government expenditures. This can continue only so long as the people have confidence in the ability of the Government ultimately to repay, but when the spark of fear of the ability of the Government to repay is struck, the devastating and uncontrollable chaos of money worth less and less will quickly paralyze the Nation. It will then be too late to discover that the banking reserves of the people of this Nation have been consumed in the great experiment.

I cannot agree with those who believe that title II of this bill can be changed so as to correct the dangers that lie within it. Of course, many of its most dangerous provisions may be changed, but it is my conviction that the whole major premise on which the theories promulgated in title II rest is unsound, violates the sound, common-sense judgment of the American people, and belongs to the realm of dictatorships. Without desiring to raise any unnecessary alarm, I say to you frankly and honestly that it is my deliberate opinion that, carried to its ultimate conclusions, title II of this bill, as now written, will destroy the Federal Reserve System of banking in the United States.

Senator GLASS. We are very much obliged to you, Mr. Wiggins.

We will adjourn until 10:30 tomorrow morning, when Mr. Owen D. Young will appear.

(Thereupon, at 4:15 p. m., the subcommittee adjourned to meet tomorrow, Wednesday, May 29, 1935, at 10:30 a. m.)

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BANKING ACT OF 1935

WEDNESDAY, MAY 29, 1935

United States Senate,
Subcommittee of the Committee on
Banking and Currency,
Washington, D. C.

The subcommittee met, pursuant to adjournment on Tuesday, May 28, 1935, 10:30 a. m., in room 301, Senate Office Building, Senator Carter Glass presiding.

Present: Senators Glass (chairman of the subcommittee), Bulkley, McAdoo, Byrnes, Bankhead, Townsend, and Couzens.

Senator Glass. The committee will come to order. Several of the members are detained at other important committee meetings and cannot be here. We are to hear this morning from Mr. Owen D. Young.

STATEMENT OF OWEN D. YOUNG, CHAIRMAN OF THE BOARD, GENERAL ELECTRIC CO., NEW YORK, N. Y.

Senator Glass. Mr. Young, just give your name, please, and your position to the official reporter.

Mr. Young. I have prepared, Mr. Chairman, a little statement giving my name and qualifications—or disqualifications—and also a statement on title II of the bill, which is the only part of the bill to which I shall speak.

Senator Glass. Very well, sir. You may proceed.

Mr. Young. That will take me not more than 15 minutes, I think, and if I might be free to present that first and then respond to questions, I would appreciate that procedure.

Senator Glass. I am sure the members of the committee will observe that request.

Mr. Young. My name is Owen D. Young. My home is at Van Hornesville, N. Y., but I spend the greater part of my time in New York City. With your permission, I shall, as a preliminary, state very briefly my qualifications and disqualifications to express an opinion on the bill before you.

I am chairman of the board of directors of the General Electric Co. In that capacity or as a vice president, I have been associated with that company for more than 20 years. Since 1923, I have been a director of the Federal Reserve Bank of New York. Originally I was chosen as a class B director, which means, as you know, that I was selected by the group of so-called " large banks " as a representative of industry and commerce. I was reelected a class B director in December 1925, and before my term expired, I resigned as a class B director and concurrently, namely, on January 13, 1927, I was

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appointed by the Federal Reserve Board as a class C director; that is, as a public director, and since that time I have served in that capacity. My present term of office expires at the end of this year, and under the ruling of the Federal Reserve Board, I am not subject to reappointment, so what I say here about this bill has the background of the experience which I have indicated and is said with the full knowledge that I shall not in the future have any responsibility for the operation of the Federal Reserve bank.

I should also say perhaps that in 1924, as a member of the Dawes Committee, I took an active part in the reconstruction of the currency and credit structure of Germany, which, as a result of violent inflation, had completely broken down, and as an incident of such reconstruction, I had to do with the reconstitution and recapitalization of its central bank, known as "the Reichsbank." Later, in 1929, as a member of the Second Committee of Experts, I was concerned with the establishment of the Bank for International Settlements which, through the constitution of its directors, became intimately related to all the principal central banks of Europe. So I have had the opportunity, at least, to observe the personnel and the organization of the central banks of the principal financial and commercial countries of the world.

I should say also that I have had no experience in commercial banking, and I have no greater knowledge of its technical details and special techniques than the average business man. So if in the course of this hearing you seek to explore the technicalities of commercial banking through me, I must warn you in advance of my disqualification and your disappointment.

It is with such a background and in the face of such limitations that I address myself particularly to title II of this bill, titles I and III, I understand, being largely corrective of existing legislation.

At the very outset one must ask whether there is need of banking legislation, and if so, whether the pending bill meets the need. One may well say that a banking system which failed to restrain the boom and collapsed during the depression should be restudied as a whole. This means not only the Federal Reserve but our whole commercial banking system. I predict that such a study would uncover even greater defects in our commercial banking set-up than in that of the Federal Reserve System. This bill is largely directed to far-reaching changes in the Federal Reserve System. One may put the question—I hope free from the charge of destructive criticism—whether it is not wise to look to the soundness of the foundation at the same time that one proposes drastic changes in the superstructure. We have had a great deal of piece-meal banking legislation. Recently we have had considerable emergency legislation. Now, it would seem prudent for us to review it all and present one comprehensive program.

So my conclusion is, Mr. Chairman, that there is need for new banking legislation based on careful study, and I do not think the pending bill meets the need because it deals in the main with only one part of the system.

More than 4 years ago I expressed the view to this committee that all commercial deposit banking in the United States should be carried on under one law; that examination of commercial banks and their controls should be under one authority; and that then, and only then,

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we could develop for the country as a whole a sound commercial banking system and definitely fix responsibility. I said then that if we were to retain in our system banks of deposit chartered by the States as well as by the Federal Government they should all be required to be members of the Federal Reserve System. That recommendation I repeat now. While this bill as introduced did contemplate that result by requiring all banks whose deposits are insured being brought into the system, I am told that even that provision has been eliminated by the House. So it seems to me that instead of curing one of the most evident weaknesses in our foundation, one of the chief causes of our banking collapse, we avoid it.

I do not criticize the bill because it fails to offer solutions for all our banking problems. That is not the work of a day. If the extension of Federal jurisdiction over all banks of deposit is a prerequisite to any sound system, it is not of itself a panacea. The collapse of 1933 was only the climax to a long and tragic chapter; in the preceding decade nearly 10,000 banks failed in this country. It is true that more than four-fifths of these were nonmember banks, subject in fact to no Federal restraints. It is also true that nearly three-fourths were situated in towns having a population of 2,500 or less, and that these small communities have consequently suffered most. How are we to get banking facilities that are adequate and safe? This question is fundamental and requires exhaustive study. It is only when such a basic question shall have been answered that we can really determine what changes are required in the Federal Reserve System. Yet here we address ourselves instead to the superstructure, which at best can be no stronger than its base.

In proposing sweeping changes, certainly hasty action is to be avoided unless it is imperative. I know of no emergency, either present or prospective, which requires legislation now. Everything which can be done by the Federal Reserve System to relieve the depression either has been or is now being done. The changes proposed in title II will add nothing to the relief of our present condition. The System has provided already, in connection with our gold imports, $2,300,000,000 of excess reserves, credit not in use. Certainly no one would expect or wish it to do more. The Federal Reserve banks are, under emergency powers, making direct loans to commerce and industry under the guidance of the Federal Reserve Board. Certainly nothing in the proposed bill would or should authorize them to do more. The only justification that I know of for new legislation now of the character proposed is to centralize power and responsibility so that we can better control another boom. I venture the opinion that we have ample time for study before that power is needed.

With the consequences of the banking collapse, we are familiar. We have faced them and dealt with them. That was an emergency and it required courage and action. This the Government exhibited and, as a result, our banks are functioning again and are safe. Broadly speaking, the direct consequences of the collapse have been cured except for such corrective legislation as is contemplated in titles I and III of the present bill.

Title II is, I take it, designed to correct some of the causes of the collapse, as distinguished from consequences. Now it is easy to recognize consequences and to cure them. Causes, however, are

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much more obscure and much more difficult to correct. Where consequences need courage and prompt action, causes require study and reflection. Consequences may require emergency legislation, causes require carefully considered laws. That is especially true in a situation so complex as our banking structure.

Therefore, Mr. Chairman, if there be no need for haste, I see no reason why title II of the pending bill should be dealt with at this session at all. All history shows that one of the characteristics of such a period as we are now going through is a demand, usually somewhat hysterical, for the manufacture of money and drastic revisions of its control. One should not be classed as opposed to corrective and progressive legislation merely because in times like these he suggests study, reflection, discussion, and comprehensive revision.

My chief objection, Mr. Chairman, to the pending bill—and this is a very basic objection—is that it sets up in fact a central bank and destroys the regional system under which we have operated so long. I can see some advantages in a central bank, but I doubt whether such a basic question should be settled until the issue has been fairly made and fully debated both in and out of Congress. It may be that the American people want to destroy the regional system and establish a central bank. I do not know. Members of this committee will not need to be reminded that the last time the issue was presented, the people rejected a central bank in favor of the regional system. Perhaps their views have changed, but I do feel strongly that a result so far-reaching should not be accomplished indirectly. If we are to have a central bank, then our entire law should be redrafted so as to be suitable to one central bank operation. The retention of the regional facade may, I fear, lead the American people to think they are retaining their regional banks when in fact they are creating a central one. Such a basic issue should not be settled by indirection.

The bill puts all the important powers and responsibilities in the hands of one central body in Washington. It diminishes correspondingly those of the 12 regional banks. They are left but little more than administrative branches of this central authority. If such vast powers are to be concentrated in a single body in Washington, then we should take all possible precaution to guarantee the ability and independence of such a group. I am sure that we do not want to have a central bank subservient to any special interests. We must, if possible, keep it free of domination either by politics or finance.

I want to speak about the independence of action in that central body.

We have discovered only two ways in America of guarding against the misuse of great power. One is to take a group of carefully selected citizens, provide for them and their families reasonably for life, and then to some extent insulate them from outside influence of all kinds. The Supreme Court of the United States is a fair example of this method. The other way is to take less care in insulating the group from bias, but to provide diversified representation on the group and to set up appropriate checks and balances within the group itself in the hope and expectation that the power will be exercised wisely even though by compromise.

In the organization of the regional Reserve System, we resorted to this second method. For example, in each of the 12 banks we pro-

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vided for a board of 9 directors, of whom the chairman and two other directors were to be public representatives named by the Federal Reserve Board in Washington. The remaining six directors were chosen by the member banks, but only one-half of them could be bankers; the other half were the representatives of industry, commerce, and agriculture. The exercise of most of the substantial powers of the regional boards, however, was subject to the approval of the Federal Reserve Board in Washington. It was in this way that we sought to get the views of 3 bankers on the board of each Federal Reserve bank, the views of 3 business men selected by the banks, and the views of 3 independent citizens—and then we superimposed on them the views of the board in Washington, which might be considered to have more intimate knowledge of general conditions, including politics. It was through this balance that we sought results.

It is proposed now to put all the substantial powers in the hands of the board at Washington with no checks or balances from the local boards of the individual Reserve banks on the exercise of these powers. In addition, it is proposed that the Governor of the Federal Reserve Board in Washington shall be recognized as the political appointee of the President, and I assume that means subject to removal by him at any time. The result is that the bill contemplates not only the removal of the regional checks on the central board, but it provides that the most important member of the board shall at least have definite political color. Is it unfair to say, therefore, that the bill contemplates not only a central bank administered from Washington, but that the board of administration shall to some extent be considered political? The proposed bill fails to provide an insulated body, such as has been described as a " Supreme Court of Finance ", and at the same time it removes the checks and balances which have been imposed in the present System. Is it any wonder that such a violent change should create apprehension and dissent?

This apprehension is not alleviated but rather increased by the present state of our budgetary unbalance and the necessity of issuing large amounts of Government obligations. There should be no removal of checks on the bank of issue against taking Government obligations direct and not through the market. It was the exercise of this very kind of power which led to the currency and credit downfall in Germany and the ultimate destruction of the Reichsbank.

I recommend that Government financing direct through the central bank, except for the usual temporary advances, be prohibited in any bill.

I want to speak about the appropriate relationship of Government to a bank of issue.

The central banking organization, whether it be a regional system such as we have or a central bank such as is proposed, must always be subject to the legislative authority of Congress, and to that extent it is politically controlled and properly so. It must always act under the laws and powers granted to it by Congress and within the limitations of these laws. It is a different matter, however, to contemplate either the political domination or the political influence of the executive department of the Government. It is to such political interference rather than to the exercise of the undoubted authority of Congress that exception must be taken.

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Whenever a central bank acts, it is an important influence in making credit plentiful and cheaper or in making it more expensive. Someone is always benefited and someone at least temporarily is injured. It has always been so with banks of issue and always will. One consequence is that if the bank does its job properly it is continuously subject to criticism by someone.

It is for this reason that experienced governments generally, while having the undoubted power to take control of the delicate mechanism of the bank of issue, have found it wiser in the interest of Government itself to turn those functions over to an independent body as free as possible from political control or influence. Thus they have sought not only to minimize the abuses which might arise from the temptation to meet the temporary political exigencies of whatever party might happen to be in power, but also to insulate the executive himself from the continuous criticism that must be directed at a central bank whenever it does as it must so often do, the unpopular thing.

Therefore, Mr. Chairman, I look with apprehension not only from the standpoint of a central bank, but from that of the sound functioning of the Government as well, toward any increase of the powers and responsibility of the executive over the operations of the central bank and to any decrease in the independence of the central authority controlling the bank.

I should like to make an affirmative suggestion as to the constitution of this central body, if you get to that point.

Lest I be charged with making merely destructive criticisms, I suggest that if we are to concentrate our banking powers in a group in Washington that we add to the group in addition to the members of the Federal Reserve Board some at least of the governors of the Federal Reserve banks. If we intend to retain fully the regional character of the system, the governors should be a majority of the central body. If we wish to make the banking system, say half regional and half central, there should be an equal number of governors and members of the Federal Reserve Board on the body. If we wish to overweight the centralized character of the institution but retain some of its regional characteristics and benefits, we might have a majority of one, say, from the Federal Reserve Board, with the governors in a minority. If we create a larger majority than one from the Federal Reserve Board, and particularly if we make the election of the governors subject to the approval of the Board, then we have almost as complete centralization as if the governors were not represented at all. In my view, therefore, whatever the number of the central body may be, members of the Federal Reserve Board should not outnumber the governors by more than one at the very most.

The question has been raised whether the Secretary of the Treasury and the Comptroller of the Currency should be members of the Federal Reserve Board. In this respect I shall differ with most of the people, I think, who have appeared before the committee. I suppose the reason for this question is the very thing to which I have previously referred, namely, the increased power of the executive department over the central bank, and in the case of the Secretary of the Treasury the fact that he is specially interested in the money market so far as Government borrowings may be concerned.

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My answer to the question is that in principle I think that neither the Secretary of the Treasury nor the Comptroller should be members of the Board. We have, however, an unusual situation in this country today. Due to our change of the gold content of the dollar there is something like two billions of dollars in the hands of the Secretary of the Treasury available for operation in the Government market and over the exchanges. It is a fact, therefore, that the Secretary of the Treasury can, irrespective of any action by the central bank, dominate the money market of the country. So long as that fund exists uncontrolled in the hands of the Secretary of the Treasury and the President, I am in favor of retaining the Secretary of the Treasury as a member of the Federal Reserve Board and thereby imposing upon him that much responsibility at least for cooperation with the central bank in the handling of this vast stabilization fund. Personally, as I have testified before to this committee, I think that stabilization fund should only be administered through the central bank and should not be subject to independent operation in the money market. Therefore, as a matter of expediency only, I would yield the principle and not take the Secretary of the Treasury off the Federal Reserve Board.

As to the Comptroller of the Currency, I have always believed that the powers vested in that office should be administered by the Federal Reserve banks, but until that is provided for I can see many advantages rather than disadvantages from the retention of the Comptroller of the Currency on the Federal Reserve Board. I trust, however, that the reason for his membership, like that of the Secretary of the Treasury, may prove temporary only and that ultimately we shall have no political officers as members of the Board.

I want to speak now about the independence of the governors of the several Federal Reserve banks.

It is proposed in the bill that the governors of the several Federal Reserve banks, and the vice governors too for that matter, shall be appointed annually by the boards of directors subject to the approval of the Federal Reserve Board in Washington. This seems to me to be quite consistent with the evident purposes of the bill, and my interpretation of it. It is intended in fact, as I have said before, to create a central bank administered by the Federal Reserve Board in Washington, and the Governor of the Federal Reserve Board shall in fact become the governor of the central bank of the United States. The governors of the several Reserve banks will be practically only vice governors of this central bank, and it is natural that, as administrative officers of the central authority, they should be subject to a veto by the central authority each year on their right to continue in office. If that is the theory of the bill, as I think it is, then this approval of the governors is entirely consistent with it. That of itself, Mr. Chairman, seems to me to destroy the last vestige of initiative and independence in the regional banks. They are not even permitted to retain the power of selecting their own executives. It illustrates again how false and misleading the facade of the regional system is to be and how truly centralized our bank of issue is to become.

If it is intended to leave even a shred of responsibility in the boards of directors of the several Federal Reserve banks, the most that the central authority should be permitted to do in the selection

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of governors would be to approve any new man elected to that office as to character and ability, and thereafter leave the power in the boards of directors to reelect. I see no other way to relieve the governors of the several banks from the overhanging threat of coercion by the central authority. This at least will conserve some of the checks and balances of which I have formerly spoken. This is highly important, too, if the governors are to be represented on a central authority in Washington; otherwise disagreement with the members of the Federal Reserve Board by any governor may at least raise the question of the approval of his next election. Obviously, no one or more members of the central authority should have the power to disqualify any other member because of his vote.

Now, I want to say just a brief word on the effect of the enactment of this legislation on recovery.

What we are concerned with today, Mr. Chairman, is to take up our unemployment. Only business can do that. Then our State and local budgets will be relieved from excessive borrowing and taxation. Then our Federal Budget can be brought into balance and all fear both at home and abroad of an uncontrolled inflation may be avoided. That is a necessary step to the stabilization of our exchanges and the restoration of foreign trade. Only when that is done will our great agricultural exports freely move again and so insure again safety and prosperity to the farmers of the Nation.

The key to our whole situation, then, is business activity and particularly in the field of durable goods, where most of our unemployment now lies. As durable goods have to be financed on long time, that market is particularly sensitive to drastic changes or threats of change in our financial structure. Business in durable goods has undoubtedly been reassured by the failure of the Patman bill. It is still apprehensive about the political domination of our central banking system, with the resulting threat to the commercial banking system. Whether business should be apprehensive over the bill pending before you or whether it should not, views will differ, but the fact is that business is apprehensive. The passage of the bill, therefore, either because it is not understood or because it is, will to some extent retard business recovery. If there were any real reason for immediate action on title II, we should be compelled to enact it and accept the delay in recovery; but seeing no reason for action now, I feel that there would be great reassurance to business if a comprehensive study of our whole banking system could be undertaken instead.

We have vast reserves in the banks, more than 2¼ billions, the base for 25 billions of additional credit, awaiting use; an ample amount, certainly, to get all the expansion we need. We have done all the preliminary things that are necessary to do in finance. We have decreased the gold content of the dollar, we have increased our gold supply, we have reestablished confidence in the banks, we have enlarged the volume of our current business and gradually restored the shattered confidence of business men. The upward surge of a basic economic demand is ready now to break through our doubts and fears, and when it does, our credit resources will be put to work by business. It isn't the bankers who are holding back the credit. They are anxious to make it work, for in no other way can they earn their living. It is business which until now has been too apprehen-

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sive to use the credit. So I say the way to get recovery today—to get expansion, in fact, today—is to do nothing more and threaten nothing more to shake the confidence of business men. It is careful conservatism, not radical new departures, which will get now the activity which we so sorely need.

I oppose the enactment of title II of this bill, Mr. Chairman, not only because it threatens to retard recovery, but even more because it will postpone the banking reforms we need. It works from the top down rather than from the bottom up. It creates a central bank by indirection. It carries with it the threat and potentialities of political domination of that bank, not by Congress but by the Executive. If it is to be passed, title II at least should be so amended as to preserve the fact and not the shadow of our present regional structure. Concentration of authority should be protected by a regional representation which is adequate and independent. Some of the checks and balances of the present system should be preserved so that the sensitive controls of money and credit may be vested in a body which is free from the fact and from the suspicion of subservience to any selfish interest, whether of profits or of votes.

It is by the revision of our whole banking structure, the commercial as well as the Reserve System, that we may hope to correct the faults which have been disclosed and prevent the recurrence of the disasters we have experienced. Then, and not till then, will Congress have met its full duty and responsibility in giving the American people the kind of banking system they ought to have.

That is all I have to say, Mr. Chairman.

Senator GLASS. Does any member desire to ask Mr. Young any questions?

Senator McADOO. Mr. Young, I was not present when the early part of your statement was made. You touched upon the point, but I do not know whether you gave an answer to the suggestion which has been made, that if the Reserve Board could be created free of political influence, as you described it, whether you would consider it wise to confer upon it the exclusive control and direction of the open-market operations.

Mr. YOUNG. You have two problems before you, Senator, on that. You can destroy the regional system and create a central bank. If you are going to create a central bank, if that be the decision, then it is all important that you establish this body of control as free from all influences as possible in order that you may have something which you might term the "supreme court of finance" and protect the members as well as we protect the members of the Supreme Court. I think that is needed if you are to centralize that large power.

Senator McADOO. You consider that desirable whether we centralize it any more or not, do you not?

Mr. YOUNG. I do not think it is so necessary if you have regional representation, because then the body, within itself, carries, in a way, its own checks and balances.

Senator McADOO. I am chiefly concerned now about this concentration of authority over open-market operations.

Mr. YOUNG. Yes.

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Senator McAdoo. Assume it were decided that it is wise to concentrate that authority. Then, of course, I understand your point, that the authority which is to exercise the power should be free of political influence or domination in any way.

Mr. Young. Yes.

Senator McAdoo. Assuming such a body, do you think, in all the circumstances, that if no other changes, for instance, are made in the Federal Reserve System as it exists today, it would be wise to concentrate in that body control of open-market operations?

Mr. Young. No; I think if you are going into the business of concentration, Senator, you have to concentrate three powers, because I think they are all interlaced, and the exercise of one affects the others. You cannot fix responsibility, therefore, without concentrating the three in the same body.

One is the power to fix the rediscount rate, another is the open-market operation, and the third is dealing with reserves.

I can see no advantage over our present system in concentrating any one of those powers and leaving the others still scattered, because the action in one field has such a direct repercussion on the other.

Senator McAdoo. I was going to ask you about the other two. Do you think that if you should concentrate one the others would inevitably have to follow?

Mr. Young. I think they should. Otherwise you accomplish nothing.

Senator McAdoo. As I understand you, you do not think it would be wise to concentrate all those powers in any central authority, no matter how free it might be from political domination or control.

Mr. Young. I do not want to say that, Senator. I would say that if, on a complete revision of our banking system, commercial as well as Federal Reserve, it seemed wise to create a central bank, and we felt we could insulate the central authority adequately, it might be the best solution of the problem. It might be.

Senator McAdoo. Do you think that if those three powers we are discussing now were concentrated in a board such as you have been considering that that would in fact constitute a central bank?

Mr. Young. That is all there is to a central bank. The rest of it is all detail or administrative procedure.

Senator Couzens. There is one other question in connection with that. Do you believe that the reserves should be statutory or flexible, however the board is constituted?

Mr. Young. The power to deal with reserves, of course, is the power of life and death over your commercial banks. I would say that such a vast power as that ought to be protected to the greatest extent possible. My personal inclination would be to have a statutory limit within which the power might be exercised but beyond which it should not be exercised.

Senator Couzens. So that to some extent you believe it ought to be flexible?

Mr. Young. Yes. I certainly think it ought to be flexible within limits.

Senator McAdoo. Do you think there should be a maximum and a minimum or merely a maximum?

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Mr. YOUNG. I do not believe I am competent to answer that question.

Senator BULKLEY. In changing the percentage of statutory reserves, do you believe the board ought to be required to declare an emergency?

Mr. YOUNG. No.

Senator BULKLEY. It ought to be entirely free to act as it thinks best?

Mr. YOUNG. Yes. In any banking system, whenever anybody starts talking about emergencies, you have got one at that moment. You create it.

Senator BYRNES. If you did not have it before, you have it immediately?

Mr. YOUNG. You have it immediately.

Senator MCADOO. I think we all see that.

Senator COUZENS. May I point out, Mr. Young, that on page 3 of your memorandum you say this [reading]:

> So I have had the opportunity at least to observe the personnel and the organization of the central banks of the principal financial and commercial countries of the world.

You did not say whether you had any opportunity to study the operations of these central banks. I think there is quite a distinction between the organization of the personnel and the operation of the central banks, and I was wondering whether you had any opportunity to observe the operations of the central banks and could give us any advice in connection therewith.

Mr. YOUNG. Of course, I have watched their operations with considerable interest during these last years in all the countries.

Senator COUZENS. Have they operated well?

Mr. YOUNG. Yes. I think, on the whole, very well, considering the difficult conditions which exist in the world. The currencies of the whole world, unfortunately, are on a managed basis, not particularly because the financial people wanted them there, or the political people wanted them there, but because we have had such dislocations, economic dislocations, and then political dislocations in the effort to correct the economic ones, that the old international functioning of the gold standard did not work any more. I think it is unfortunate.

Senator GLASS. Do you know of any central bank, Mr. Young, that is permitted to manage the property and the deposits of all the other banks in the country?

Mr. YOUNG. No, sir.

Senator COUZENS. From your observation of all the personnel and the organization of these central banks, has any one of them stood out as more effective and efficient than any other?

Mr. YOUNG. It is very difficult to make the comparison, because they function under such different conditions. The Reichsbank, for example, since its restoration, has had exceedingly difficult problems. It is directed by a very able man in Doctor Schacht. The Bank of England has had its own peculiar conditions, and the Bank of France has had them and is having them.

Senator GLASS. There had to be a restoration of the Reichsbank.

Mr. YOUNG. A complete restoration, Senator. The nations of the world had to raise $200,000,000 in gold in order to reestablish the Reichsbank. We established a new reichsmark and provided for the

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exchange of the old reichsmarks at the rate of 1,000,000,000 of the old for 1 of the new. So you can see the extent to which the currency depreciation had gone in Germany.

Senator Glass. The Reichsbank was wrecked.

Mr. Young. Completely wrecked.

Senator Glass. Upon the issuance of its notes upon Government bonded indebtedness.

Mr. Young. Quite true. That is one of the reasons why I am saying that I think any bill here ought not to permit the central bank to take obligations of the Government direct.

Senator McAdoo. You mean long-time obligations?

Mr. Young. Yes. Temporary advances, of course, must be made. Such Government obligations as the central bank holds it should take in the open market. What happened in Germany was that the Government put its bonds into the Reichsbank, and the Reichsbank issued its notes against those bonds, and it was only just doing in a roundabout way what the Government might as well have done direct, by the printing press.

Senator McAdoo. Was not that done for a specific objective?

Mr. Young. A very specific objective. They were seeking inflation.

Senator McAdoo. They were seeking inflation for the purpose of destroying all debts, were they not, in large measure?

Mr. Young. They were seeking inflation partly for the purpose of reducing the burden of debt, but I think more largely, Senator, after the end of the war, for the sake of getting a better base for their exports.

Senator McAdoo. Whatever it was, it was not done just for no purpose. There was a definite objective.

Mr. Young. Oh, yes.

Senator McAdoo. In other words, that was the method employed, not because it was inflationary, but because it was the means by which they could accomplish the results.

Mr. Young. Quite true.

Senator McAdoo. And no other was available.

Mr. Young. I was in Germany several times during the progress of that. The result at the beginning was a stimulation of business. Business itself felt that under those circumstances it would be wise to have some inflation. Everybody was confident that that inflation, after having proceeded just to the right amount, could be stopped. It turned out, as it has always turned out before, that when you get that thing started there is no power to stop it, and so they rode to ruin.

Senator Glass. They did not happen to cut the heads off those fellows as they did in France in the revolutionary days, did they?

Mr. Young. No. They saved their heads.

Senator McAdoo. I do not think it necessarily follows that an expansion of currency under conditions that seem wise at the moment, if it is rationally done and properly safeguarded, results in such an infection that a fatal and malignant disease is going to pursue you to the death. I think it depends entirely upon the conditions and the manner in which this power is exercised.

Senator Glass. It does not necessarily follow, but it has historically followed.

Mr. Young. It has historically followed.

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Senator McAdoo. In other countries, yes; but when we deal with those things and discuss those things, I think we have to discuss them with reference to our own conditions and attempt to apply them here.

Mr. Young. My attitude toward inflation is this, Senator McAdoo—and this is why I am apprehensive about it: I am apprehensive for the same reason that I would be apprehensive if a man who had my most precious possessions began morphine. I would be troubled about that. I would be apprehensive about it. He might argue, and his friends might argue, that he was a good strong chap, and that a shot of morphine now and then did not hurt him, and relieved him a little from his depression of spirits. But, nevertheless, I would not feel comfortable or confident in going on with that chap any longer. That is the reason why I am so scared, as the chairman says, in the light of history.

Senator McAdoo. I do not think the analogy is good.

Mr. Young. Perhaps not.

Senator McAdoo. Nevertheless, while I am not arguing for inflation, what I have been very much interested in is to find out, if possible, where inflation begins. Take the conditions of the country today. Are we on an inflation basis now?

Mr. Young. No; I do not think we are.

Senator McAdoo. Why not?

Mr. Young. That may require definition.

Senator McAdoo. Exactly.

Mr. Young. That is, as to what you mean by an inflation basis. If you mean that we have had so much expansion and we have so much currency and credit in use that we have inflation, I say "no", of course. If you mean to ask whether we have the base on which to get it, I say "yes."

Senator McAdoo. We have created all the evil potentialities, undoubtedly.

Mr. Young. We have what?

Senator McAdoo. We have undoubtedly created all the evil potentialities of which you speak.

Mr. Young. No.

Senator McAdoo. In other words, we have an abundant supply of morphine. It is a question of whether or not it is going to be used.

Mr. Young. We are not in danger because it can only be expanded as business uses it. That is a check, and that is a very real check.

Senator Glass. Adverting to your statement of your observations of central banks in other countries, do you know of any central bank the chief managers of which have not had considerable banking experience and observation of banking policies and technique?

Mr. Young. Every central bank that I know of has officers who have had experience.

Senator Couzens. If you had to reorganize the Federal Reserve System and set up another form of centralized control, have you any plan of your own that you think would be adaptable to it?

Mr. Young. I have not, Senator.

Senator Glass. But if charged with the study of the problem you might have, might you not?

Mr. Young. Indeed.

Senator Glass. You could not do it overnight?

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Mr. YOUNG. Quite so, because the problem is so complex; and because I think it has not been adequately studied is the reason why I say that I see no occasion now for the enactment of such a bill as is proposed. That does not mean that I am opposed, necessarily, to many of its provisions, but I think it will delay the comprehensive reforms that we need in the banking structure of the United States.

Senator MCADOO. With 49 different banking systems, I have to agree with you that it is a very complex problem.

Mr. YOUNG. Very.

Senator COUZENS. Do you agree with General Dawes, that we are going to have a comeback in July?

Mr. YOUNG. I told the General that it was all right to be a prophet, but he should not fix the date.

Senator MCADOO. Sometimes good prophets are wrecked by dates.

Senator COUZENS. You do not contemplate, then, that before any general revision can be made such as you have suggested, there is likely to be a runaway market in the heavy goods industries?

Mr. YOUNG. I am not that optimistic, Senator, certainly.

Senator COUZENS. Have you any optimism with respect to that, that there is going to be a fairly quick comeback in the use of heavy goods?

Mr. YOUNG. It depends entirely on whether or not the reviving confidence is shattered again or whether it can be continued and built up. There is a great underlying demand for durable goods in this country, and if we could get the road cleared to finance them and have confidence on the part of people to buy them, they would revive very quickly and in very large volume, in my judgment.

Senator MCADOO. Do you think our $4,000,000,000 is going to help in that regard?

Mr. YOUNG. I do not see how it can, very much. That is one of the fields where I see no way that the Government can reach it. If we could build one or two million $5,000 houses in this country, small houses which are greatly needed, it would do more than all the appropriations that the Government could make toward a restoration of the durable goods industry and the taking up of the slack in unemployment.

Senator MCADOO. There is no question about the fact that it is to be employed in useful work and that there will be a distribution in the matter of materials.

Mr. YOUNG. I think you will find, Senator, that it will have only a slight repercussion in the material market. Much of it has got to go for labor, and therefore it will have a repercussion on goods of current consumption, much more than on durable goods, I think. Durable goods require great plans, for example, long planning, a long time for fabrication, and they are not very suited to the quick employment of the $4,000,000,000 which is needed to relieve the distress.

Senator BYRNES. Assuming that $2,000,000,000 of the $4,000,000,000 were spent for material, what effect would an expenditure of that size have?

Mr. YOUNG. I cannot conceive that there would be any such an amount as that spent for material; and if there were it would not have a tremendous effect on the durable-goods market, on the material market, because that field is so large and runs into money so rapidly. You see, a million small houses, which is not a very large amount for this country, at $5,000 each, which means $5,000,-

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000,000—that, of course, would have tremendous consequences, a repercussion on the whole durable-goods field.

Senator COUZENS. What would you suggest might be done to restore the confidence of the investors in durable goods that you spoke about a while ago?

Mr. YOUNG. I made the statement here this morning, Senator, that I think now the less we do and the less we threaten to do, the quicker confidence will be restored and the quicker we will get recovery and prosperity in this country. We have done enough now.

Senator COUZENS. You mean, we ought to adjourn and leave everything as it is?

Mr. YOUNG. I think that would be very good.

Senator MCADOO. Will you make a motion to that effect? I might support it.

Senator BYRNES. Have you felt that way ever since 1931 and 1932?

Mr. YOUNG. Oh, no, indeed; not until we had to clear away a great deal of the impediments. We had to enact a great deal of legislation and clear the ground. But we now have, as I said, perfectly sound banks. The people have confidence in them. They have two and a quarter billions of unused credit in those banks, which is a base for $25,000,000,000 of operating credit, and the only question is to get business to use that $25,000,000,000 of operating credit. It will use it the moment it has confidence, because I think the economic needs are here; but it will never use it as long as confidence is impaired. Therefore, I would say that we ought to stop now and take a breathing spell and do nothing and threaten nothing further.

Senator GLASS. Thank you, Mr. Young.

(The witness withdrew from the committee table.)

STATEMENT OF GEORGE L. LE BLANC, NEW YORK, N. Y.

Senator GLASS. Give your name and occupation, please.

Mr. LEBLANC. George L. LeBlanc. I was born in Montreal, Canada. I am an American citizen, and I have been engaged in the banking business all my life.

Senator TOWNSEND. Where?

Mr. LEBLANC. New York City. I have been the senior vice president of the Equitable Trust Co. of New York and, simultaneously, president of the Equitable Eastern Banking Corporation and later president of the Interstate Trust, of 37 Wall Street, New York City. I have had many conferences with the governors of central banks abroad, because most of my experience has been in the foreign banking field, in which I probably have financed more imports and exports than any other banker in the country.

I thank you, Senators, for giving me the privilege of addressing you. It will only take a few minutes.

Our primary objective is to restore and maintain our national economic existence, which must prevail. The most important mechanism to secure this result is now under probe—our banking system.

We now have a privately owned bank, owned by bankers, primarily a reserve bank for bankers, controlled by 108 directors, 13

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boards, which are in turn separately governed by 13 governors, and in addition to this we have nearly 3,000 State legislators who can also legislate banking measures.

The already-proven inefficiency of this outworn banking system, accompanied by mistaken leadership, has been powerless in preventing the worst financial calamity in the world's history. Therefore, it is imperative that we should take necessary steps to prevent future occurrences of that kind. You may be surprised to hear that as far back as 1918 the leading bankers of New York were well aware that the Federal Reserve could not cope with a serious banking panic, which has since been demonstrated. This must of necessity be changed.

While the banking amendment of 1935, intended to liquidify the good banking assets and to protect further the Government's credit, is honest in purpose and much needed, however, it is unthinkable to put the Government permanently in full control of the Nation's banking business. You may put me down on the side of the bankers in opposing this legislation.

On the other hand, I believe that the banking control should be put under neutral leadership, and not in the hands of the administration or arbitrary selfish interests.

Overlooking the political reactions, the banking leadership evidently would allow the enormous debts hanging over this country to be partly decapitalized through the bankruptcy courts, while the administration, cognizant of this fact, would use the resources of the Federal Reserve, privately owned, to prevent the ravages of such a policy. No doubt you readily realize that, as long as the Federal Reserve stock is held by banks, its resources cannot be used for political purposes. The stocks of similar banks throughout the world are held in the hands of public citizens. It is undoubtedly a wise step.

On my part, I would much prefer to have a bill such as the Nye-Sweeney bill, because it has the essence necessary to create a sound and practical national banking system, as free as possible from selfish motives, while benefiting and protecting our economic existence, including our banking system. It has also much more potency in regulating bulges, which have in the past been seriously detrimental to our economic life.

The Nye-Sweeney bill is the base of what should be enacted by this Congress. It must follow the course of all legislation with minor correction of detail in this committee and on the floor of the House of Congress. It should not be left to the selfish interest of bankers or politicians to remodel. It should have the aid of impartial, honest critics to refine it.

Probably later on I will read another statement about our situation, but in the meantime I wish to say that a Federal Reserve bank is a reserve for banks. It is an arrested development. We are artificially trying to make it Federal on top of that. It is most important, judging from the experience of the banks of Europe, which have had a great deal of experience, that the leadership must be put in neutral hands, somewhat along the line of the Supreme Court of the United States, which has the confidence of the country. We are going to meet many serious problems, and if the blame is put on the banks according to the present system I do not think it would be wise.

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Senator BYRNES. How about the provision in this bill that "the board of directors of the Bank of the U. S. A. shall be composed of one representative from each State, elected by the people thereof"?

Mr. LEBLANC. That is one thing that I shall cover in a paragraph. It has to be reconstructed in the best interests of our country.

Senator BYRNES. I understand that you are going to discuss that later?

Mr. LEBLANC. I am going to discuss——

Senator BYRNES. Are you in favor of that provision?

Mr. LEBLANC. I am in favor of many provisions of that bill.

Senator BYRNES. I mean, of this particular provision, that the directors shall be elected by the 48 States.

Mr. LEBLANC. I will leave that to people who are more versed in it.

Senator BYRNES. What is your view about it?

Mr. LEBLANC. I believe that the men that should be at the head of this supreme court of banking should have no interest in any other activities; that their money should be in governments and municipals. They should be provided for for life, which makes them as neutral as possible.

Senator BYRNES. This provision of the bill reads as follows [reading]:

> The board of directors of the Bank of the United States of America shall be composed of one representative from each State, elected by the people thereof at the same time and by the same method as Representatives in Congress, for a period of 12 years.

Mr. LEBLANC. If that is the best neutral way of selecting these officers, I am in favor of it—unless you show something better.

Senator BYRNES. What is your view of it? Is that the best way that you know of?

Mr. LEBLANC. That I know of.

Senator BYRNES. To be elected by the people for 12 years?

Mr. LEBLANC. It might be better for each legislature of each State to appoint its director.

Senator BULKLEY. Do you mean that that would be the best way to keep it out of politics?

Mr. LEBLANC. The principal thing is that these men cannot have any outside interest.

Senator BYRNES. You call that a "supreme court of banking", and you want them to have this power?

Mr. LEBLANC. To have no interests whatsoever outside of their positions, and not be dependent on any outside interest.

Senator BYRNES. All right.

Mr. LEBLANC. For instance, a good many banks in Europe have that same clause, and I think it is the only proper way to handle it. Unless we have something better, I am for that.

Senator COUZENS. Do you have any other statement to make?

Mr. LEBLANC. I want to make another statement. For years I have faithfully served my masters. Now I have no master but myself, and I come down here to serve my country in the matter of public policy in the most important question of the hour, namely, the money and banking question.

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We are facing a serious crisis, and I came to tell you the truth so that you might be guided.

Gentlemen, if we had been told the truth, and had faced the facts, we would not have gone down the way we did. When England went off gold, that automatically made our banks insolvent, and if we had faced the facts then, instead of trying to cover them up, we would not have gone down in a catastrophe as we did. That is one of the important points. With a neutral bank, from a neutral standpoint, we would have stopped that and prevented going down the way we did.

Senator BULKLEY. What would have been the method?

Mr. LEBLANC. To immediately go off gold. In 1927 I was with the Deputy Governor of the Bank of France. I loaned him one of our men to help out their stabilization in 1927, and according to all economic laws 1927 was the year in which we were due to have just what we went through. One of the leading English bankers went to see the President and spoke to him, and at that time I knew what the conversation was, what this country was due to go through, but on account of the boom we had it was delayed. If we had had a central bank run by unselfish interests, we would not have had this tremendous bulge on the way up, and the consequential depression.

Senator COUZENS. The only thing you recommend to have done at that time was to have gone off gold?

Mr. LEBLANC. There was nothing else in the world.

Senator COUZENS. Was that the only thing to have done?

Mr. LEBLANC. There was no other thing to do. On account of the economic life of the world it could not be avoided. England tried to do its best, and on a Friday they had a meeting of the leaders and they said, "We cannot open our banks and stock exchange on Monday." But they did not let them close. They went off gold.

Senator GLASS. England had about $20,000,000, and this country had 43 percent of the gold of the world.

Mr. LEBLANC. But, Senator Glass, England had a foreign investment of probably $15,000,000,000, practically the equivalent of gold. To make the statement that England went off gold because she had no gold is all right for people's consumption, but not for right-thinking bankers.

Senator GLASS. It is a fact, is it not?

Mr. LEBLANC. I never believed it, Senator. Do you know, Senator, that the banks had several hundred millions of gold in their vaults at that time, when they went off gold, and England had a foreign credit balance of perhaps $15,000,000,000, which is the equivalent of gold, and yet a country like that has to go off gold because she has no gold? It is unbelievable.

Senator GLASS. The Bank of England had about $20,000,000 in gold when she went off the gold standard.

Mr. LEBLANC. The Bank of England's statement showed about $650,000,000 gold when they went off, and it did not include in that the gold that was in the English bank vaults.

The surplus gold of the Federal Reserve System should have been kept in the coffers of our American banks instead of letting the public have it. The minute the public had it I said then, "You will lose all your gold." And that is just what happened. It was badly led at that time, and that is what brought on these results.

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Let me tell you this economic policy. I do not have to apologize about the technique of it. I have discussed these domestic questions with the foreign governments, with the governors of various Federal Reserve banks in their handling of the situation. We were friends. I knew their inner minds. In 1924 we started our economic policy here which led us to this tremendous boom. England was shipping gold to us. They wanted a higher price level so that they could dump their goods here. The manufacturers and the corporations were called in, and they said, "Gentlemen, don't reduce your wages; don't reduce your earnings, but you must reduce your costs." So they said, "We can only do that by mass production." The question was asked, "How are we going to dispose of goods manufactured by mass production?" They said, "We are going to enter into a policy of foreign loans. That will automatically develop a purchasing power in this country and abroad and you will be able to dispose of your mass production."

That was the beginning of the pyramiding of these foreign loans. In 1929 we called a halt. "No more loans. Pay us."

Well, first, the foreign countries started to put up their tariffs to protect themselves. They started to form exchange control. They started barter; they started cartels, and finally they developed their armies. In 1929 we used a wrong policy. We should have said, "We have made fools of ourselves in this orgy of lending. Let us nurse it through now." But we said, out of a clear sky, "You have got to pay us." Then the whole world became gradually driven to chaos, and ourselves the same way.

Senator GLASS. Do you discuss the provisions of the bill in your statement? If you do, I think we would better have your discussion of them.

Mr. LEBLANC. All I mention, Mr. Chairman, is the control of the situation. I am not so interested as to the first candlelighter and the second candlelighter and who is going to light the candle. I am only talking of the control, because, after all, the control will be what will determine a great deal of the construction of the bank.

Senator BYRNES. May I ask you one further question? I call your attention to this provision of the Nye bill [reading]:

> Within 1 year after the passage of this act all banking institutions under the jurisdiction of the Bank of the United States of America shall be required to keep on deposit with the Bank of the United States of America, or in its vaults, United States bank notes herein provided for a full 100 percent of its deposits which are subject to check and payable on demand.

What do you think of that?

Mr. LEBLANC. I myself would be in favor of keeping a lower amount of demand deposits, starting with 15 or 20 percent, so when the banks are overloaned and the deposits are withdrawn, they do not have to dump securities over.

Senator BULKLEY. Fifteen or 20 percent of what?

Mr. LEBLANC. Of currency against demand deposits.

Senator BYRNES. Have you studied this bill?

Mr. LEBLANC. Yes; I did, sir.

Senator BYRNES. What do you think of this provision?

Mr. LEBLANC. I am interested in the essence of this bill, but I do not see——

Senator BYRNES. You do not agree with that provision?

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Mr. LeBlanc. Well, no. Frankly, gentlemen, my opinion is that it would be probably better to have 15 or 20 percent. Every bank in the world carries more currency than we do.

Senator Byrnes. It says further (reading):

and, in addition thereto, it shall keep within its vaults the further sum equal to 5 percent upon all savings or investment deposits, commonly known as "time" deposits.

Mr. LeBlanc. Yes.

Senator Byrnes. A hundred percent of all deposits subject to check?

Mr. LeBlanc. Yes. I would say 15 or 20 percent, and then it would be left to the head of the bank to determine the reserve of currency.

Senator Byrnes. You would change that to 15 or 20 percent?

Mr. LeBlanc. Yes.

Senator Couzens. Have you any comment to make on the Eccles bill as it passed the House of Representatives? That has been more currently discussed. Have you any point about that?

Mr. LeBlanc. It is an emergency affair. It is only an emergency affair; I am not so opposed to it in one way, because we need it. If our first mortgages in the savings banks and insurance companies are not liquid, we are going back the same old route of insolvency. They must be made liquid.

Senator Couzens. And if we cannot get the Nye-Sweeney bill through at this session, you would not oppose the Eccles bill; is that right?

Mr. LeBlanc. I would not oppose it, provided it is not permanent.

Senator Couzens. Well, nothing is ever permanent, with Congress changing every few years.

Mr. LeBlanc. I am entirely opposed to the Government controlling the banking situation, because they can inflate just whenever they wish to protect themselves, and the banking interests are opposed to that.

Senator Byrnes. You favor the purchase of the stock of the Reserve banks?

Mr. LeBlanc. As long as the stocks are in the hands of the member banks I do not see why anybody would play football with their resources.

There should be an intelligent nursing policy of long international credits against purchasing of goods from this country. This includes stabilization of the currencies of the world.

Long-term domestic credit will not be resumed by private banking until this stabilization is accomplished.

Private banking will remain on strike until stabilization is accomplished. Without it we have only central banking as an alternative.

The only source of long-term credit today is Government credits.

The whole domestic reconstruction program must rest upon breaking the strike of capital. As long as the debt structure is at its height it cannot be paid on present low income. The bankers would like this excess debt wiped out.

What a conservative should stand for is some plan to save the ravages of such a policy which will inevitably lead to another banking moratorium.

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Central banking, independent of misguided banking interest and independent of political influence, has promise as never before.

Senator COUZENS. Is that all that you have to say?

Mr. LEBLANC. That is all, unless you have some more questions.

Senator GLASS. We will recess now until 2 o'clock, and will meet in the Appropriations Committee room in the Capitol.

(Whereupon, at 12:05 p. m. a recess was taken until 2 p. m. to meet in the room of the Senate Committee on Appropriations, in the Capitol.)

AFTER RECESS

The subcommittee reconvened at the expiration of the recess, at 2 p. m.

[Uncorrected]

STATEMENT OF HENRY PARKER WILLIS, ECONOMIST, NEW BRIGHTON, NEW YORK CITY

Senator GLASS. Give the reporter your name, address, and occupation.

Mr. WILLIS. My name is Henry Parker Willis; residence 215 Prospect Avenue, New Brighton, New York; profession, economist. The only part of my professional career that I think is germane to the present proceeding is that I was associated with the House Banking and Currency Committee during the time that the Federal Reserve Act was under consideration, and I was then secretary of the Federal Reserve Board during its first 4 years.

Senator GLASS. You were secretary when the position of secretary was of an advisory nature.

Mr. WILLIS. Yes.

Senator BANKHEAD. What period were you secretary?

Mr. WILLIS. From 1914 to 1918. Then I was economist of the Board. I think I had the title of economist of the Reserve System during the following 4 years.

Senator TOWNSEND. From 1918 to 1922.

Mr. WILLIS. From 1918 to 1922. I organized the statistical services of the Board and started and edited the bulletin during my term of office.

How shall I proceed?

Senator GLASS. You had a large part in drafting the original Federal Reserve Act, and therefore you were adviser to the Ways and Means Committee when Senator Underwood was chairman, I believe.

Mr. WILLIS. Yes; for 2 years.

Senator GLASS. You are now professor of banking at Columbia University?

Mr. WILLIS. Yes.

Senator GLASS. You understand what we have under consideration—this bill to reorganize the Federal Reserve Banking System. I would be glad to have you express any views you might entertain on the subject.

Mr. WILLIS. Is it your wish that I present a prepared statement, Mr. Chairman?

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Senator GLASS. If you have one prepared.

Mr. WILLIS. I have one that I have prepared, and with your permission I will file it. In order to save the time of the committee I will briefly summarize it, and then add some comments on the bill.

Senator GLASS. Very well.

Senator TOWNSEND. Are you discussing all parts of the bill?

Mr. WILLIS. Of course, there are many things in the bill that I should like to discuss in detail, but I think time will not permit. I shall present merely a general survey of the bill.

Senator TOWNSEND. All three titles?

Mr. WILLIS. Generally speaking; yes.

Gentlemen of the committee, my statement here covers three sections. The first is an argument as to the necessity of the bill at this time. The second is a discussion of the general purport and content of the bill itself; and the third part consists of some suggestions and recommendations with reference to technique in the bill, assuming that it is practically unavoidable to go ahead with the bill at this session of Congress.

In a general way, perhaps the matter I consider most important in what I have to say is to recommend as strongly as I can that the legislation be deferred and not acted upon at this time.

Senator COUZENS. You refer only to title II when you say that?

Mr. WILLIS. I refer to the whole bill.

Senator COUZENS. Titles I, II, and III?

Mr. WILLIS. Yes, sir; unless title I can be considerably altered. I will explain that briefly in a moment.

Senator COUZENS. Is not title I necessary, in view of the Federal deposit insurance?

Mr. WILLIS. I think some portions of it are very desirable. At least, it is very desirable to have those topics covered, because I think the Federal Deposit Insurance Corporation is not now in a position to meet any serious emergency. If that be true, the sooner something is done to put it in a stronger position the better we shall be.

With reference, gentlemen, to the whole question of the immediate necessity of the bill, I want to say that we are officially assured that the banking situation is most satisfactory now; that the recent emergency is over; and that there is no difficulty at all with present banking conditions. If that be true—and I am merely stating what has been officially announced—there would seem to be no good reason for proceeding with any such bill, or, indeed, with any bill, at the present moment.

Senator BULKLEY. What official announcement are you referring to?

Mr. WILLIS. The report of the Comptroller of the Currency. In the first paragraph or two of his report, he states that in so many words, I believe.

Senator BANKHEAD. What is your present relation? What is your present connection?

Mr. WILLIS. Professor of banking at Columbia University.

I will give you the reference to that report of the Comptroller of the Currency a little later, Senator Bulkley.

Senator BULKLEY. It is quite all right. I just wanted to identify the statement.

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Mr. WILLIS. Generally speaking, the question whether any such large bill should be enacted at the present time seems to me to be largely a question of whether the material is ready for it, whether we are prepared for it at the present moment and are in a position to enact a final measure that will cover the whole ground. At the present moment it seems to me that that is not the case.

Our monetary policy at the present moment is certainly not settled, and it would seem it cannot be settled for some time to come. There are various portions of this bill that seem to me unfeasible, or, at least, not applicable until one knows what the monetary policy of the country is likely to be in the near future, and if there be any prospect of getting a definite solution of that before a great while, the bill would profit a great deal by being deferred until that time.

In the second place, it seems to me that the bill as it stands now is based upon what I hope will be a temporary emergency in public financing, and one which, if it should pass without serious disaster, would pave the way or permit a very different type of measure from this one.

In the third place, it seems to me that the situation as it stands now necessarily looks forward to a condition of affairs in business and the commercial paper situation that is almost certainly temporary, and until we can see how that is coming out, it seems to me unwise to enact a comprehensive measure of this sort.

Furthermore, many of the powers that are conveyed in the bill here are those that are already enjoyed under emergency legislation, or at least have been exercised by an interpretation of the existing rules and enactments of Congress, so that in fact you are getting, under existing legislation, about all that can be said to be needed under existing conditions without actually having the matter put into permanent form as a constituent act for our banking system.

The great objection to this bill, as it seems to me, is not that it is going to change immediately very drastically what is actually being done at the present time. I am not one of those who look upon the bill as a measure that will immediately bring disaster. I deprecate extreme statements of that kind that are frequently heard at the present moment. The harm in it is that it seems to me to consolidate the bad tendencies in existing legislation, and practically renders them permanent, and treats them as the fruit of valuable experience during the emergency of the past 2 or 3 years, and thus seemingly looks forward to their remaining on the statute books indefinitely.

As against that, it seems to me that what we have done under the stress of emergency, whether right or wrong, should be regarded as definitely emergency legislation, and as such, not to be sanctified or accepted as a permanent basis until we can be perfectly sure the the emergency has passed, and that we know exactly in what direction we are going to go.

Furthermore, there is certainly a very large amount of difference of opinion about this proposed bill. By that I do not mean a controversial, hasty, or superficial opinion, but I mean that the measure as it stands raises some essential differences of view which are supported on either side of the discussion by weighty argument, and which ought not to be hastily dealt with.

I feel in disagreement with some of the statements in your hearings here, to the effect that the bill is based entirely upon the

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experience of the past 20 years; that no amount of investigation will alter the teaching of that experience; and that consequently Congress is in as good a position to enact it now as it ever will be.

On the contrary, it seems to me that the experience of the past 2 or 3 years, particularly, and in a good many cases of the whole 20 years of the life of the system, is open to very dubious interpretation, and that that deserves a great deal more care and thought in ascertaining what the meaning is than it has ever thus far received.

This, however, is not a plea for indefinite delay. On the contrary, I am fully in agreement with the radio address of Governor Eccles on last Sunday night, I believe—I read it in the newspapers on Monday morning—in which he says that we certainly should do very wrong if we failed to enact legislation designed to correct the evils and bad features in our banking system, especially those that have been developed as the result of experience during the past 3 or 4 years, and that the matter ought to be taken in hand at once. I agree with that fully, but I think the best way in this case to make haste is to proceed slowly and to get competent advice in the matter.

To that end it seems to me the best results would be obtained by appointing a small commission, such as has been recommended by various commercial bodies, with orders to report promptly. Its life might very well be limited to 6 months, or something of that kind, so that it would report before this Congress came again into session.

To that Commission, it seems to me, should be referred the task of finding out exactly what the opinion of experienced men in this country points to as the desirable change in our banking legislation. That such a Commission could wholly overcome all differences of opinion and all prejudices I do not for a moment believe, but I think that it could iron out a great many things, and bring about satisfactory compromise on a good many things, and definitely indicate the lines within which a great statute of revision should be enacted.

In those circumstances I believe that a Congress meeting in January next would be in a far better position to legislate than this one can possibly be, with all due respect to the care and thought that has been given to this matter by the members of the committee.

Furthermore, it seems to me clear that if time will warrant it, another Commission, or a subordinate commission or group in the employ of this first one could codify the National Banking Act. I have been recommending this, by the way, at intervals for the past 10 years, so that it is not a mere emergency proposition. Our banking laws are now full of contradictions, obsolete material, and data that do not exactly fit the situation, and provisions that have been held ineffective or unconstitutional, or otherwise unsatisfactory. A code commission, composed in part of competent lawyers, and some economists, perhaps, would be able to solidify and consolidate our banking statutes, both those relating to commercial banking, investment banking, and agricultural banking, relate them closely to one another, rearrange them, and, without changing anything except the matters I have just spoken of as being obsolete or out of place, establish a workable statute that can be understood by everybody, and will not be constantly giving rise to reinterpretations or revocation of old interpretations.

In addition to this, it seems to me that while I am aware that, of course, nothing of the kind could be put into legislation, it would be

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desirable if there could be a general understanding or agreement that whatever was done by Congress was going to remain on the statute books for a period of 5 or 10 years without any changes other than those that are necessary to correct obvious errors or meet new conditions. In Canada there is a decennial revision of the banking act, and while minor changes occur from year to year during the 10 years, it is understood that there will be no general recasting, no fundamental alteration, in the intervals between the decennial enactments.

Banking processes are slow. They produce their results only after a lapse of time. It is not well to be changing them from year to year. The fact that that is done unsettles business, prevents bankers from ever really learning the law, and, of course, prevents administrative authorities from applying it very thoroughly or satisfactorily.

If something of that kind could be agreed upon, so as to give the country surcease from banking legislation for a while, it seems to me it would be one of the most helpful things that could possibly be done. We have enacted, in the past 20 or 25 years, 25 or 30 alterations in the Reserve Act. Some of them have been important, and others not very important, but there was no reason why a good many of them could not have been saved, carefully refined by the Reserve Board and its staff, and eventually put into law at the designated periods. That, it seems to me, would enormously have helped the situation.

There is one final reason I have to present in behalf of such postponement as I have spoken of, and that is the exceedingly dangerous and delicate situation of banking in this country at the present moment. The fundamental difficulty there is not, as many have supposed, unwillingness of the banks to lend. On the contrary, they are morbidly anxious to get out loans and to pay their expenses. This subject has been carefully investigated by various bodies, notably by the Industrial Conference Board in New York, as well as by others, and a glance at their monographs, as well as a very limited amount of personal investigation, I think, is convincing on that point.

Then why do not business men borrow more freely at the present moment? One reason, of course, is that they are doubtful about the future, and unwilling to make long-term commitments pending the time when they can find out exactly what their standard of value will be, and exactly what the conditions of repayment may be. But, in addition to that, you have the fact that the Government is steadily taking business away from the banks through its various financial organizations. Governor Eccles has courageously called attention to that in his testimony here before you the other day. He says [reading]:

> Our banks have been losing a large part of their business to the Government which has sold its bonds to the banks and has used the funds to make mortgage and other loans, many of which the banks should be in a position to make themselves. Unless the banks regain some of the business which has been taken over by the Government credit agencies, there will not be sufficient business to support the banking system.

That is profoundly true. Governor Eccles adds [reading]:

> There will also be great pressure for a constantly growing public debt incured in part in taking over business that could be done by the banks.

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Senator BANKHEAD. The banks were not willing to lend at the time the Government agencies took over this business. What have you to say about that?

Mr. WILLIS. So far as I have been able to look into it, I have felt that the banks, like other people, were subject to the same psychological hesitations.

Senator BANKHEAD. I am not criticizing them.

Mr. WILLIS. I do not know why you should not. I criticize them a great deal.

Senator BANKHEAD. My inquiry is not for that purpose but to bring out the reason for such a situation. If the Government went into this lending business at a time when the banks would not do it, was it objectionable?

Mr. WILLIS. I think it was, because I do not think the banks were anything like as reluctant as they have been supposed to be, and I think the pressure for very low rates of interest has greatly contributed to the expansion of these lending agencies. I was about to say, if you will allow me to finish this one note, that that situation is very well reviewed in a table regularly printed in the Federal Reserve Bulletin, and appearing in the May number, on page 279, which reviews the operations of the various lending agencies of the Government. One has only to look at that in order to realize the speed with which these agencies are rapidly taking over the entire business of banking throughout the United States.

One of the latest such agencies to be developed in that way is the so-called "savings and loan associations" which, as I understand it, are organized with a contribution of $3 of the Government's money to one of private funds. If my information is correct, they are now being organized in New England with permission to take time deposits at 3½ percent, while the old New England mutual savings banks can pay only 2½, or something of that kind. So that you have a strong impetus to the shifting of savings and long-term business to Government agencies. The men who run the Government agencies are naturally humanly desirous of making a showing and indicating big transactions, and the like, and they do what they can to bring that about.

Then there are the production credit corporations, which are reported here in this table as having aggregate assets, other than interagency, amounting to $121,000,000. After a very short period of months they are paring off the business of the banks at the other end. That is to say, they are taking the liquid business of the banks, moving the crops, and so forth, while the mortgage lending concerns are undercutting the banks foundationally. At that rate you are soon going to have a condition in which banking is much more highly governmentalized than it is today. Suppose that continues for some time hence—I do not know how long. The time may come when we ought to decide whether we are going to definitely socialize the business of banking, as various persons have urged, and have the Government take it over and do it all or to what extent you are going to do that, and where you are going to draw the line between them. It is the same question that the Russian Government has had to settle in its own way, as to just how far it was going to go in carrying on banking as a Government monopoly.

Senator TOWNSEND. How did the Russian Government settle it?

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Mr. WILLIS. It settled it, according to my understanding when I was over there, by taking over for itself the entire financing of all industrial business, everything involving capital loans, and leaving the agricultural financing in substantial measure to the local associations of peasants engaged in agricultural lending. But it has been very unsatisfactory, and there has been a great deal of feeling there, I believe, even among good Communists, that it would be better to allow a substantially larger amount of initiative in banking to private enterprise.

For those reasons it seems to me that you will do a very much better and more satisfactory job a few months from now, if you order in the meantime a fairly careful, quick summarization of conditions by a group which, while not more competent than Members of Congress to do the job, is outside the milieu in which Congress exists, and I hope would also be outside the financial milieu. That is to say, you would get the opinion of a small group of men of standing and probity—not necessarily bankers—as to just how far it was desirable to have this country go in socializing the credit. You are on the road to a very complete socialization of it now, but it is a haphazard socialization and one which can only result in disaster because of the dangers that arise from the diversion of capital and funds in directions that duplicate one another, and which thus repeat and intensify the evils of the old banking regime, which were numerous.

That, generally, summarizes the first part of what I have to say.

Senator BANKHEAD. Let me ask you this question. I am interested in what you say. Do you believe that the conclusions reached by a commission of that kind depend very largely upon the philosophy of the members of the Commission, the preconceived philosophy?

Mr. WILLIS. I am quite in disagreement here with Governor Eccles, who states in his testimony that differences of opinion on the proposals contained in title II of this bill are not the kind that can be resolved by study. I am of the opinion that any differences of opinion can be resolved by study on the part of open-minded men, and I see no reason whatever why you should not have the substantial differences of opinion here fairly well ironed out and reduced to, perhaps, something not that all will agree to, but something that all could support. It is very desirable that whatever you do here should have the substantial support of the financial community and of everybody concerned.

Senator COUZENS. Did the Federal Reserve System have that support generally?

Mr. WILLIS. Generally speaking, I believe it did. Bankers, I hasten to say—a good many of them, at any rate—were recalcitrant and threatened to give up their charter—that is, the national banks—while the State banks said they would never join. The fact is that within a year that had entirely disappeared, and you had practical agreement. I believe it is true that before the Federal Reserve System was enacted all except very intransigent bankers were convinced that the essential ideas of the Reserve System would work, and while they were not particularly pleased with them, they had, as reasonable men, to say that they would be substantially satisfactory.

Senator GLASS. Was it not a fact that the antagonism of a large part of the bankers at that time was brought about by a sort of

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idolatry? In other words, Senator Aldrich, who was at the head of the Aldrich commission, and who bitterly assailed the Federal Reserve proposal, was a master financier, and he practically dominated the American Bankers' Association, and controlled banking opinion largely.

Mr. WILLIS. Very largely. Where you have a few outstanding personalities who are determined to do something you get that result. The trouble with our banking community at the present time is that there are a few or no outstanding personalities in it; and that many of those are afraid of being investigated, as they frankly admit, while a great many others are—well, unwilling to speak for themselves. So that at the present moment we have no leadership in the banking community. If that were merely my own expression of opinion I should hesitate very much to give it publicity here, but I have heard a great many bankers express that opinion themselves.

Senator COUZENS. What is it that they have done that they do not want to be investigated about?

Mr. WILLIS. I think this committee can find out much better than I, and I should like to know myself, so the question is referred back to the Banking and Currency Committee.

Senator GLASS. Doctor, before you get off that phase of the discussion, you, I believe, were secretary to the Indianapolis monetary conference.

Mr. WILLIS. Yes; I was.

Senator GLASS. You know perhaps better than I—certainly as well as I—the futility of the Aldrich Monetary Commission in bringing about legislation.

Mr. WILLIS. Yes.

Senator GLASS. I do not know of any legislation of a valuable nature that has been secured by or through the recommendations of commissions. It is my view that this Senate Banking and Currency Committee, given ample time for securing testimony and discussing both principles and details, could do the work better than a commission.

Mr. WILLIS. I have no doubt that is true, Senator, with the experience of the committee in legislation. But have you that time, and will the Senate allow any such thoughtful consideration to occur?

Senator GLASS. That I do not know. I am waiting to hear.

Mr. WILLIS. As for the various commissions, we have had, of course, within recent years, the well-known commission in Germany, and the McMillan Commission in England, and numerous others which have done rather remarkable work in reestimating the banking position of those countries. The commission I have been inclined to favor would certainly not be one of the Aldrich Commission type, that had practically an indefinite lease of life, with a great deal of money to spend. I suggest that you make the Commission unpaid, a situation that has a tendency to hasten the work of commissions tremendously, in my observation, and, in order to hasten it along still more, that you state to it plainly—perhaps by way of legislation—that it is expected to report and disband by the first of next January. Its work for the next 6 months, then, would be devoted to sizing up the situation and giving the verdict of a nonpartisan group of men.

Senator GLASS. Who would select a commission like that?

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Mr. Willis. That you would have to decide among yourselves, but I see no reason why this committee could not select such a commission perfectly satisfactorily, and have entire confidence in it. I believe that any group of reasonably outstanding men with reputations to preserve would come to about the same conclusions on this subject, if given a reasonable length of time to talk it over.

Now, I turn to the second phase of what I have to present this afternoon. I have now made it my first recommendation, that the method to be followed shall be the one I have spoken of. I recognize that it is not possible to follow idealistic methods, and that there may be reasons that I am not familiar with which necessitate the passage of some bill on this subject right away. If that is true, I would urgently recommend that title II should be eliminated, and that the final bill should consist merely of the data with reference to the insurance fund and the so-called "technical" amendments to the National Banking Act. You would then at least apply another patch to the existing situation, and one which should enable it to carry on perfectly well for another year or so. If you should do that, however, I strongly recommend that you eliminate from it the provision which requires State banks to enter the Federal Reserve System, whether directly or indirectly, so that they are left free to bring that about. The House bill, I think, has eliminated the 1937 provision on that point, and to that extent I support it.

Senator Townsend. Will you elaborate on that somewhat, Doctor Willis, in giving your reasons?

Mr. Willis. I may as well do that at this point, if you approve. I have never favored compulsory membership in the Federal Reserve System. I think that membership in the Federal Reserve System ought to be earned and not forced upon a bank, and I think it would be infinitely better if you had a small Federal Reserve System, consisting of no. 1 banks, so that membership in the Reserve System was a "feather in the cap" of the member, and, instead of working on the scriptural principle of going out and compelling them to come in, it should be left, first of all, to the voluntary decision of the banks whether to come in or not, and then, when they had qualified and wished to come in, it should not be a matter of course that they should enter. This bill works upon the opposite attitude with respect to that. It not only includes the guarantee of deposits provision to which I have taken exception, but it also authorizes, in another section of the measure, the Reserve Board to relax all restraints, both those of the capital stock and every other—to waive those in order to get State banks to come in. The result of that, then, is that you will have two kinds of banks in there, one of which, to use the cant expression of the day, is "underprivileged", while the other one is subject to the more strict requirements of our national legislation.

Senator Glass. If you would apply that freedom of action to the State banks, would you not be willing to apply it to national banks as well?

Mr. Willis. I should, sir; yes, sir.

Senator Glass. So that they may withdraw from the System if they desire to do so?

Mr. Willis. Quite so. I have seen some of the workings of the Federal Reserve System, and I am convinced that the effect of this

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compulsory membership has been to allow meticulous Federal Reserve officers to lean back in their comfortable armchairs and to say to themselves, "Well, we should worry." The banks have to be members of the System, and no matter whether they like it or not, they have to pay their assessments and live up more or less to the requirements of the organization.

If the Federal Reserve administrators had been obliged to make the System useful, you would have a totally different attitude toward it now among the banks. The banks who protest against this Eccles bill do so for various reasons, but I do not believe that the love for the Federal Reserve System, in the abstract, is one of them. As a matter of fact, the Federal Reserve banks have not endeared themselves to the member banks, with very few exceptions, and particularly have they not endeared themselves to the small member banks. This very committee, when it was preparing for the Banking Act of 1933, sent out questionnaires to Reserve banks asking them specific questions as to what they had done for their member banks, and as to whether the variations which they made in the discount rate ever resulted in cuts to the public. The answer was no. The Bank of France, with its hundreds of branches, transfers the benefits of a cut in discount rates directly to its customers.

Senator GLASS. That is what I have been contending over this table here ever since we have been having these hearings.

Mr. WILLIS. I know you have, sir. The Bank of England transfers the benefit of the cuts in the discount rate through the money market. I notice that one of your witnesses here said that there is only one kind of central bank in the world, and that was a banker's bank. There are, of course, at least three kinds of central banks in the world: The bankers' bank type, which we have here in the Reserve System; the public-service type, such as the Bank of France; and the money-market type, which you have in the Bank of England, where the benefits of what is done are rapidly transferred to the public through a competitive discount market.

In this country we have not any of those, and the changes in the discount rate do not influence the rates that are made by the banks to their own customers, nor do the Reserve banks concern themselves particularly about serving their customers. It was only after a long time, and against the wishes of the Reserve banks, that we succeeded in getting the idea of par collection over, and we never succeeded in getting it over fully put over, but only to a limited degree under certain conditions. It has been difficult, or impossible, to get the Reserve banks to perform the part of city correspondents for such country banks as wanted to have them do it; and, as you well know, they have never gone into the foreign branch business. If they had we would never have had the trouble with foreign loans, and the like, that we have had.

In those circumstances, I submit that the teaching of experience is that the membership in this system should be voluntary, that it should be left to the banks to maintain a system for their own protection and for their own better organization, subject to constant public supervision.

If it be true that that is not sufficiently helpful, and that there still is a great deal that needs to be done, then let the Government continue its direct intervention in banking. I can quite conceive of a situation

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in which you may have a set of Bourbon bankers, who never learned anything and never forgot anything, which would result in having the State or the community find it necessary to do that. I hope we will never get to that point, and I do not believe we shall. One way of avoiding it is to make membership in the Reserve System a "blue ribbon" matter, and, as a result of that, to make Reserve bankers active, public spirited, and desirous of doing their utmost for the banks which deposit with them or which own their stock.

In addition to that, in reply to the gentleman who just asked me about the membership, I do not believe that it is a right thing to force State banks to come into this system, either through direct legislation, if you can do it—if that be constitutional—or through holding out competitive inducements to them to come in. I think that the incorporation of banks is a power that belongs to the States of this country, and that their banks ought not to be interfered with, but left to operate as the States in which they are situated think best that they should operate.

Such organization as is arranged over and above that, I think, should be a matter of voluntary acceptation on the part of the State member banks. However, if that doctrine be too old-fashioned you still have the question whether it is a wise thing to compel large banks practically to pay the expenses of insuring the deposits of the small ones by the device that is used in this bill. It seems to me that is what the Supreme Court apparently dislikes—that is to say, the taking of the property of the larger banks without any due process of law, by compelling them substantially to carry the load of bank failures, which as we know, is far greater among the small banks than it is among the large ones—at least, ordinarily so.

Those are my reasons, gentlemen, for feeling that that provision should be eliminated here, and that if you are going to act upon this matter, you should act upon it purely in the way of perfecting the financial responsibility and the smooth operation of the Deposit Insurance Corporation. The Corporation needs it, for I do not think that it can go through a severe panic or crisis and meet the immense obligations that have been imposed upon it.

Some time ago I had the honor of a visit from a representative of the Deposit Insurance Corporation, who asked me to devote some attention to that question and reach some conclusion about it. He supplied me with the figures that were necessary, and I devoted quite a good deal of time to it and that is my conclusion. I do not think the Deposit Insurance Corporation is in a position to do very much insurance if it should be asked to take care of a very high mortality among the members.

If you are going to enact the bill on this narrow basis, then, of course, there is a provision in the latter part, title III, that I regard as of equal rank with this insurance proposition. That is the eligibility of real-estate loans which is provided for here. I strongly urge the committee not to include that.

Senator BULKLEY. What is the section number of that?

Senator GLASS. That is in title II.

Senator BULKLEY. That is in title II.

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Mr. WILLIS. But there is a further provision in title III in that connection.

Senator BULKLEY. What section are you referring to?

Mr. WILLIS. I am speaking of titles I and III.

Senator BULKLEY. In connection with the real estate?

Senator TOWNSEND. That is in title II, is it not?

Mr. WILLIS. I had the impression that a large portion of it was in title III. I will not stop to go into that. I will discuss it at this point, if I may.

The inclusion of the real-estate loans is undesirable, not because real estate is bad or because there is anything wrong about financing a real-estate boom under proper conditions, or anything of that kind, but it is undesirable for two reasons.

The first is that it will disturb your existing real estate loan mechanisms. The savings and loan associations of New York are already exceedingly worried about this proposal, that is, to put the banks into the real estate business. The banks have not the mechanism for appraising and studying and finding out about the validity of real estate. The original Reserve Act did a very unwise thing in opening the way for real-estate loans by country banks, but that was very pardonable. The country banks were already in the business. It merely sanctioned an existing situation, and one which, perhaps, was not severely to be criticized. The country banker usually knows all about the real-estate values of the farms in his vicinity. That is not true of the city banks, and the making of city real-estate loans is a complex operation which calls for a high degree of skill and for the organization of an elaborate department in the bank. Our banks have not got that. Some of them probably will develop it—the larger and more careful ones. Others will not. The result is that you inevitably have a lot of doubtful and bad loans, to say nothing of the disturbance and interference to which you will subject the existing loan agencies, particularly the savings and loan associations in the cities. So it seems to me that, at least, should be eliminated, if there be anything about it in title III, as I was under the impression there was, before any enactment takes place.

While there are a great many other provisions that seem to me to be undesirable in titles I and III, I do not think I ought to take the time of the committee to speak about them, but I wish to speak now in some detail of title II, which seems to me to be the real central part of the whole measure.

In the first place, title II, of course, fundamentally changes the general underlying organization of the Reserve System, as well as the theory upon which it is based. There have been a great many statements of late to the effect that the object of title II is merely to carry out the ideas of the Federal Reserve Act which had been seriously marred by some persons unknown, so that they had not quite got full interpretation. So far as I understand the Federal Reserve Act, the ideas of the Eccles bill are diametrically opposed to it; and title II, if it should be enacted, far from carrying out the ideas of the Reserve Act, will carry them out only on a stretcher—in other words, would render them wholly ineffectual. Title II is simply a complete negation of everything in the theory of the Reserve Act.

The fundamental idea of title II is that the supply of money is regulated by banking, and that the total of it that is available there

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affects business directly. That is, if you have more money you have more and better business; if you have less, then you have what is called deflation.

The idea underlying the Federal Reserve Act is that money is the product of business, and that credit, which is a very different thing from money, is used to supplement the supply of money and to provide that elastic element that is necessary in order to permit a larger volume of business to be transacted without the necessity of importing gold; or, where you have a closed regime, as we have here now, without the necessity of enlarging the legal tender note issue.

Those two ideas are as wide apart as the poles; and, of course, when one starts with one of them to write a banking bill he gets to a very different result from that which he gets if he starts with the other.

I notice in the testimony of Governor Eccles here a statement that there is comparatively little difference of opinion on these essential points. I think there is a very wide difference of opinion about them—so wide that I do not believe that you can reconcile the underlying ideas there, although I do believe, as I said a few minutes ago, that it is possible to bring about some reconciliation of them in practice, so that if you have a careful body of men working on the thing it might be possible to get our fundamental day-to-day mechanism into a shape that would satisfy all sides if they were not determined to go to extremes.

That fundamental idea, or difference of idea, runs through the whole measure. As the outgrowth of it, you have the bill here authorizing the Reserve Board to change the reserve requirements at all times, whenever it gets ready. The bill is not exactly frank or sincere on that subject. I have read through the testimony here, and I find that the provision on that subject is constantly referred to as being a provision for changing the amount or percentage of the reserves. That expression is constantly used in the hearings. But when we turn to the actual language of the law, what we find is that it is the requirements as to reserves that may be altered by the Reserve Board. It is not the percentage of reserves. We have three requirements as to reserves at the present time. One is as to the place where the reserves shall be kept. In the original Reserve act they were kept partly in the Reserve banks and partly in the vaults of the banks. Then, in 1918, under the plea of necessity for inflation, we provided that only credit in the Reserve bank should be reserves.

Senator Glass. Counted as reserves.

Mr. Willis. Counted as reserves. At the present time we still stick to that.

The second requirement as to reserve is the percentage of reserve, which has been varied two or three times since the Reserve Act was adopted. Then third, and, perhaps, most important, is the question of what the reserves shall consist of. We had it at one time lawful money. Then we had it gold, and we had various things. As the reserve paragraph stands, the Reserve Board, as I read it, is given power to alter all of these reserve requirements, which means, of course, that it would be possible for the Reserve Board to direct a bank to hold its present balance in Reserve banks and hold the rest

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of it in Government bonds; and since it can change the amount of reserve to be held, I see no reason why you should not put into effect a 100-percent reserve at once, such reserve to consist partly of cash—reserve credit, rather—and partly of Government bonds, to be held in the vaults of the Reserve banks.

In fact, I heard a member of the House committee say in public that he hopes that a 100-percent reserve will be put into effect very soon—not soon enough, of course, to disturb business, but as soon as possible.

The provision here, then, as I say, is not a very sincere one, and is one which ought to be reviewed with exceedingly great care. If this is what you mean, then the act should specify that the reserve requirement may be changed.

Senator GLASS. The percentage.

Mr. WILLIS. May be changed as to percentages, as to composition, and as to place, so that you know exactly what you are going to do. If you mean only one of those things, then that should be specified in that same way, so that at least there will not be, after the act is passed, a great deal of debate and uncertainty and controversy about what that means, but so that you will have a perfectly outstanding, clear-cut situation. That is certainly not an unreasonable thing to ask.

Now, in addition to that, the bill as a whole, as I have said, is based upon an entirely new theory of banking. That theory is the one that has gained ground in Russia, to some extent in England, and in other places. But as it is presented here it seems to me quite inconsistent with itself. For example, the proposed act eliminates the present note issue plan in the Reserve System entirely, and substitutes a new one. The old system of note issue, as you know, provided for the collateraling of Reserve notes, so that the notes are not only a prior lien on the assets of the bank but they were a collateral prior lien, the Reserve agent holding the eligible paper or the bonds or the gold in his department. That was based upon the idea that outstanding new currency should come into existence when there was need for it, not because someone wanted to sell bonds or convert bonds into purchasing power, but because somebody really had some business to transact. And so this rather clumsy provision, as it seems to me, was made to secure that.

Senator GLASS. And the notes were to be retired automatically when that business transaction matured.

Mr. WILLIS. Quite so. I have never been a very great friend to that way of issuing notes. It is certainly an anomalous one. It is not found in any other country so far as I know, and I believe it would be a great deal better if you could have a straight bank-note issue so that, as this bill professedly would have it, you get a straight issue of Federal Reserve notes that come out just as the deposits are created and are direct liens on the bank. But unfortunately, as the thing stands now, as I understand it, all of our notes are legal-tender notes, so that apparently what this bill proposes to do is to allow a private corporation, owned by the banks and, of course, carefully supervised by the Government in the extreme way that is provided here, to issue legal-tender Federal Reserve notes. That is as I understand the bill. I do not see anything in it that alters the present status of the Reserve note in that respect.

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Senator BULKLEY. A Federal Reserve note is a Government obligation.

Mr. WILLIS. Yes; but it is legal tender.

Senator BULKLEY. It is issued through the banks but by the Government?

Mr. WILLIS. Yes. But here you make it, as I understand, a general claim on the assets of the Reserve bank. If you are prepared to revoke the legal tender quality of the Federal Reserve notes and make them plain bank notes so that, as Governor Eccles expresses it, they do not have the same status as the check-book deposit, I think there is no reason why you should not make this change. Twenty years ago, of course, Congress would not have heard of it.

Senator BULKLEY. Do you think there is any great significance in the character of what is behind the note?

Mr. WILLIS. That depends upon the status of the note. If it is a real bank note, I do not like it at all. The Bank of England, of course, in the old days required a deposit of government bonds or gold for every note that was issued. At the present time that is in abeyance. But generally speaking, the theory of banking calls for the making of the notes and obligations of the bank just the same as the deposit accounts, demand deposits, and of course without debt-paying power unless people are willing to take them.

Senator BULKLEY. Does not this place them in a preferred position?

Mr. WILLIS. I think they are given a prior lien.

Senator BULKLEY. Then what is the difference whether the specific collateral is deposited or not?

Mr. WILLIS. None of importance, as you describe it, but I think it makes a great difference whether a man can refuse to take a Federal Reserve note if he does not like it.

Senator BULKLEY. I am not sure about what point you are speaking of. I thought you were condemning it, because of not having collateral security behind it.

Mr. WILLIS. If you take away the collateral security and leave it to the Federal Reserve banks to issue the notes just the same as they create deposits so that the volume of currency depends entirely upon the will of the Federal Reserve bank, it is not proper that they should be legal tender.

Senator BANKHEAD. Is there any change in this bill that would prevent them from being legal tender?

Mr. WILLIS. No; not that I know of.

Senator BULKLEY. You want to hitch it up to a specific amount of gold and reserve; is that right?

Mr. WILLIS. If we are going to have a Federal Reserve note in approximately a form of money that is identical or nearly identical with a Government legal tender note, it seems to me that the collateral idea is the proper one.

Senator BULKLEY. In order to limit the supply of notes?

Mr. WILLIS. And in order to prevent an individual man from having to take it.

Senator BULKLEY. There are two different things there. If it is legal tender, he does have to take it?

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Mr. Willis. Yes. But my thought is that if it is a bank note it should not be legal tender. The question is whether it is a bank note or not.

Another fundamental conception in this bill relates to the question of open market, and as to that I want to speak very frankly. When the Federal Reserve Act was adopted I was exceedingly anxious that it should include an open-market provision, and I hoped that the open-market provision would be used for the purposes for which it was used under central banking systems, namely, that of making the discount rate effective, so that if a discount rate of 3 percent were made by a Reserve bank, if a Reserve bank were to fix its discount rate at 3 percent and the other banks would not let that get to the community, that then the Federal Reserve bank should be able to go out into the open market and buy or sell the paper of a business concern, the ordinary business concern, assuming it was prime paper. Now that, of course, is what the Bank of England habitually has done for many long years. Our bankers were not willing to do that. We strained every nerve to have the open-market provision omitted, and they wanted it omitted because they were afraid that the Reserve banks would come into direct competition with them and cut the rate of interest. Of course that was not necessarily the case.

I was talking this matter over with the governor of the Commonwealth Bank of Australia, an institution that was started at just such an agitation as we are having now, and it was headed by a very capable banker and he took pains to use this open-market power merely for the sake of seeing to it that the other banks followed the leadership of the central bank. During the early years of the Board we were never able to get them to use that power; the resistance of banks was so strong and the hostility of some members of the Board was so powerful to the application of it that it never got into effective use at all. It was not until after the war was over that New York bankers began to see what a wonderful opening it gave for siphoning funds out of the Reserve bank, and we began then to have the development of the revolving acceptance and the acceptance based on commodities in stores, and so on, and when the breakdown came we had an enormous volume of acceptances outstanding. I think there were a billion seven hundred million, and we were constantly boasting of how we had beaten England on the acceptance business.

Those acceptances were collateral. They were merely another way of making commodity loans. They had nothing to do with the open market. They were called open market, but they were not.

When the Government began to get into difficulty with its deficits the open market was a very easy way of dumping bonds on the market and of getting them carried along in the way it is being done at the present time. If you are in the hole and Government bonds threaten to go down, you order some open-market operations. You do not say there is anything wrong with the bonds. You say it is for the public welfare, and you desire to order a couple of hundred millions of open-market operations per month. Your central bank buys a lot of Government bonds in the open market and takes them right off the market.

It would be well, since Congress is planning to legislate on this subject, if it would end the open-market hypocrisy completely. I

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notice in the statements of some of the witnesses that the open-market idea was a brand new idea that was gaining ground all over the world. The open-market idea is a very old one. It has been used by every central bank when and if it was necessary; and it had worn itself out in some countries so that the Bank of France, for example, prohibits it entirely, and one of the finance ministers over there has referred to it recently as an Anglo-Saxon device, which I think is a very good description of it as it had been employed in this country.

If you are going to have open-market operations of the kind that you have now, then they ought to be most carefully safeguarded, free from hypocrisy, and allowed to stand for just what they are worth.

As to who should conduct them—well, that depends entirely on the kind of men that you have got carrying them on. In this bill you practically hand over to the Governor of the Reserve Board, who is a direct appointee of the President, the power of open-market operations. It is too great a power for him to have.

Senator TOWNSEND. Would you care to illustrate your thought there of hypocrisy?

Mr. WILLIS. You mean, what it is?

Senator TOWNSEND. Yes.

Mr. WILLIS. What I have just spoken of, treating open-market operations as a kind of esoteric operation done for the good of the general situation.

Senator BULKLEY. Your contention is that it is only done to support the market for Government bonds?

Mr. WILLIS. At the present time I do not think anybody would deny that.

Senator BULKLEY. That is what you meant?

Mr. WILLIS. Yes, sir.

Senator GLASS. And that is the only kind of operation that they have engaged in?

Mr. WILLIS. Just now; yes. Bankers' acceptances at one time formed a proportion of the operations; but that was only when the acceptances would not go, and for the same reason they had to be taken off the market.

Senator BULKLEY. Part of those bonds were bought not so much for the purpose of supporting the Government-bond market as for the purpose of increasing excess reserves of banks, were they not?

Mr. WILLIS. For the purpose of increasing excess reserves?

Senator BULKLEY. Was there not a theory that we could promote prosperity by forcing the banks to lend——

Mr. WILLIS. There may have been such a theory. There have been many theories; but certainly if that was held by anybody it must be pretty well abandoned now, because we have $2,250,000,000 of excess reserves today and less actual lending than we ever had before.

Senator BULKLEY. I never believed much in that, in the first place, but it certainly was asserted.

Mr. WILLIS. I am afraid it was, and a good many other things have been.

Senator BANKHEAD. Does the volume of excess reserves cause you any concern?

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Mr. WILLIS. There are other things that have given me more concern. You can get rid of them in 5 minutes if you want to.

Senator TOWNSEND. How?

Mr. WILLIS. By just having the Reserve banks sell the two and a half billions of Government bonds.

Senator GLASS. What would happen then?

Mr. WILLIS. It would break the Government-bond market.

Senator GLASS. It would not only break the Government-bond market but would break every other security market.

Mr. WILLIS. Then you do not want to get rid of them? Is that it?

Senator GLASS. I did not want them to get them in the first place.

Mr. WILLIS. As it stands now, you would rather keep them?

Senator GLASS. We have got to keep them.

Senator COUZENS. If we have a stabilization fund existing, I do not see why we need to be disturbed about the bond market.

You were speaking about the catastrophe that would happen to the banks if they unloaded Government bonds, but I do not see any catastrophe with the stabilization fund.

Senator GLASS. You mean, the stabilization fund that the Government stole from the Federal Reserve banks?

Senator COUZENS. I am not talking about how we got it. If they unloaded these bonds, the stabilization fund could buy them and there would not be any disturbance.

Senator GLASS. You know the stabilization fund is not going to buy them.

Senator COUZENS. It would if they started to unload bonds on the part of the banks.

Senator TOWNSEND. What is going to happen if we put this additional four billions of currency out?

Mr. WILLIS. If you will allow me to answer—I do not think I said it would cause a catastrophe. I merely indicated what I thought would happen.

Senator COUZENS. I do not think it would happen. We have not got more than two and a half billions out of the whole issue that is out.

Senator GLASS. In the Federal Reserve banks?

Senator COUZENS. Yes. So there is still opportunity for the four billion we have got without anybody getting " het " up about it, as I see it.

Mr. WILLIS. I started on this matter, not with the intention of bringing out any controversial question but with the purpose of discussing the general theory of open-market operations; and the point I came to is this, that the open-market operations that we are now carrying on, if such they may be called, are not open-market operations in the central banking sense at all; that they are not being generally used throughout the world except where they are unavoidable; that they are prohibited in France as the result of experience; and that the Millan committee, which investigated this whole thing very closely, said they might be used in England slightly more than they were, but it would have to be done with a great deal of caution.

Senator GLASS. Is that the committee that set up a bank in Canada?

Mr. WILLIS. No; it was established by Mr. Ramsay McDonald soon after he took office, the committee of which Mr. Kane was a member.

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I have covered what I consider the essential differences of opinion about this bill, with one exception. That is the question of eligibility, and I have a few words on that if you will allow me.

The original Federal Reserve Act provided for very narrow restrictions on so-called "eligible paper", with the design of limiting the amount of currency we got out. The theory was that if business increased it would create credit paper to be used as a basis for note issues. That strict interpretation is blamed for most of the ills that exist at the present time; but of course, the trouble with that is that it never was applied. Two weeks after the Reserve System was organized we had a letter from the Federal Reserve bank in Richmond saying that that bank's officers had always been in the habit of taking collateral, and it was a much safer way to do, and they wanted to loan on collateral. The Board allowed them to follow their practice by exacting collateral, provided that the paper which was thus collateraled was technically eligible. Various other Reserve banks have, of course, been able to act under the same general ruling and have done so.

So it has often happened that a Reserve bank would have almost all of the assets of a bank that was just on the point of failure, placed with it as collateral; and you would then have the depositors, and especially the savings depositors, holding the bag. They would simply be an empty shell, while the Reserve bank or branch would have the entire assets of that bank.

Senator COUZENS. When they made those exceptions, did they make any exceptions as to maturities?

Mr. WILLIS. They took the notes, and then they renewed them over and over again in the classical banking way.

Senator COUZENS. So that a maturity of 15 days, 30 days, or 90 days did not mean anything?

Mr. WILLIS. No.

Senator COUZENS. That is another fiction?

Mr. WILLIS. It was a fiction of mere practice, Senator, if you will allow me.

Senator COUZENS. The public have not generally understood that that fiction continued.

Mr. WILLIS. The public knows very little about what has happened in the Reserve System.

Senator COUZENS. I am afraid that is true.

Mr. WILLIS. That is the situation. I am speaking as a realist in the proposition, having seen it developed from inside; so that those who say that this country has been dreadfully handicapped and hobbled by the fact that the Reserve banks would not loan on anything except eligible paper are merely reckoning without their host at all.

In New York, of course, under the 15-day clause, the Bank of New York has merely loaned to the stock market right along for years by permitting the member banks to borrow on their own notes collateraled by Government bonds. The Banking Act of 1933 makes provision for stopping that; and if enforced, I believe it will correct that.

Senator COUZENS. Why do you say "if enforced"?

Mr. WILLIS. The question in my mind is whether you can enforce it. Under this bill I know you cannot, because it practically repeats that and lets in any kind of paper as an asset.

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Senator COUZENS. I never saw any law ever passed that we could get the New York Bank people to obey.

Mr. WILLIS. Because they did not want to obey, perhaps.

Senator COUZENS. I am afraid that that is true also.

Mr. WILLIS. Then we are agreed on that.

This is a question that ought to be seriously faced by Congress, this question of what the Reserve System is for; that is, whether it is for the purpose of financing any sound assets or whether it is really a system whose purpose it is to finance business and commerce.

The stock exchange, as you well know, just before the panic in 1929, had its plans all laid. I say that because the then president of the stock exchange admitted it in a public speech. They had their plans all laid for the direct admission of stock-exchange paper as eligible to the Reserve banks. The then chairman of the House committee, Mr. McFadden, told me that the pressure was so strong to get that passed that he doubted whether it should be resisted.

This bill provides on page 52 that—

> any Federal Reserve bank may discount any commercial, agricultural, or industrial paper and may make advances to any such member bank on its promissory notes secured by any sound assets of such member bank.

That opens up the whole world of assets, provided only that the Board has declared that they are abstractly sound; that the class of assets is sound—Anaconda Copper, or Allied Chemical. If that is a sound asset and you put out a ruling to that effect, there is no reason why you cannot lend on any kind of paper, mining stocks or anything else, unless some administrative authority should step in to prevent it.

Senator BANKHEAD. Is not the whole question whether or not the assets are sound?

Mr. WILLIS. It depends on what you mean by "sound."

Senator BANKHEAD. Good, liquid.

Mr. WILLIS. I do not think loans ought to be made on assets because they are ultimately collectible. I believe the correct theory of central banking is conversion into immediate means of payment of assets which represent the production of new wealth on its way to consumption. In other words, it should be equivalent to the aggregate of new production of consumers' goods which are on the way to their users.

Senator BANKHEAD. Why that limitation?

Mr. WILLIS. Because the rest of the wealth that we produce is the so-called "frozen" assets, an asset that may be perfectly good 5 or 10 years hence, but not convertible at the present time into a means of payment.

Senator COUZENS. How could you tell whether the assets would be sound 20 years hence?

Mr. WILLIS. I do not think you can, because too many things can occur in that time. You can approximately tell 90 days hence or 6 months, even.

Senator COUZENS. When you use the words "sound assets" I think that is about as broad an expression as "interstate commerce."

Mr. WILLIS. It is a euphemism, I would say.

Senator GLASS. As a matter of fact, as I have called attention to repeatedly, Mr. Whitney and other stock-exchange men testified before the Banking and Currency Committee of the Senate that the

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soundest asset in the world was a broker's loan, and yet we textually excluded brokers' loans from the Federal Reserve System. We textually excluded them and the bankers actually took them.

Senator COUZENS. Going back to the statement you made previously, about the Government extending its activities into the loaning business and taking business away from the banks, in that statement you made no discernment between investment banking and commercial banking?

Mr. WILLIS. No.

Senator COUZENS. It seems to me that most of the activities of the Government are in investment banking instead of commercial banking.

Mr. WILLIS. To a large extent they are; but you also have the production credit corporations, of which, I believe, there are now some 600.

Senator BANKHEAD. Six hundred what?

Mr. WILLIS. Production credit corporations.

Senator BANKHEAD. They do their financing through 12 regional banks, do they not?

Mr. WILLIS. From groups——

Senator BANKHEAD. They borrow collectively from the production credit bank.

Mr. WILLIS. Do they not recommend loans?

Senator BANKHEAD. They borrow. They do not lend. They get their money directly from the bank.

Mr. WILLIS. It seems to me that if I sign a man's note I am loaning to him.

Senator BANKHEAD. They are borrowing collectively, several signing a note and getting the money.

Mr. WILLIS. They are liable.

Senator BANKHEAD. Yes; but they are not engaged in making loans.

Mr. WILLIS. The effect is to have that amount of business in merchandise?

Senator BANKHEAD. Oh, yes. Banks in agricultural sections cannot do that sort of business because they do not have the money. They were not sufficiently liquid to do it.

Senator COUZENS. Do you think there is justification for a combination of investment and commercial banking?

Mr. WILLIS. I think we have got it now, and we had better make the best of it for a time. Abstractly, I do not like it. The California system, I think, is the best protection against it, perhaps, that we have devised, where we have a savings-bank section, an entirely separate entity within the bank, and no transactions between that and the commercial bank.

Gentlemen, I have finished with the basic differences that divide the Eccles bill from the Federal Reserve System. It seems to me as if they were at opposite poles of credit theory and sound practice from that which was set up in the Reserve System. The fact that the Reserve System has been in the hands of the Philistines a great deal of the time and has not lived up to its early promise is regretted. But it has nothing to do with the validity of the principles under which it was organized.

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Senator COUZENS. Do you believe that it is desirable to have some centralized control rather than to have the control diversified or decentralized in Reserve banks?

Mr. WILLIS. I think if the System planned in the Reserve Act is carried out in good faith and effectively it would be a sufficient centralization. If you have good reason for not thinking so—and I can see arguments on that side—then I think we had better frankly have a central bank confessedly operating under that name and title and subject to all of the controls that would surround it.

Senator BULKLEY. How would you make the transition from our present system to that?

Mr. WILLIS. You have already made it pretty well. I should think you could disestablish the Reserve banks and simultaneously start a central bank of the Government.

Senator BULKLEY. Owned by the Government?

Mr. WILLIS. If you want to. I should hate to see that done.

Senator TOWNSEND. Then you do not agree with the Secretary of the Treasury that the Government ought to own the stock of the Federal Reserve banks?

Mr. WILLIS. And pay for it?

Senator TOWNSEND. He did not say that.

Mr. WILLIS. If you interpolate the assumption that he means to pay for it, I think it might be a good thing, because he runs them now. Why not let him pay his bill and take them over?

Senator GLASS. You do not seriously think that, do you?

Mr. WILLIS. I think the way we are going now——

Senator GLASS. I am not talking about the way we are going now, but about the way we ought to go.

Senator COUZENS. This committee has had testimony to the effect that diversity of opinion and interference with the Federal Reserve Board by banks and public officials have tended to diversify authority to such an extent that it has been injurious to the country.

Mr. WILLIS. Yes.

Senator COUZENS. And you would correct that?

Mr. WILLIS. By establishing a Federal Reserve Board which in fact, as well as in theory, is independent and is entirely free from political control.

Senator BULKLEY. How would you do that?

Mr. WILLIS. Simply select a group of the best men you can find, with long terms, and leave them to work out their own salvation.

Senator COUZENS. But if you did not give them the authority, how could they work it out?

Mr. WILLIS. They should have the authority.

Senator COUZENS. That is what I was trying to find out, whether you did not think we should have centralized authority somewhere.

Mr. WILLIS. My view would be that the authority given to the Federal Reserve System in the original act is authority to permit complete centralization for all necessary purposes.

Senator COUZENS. It has not done that, because one of the big outstanding banks of the 12 Reserve banks refused to cooperate, and there was no centralized authority to compel it.

Mr. WILLIS. I would simply say that you did not have men on the Reserve Board who had the courage to oppose that bank.

Senator GLASS. Or to carry out the law and remove that man, as it has authority to do under existing law.

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Mr. WILLIS. There is no human mechanism that will ever take the place of upstanding courage, as you very well know, and you have exemplified it in your own career.

Senator COUZENS. I want to go back to that same old question again. The Federal Reserve Board, no matter how strong it has been, has never had the power to compel the New York bank to do anything, has it?

Mr. WILLIS. It has had that power; and the chairman of the committee, when he was Secretary of the Treasury, did just that.

Senator COUZENS. It has been testied here that any one of the banks could refuse to comply with an open-market operation directed by the Federal Reserve Board.

Mr. WILLIS. They will not refuse to comply.

Senator GLASS. The Secretary of the Treasury told me distinctly, and repeated it again, that they had had 100-percent cooperation with the Federal Reserve banks in open-market transactions.

Senator COUZENS. I am going back to testimony that was had in executive session, not during the period of the existing Secretary of the Treasury, in 1927, I think it was, when the banks refused to cooperate. That is one of the difficulties of getting impressions and convictions in executive session that you are charged with being in error about. But I am not in error about that.

Mr. WILLIS. In 1927 the Board had fallen upon very difficult times, with a personnel that was anything but what one would wish it might be. If you have a board of that kind it will never have the courage that is necessary in financial transactions—and more courage is needed there than in almost any other branch of the public service, because you have got direct responsibility coming right home to roost.

Senator COUZENS. That goes back to the very point that unless the Federal Reserve Board has absolute control you will never be able to have assurances that all of the 12 banks will come into line on any one thing.

Senator BYRNES. If the appointments to the Board are made in the manner you suggest, they would be made by the President, would they not?

Mr. WILLIS. Well, they might be, yes. In one of the original drafts of the Reserve Act we did provide for a selection by the Reserve banks themselves of certain members, so we had theoretically a self-governing bank mechanism. Of course there were always Government representatives on the Board.

Senator BYRNES. But assuming that they are appointed by the President and are lacking in courage or experience, as you have indicated, would it be wise then to appoint them for a long term?

Mr. WILLIS. No; I do not think so—not unless you had a much higher sense of the duties involved in making the appointments.

Senator BYRNES. But the manner of appointment would be by the President of the United States, just as it has been in the past?

Mr. WILLIS. We are assuming it would be; yes. When Senator Bulkley asked me about that and how we would get such a board, I answered that it could be done by appointing courageous men with long terms.

Senator BYRNES. I gathered from your statement, however, that they had been lacking in courage and, in critical times, had failed.

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If so, and they were appointed by the President, I am wondering what your suggestion would be to overcome that, whether you would overcome it by appointing for a long term men who are lacking in courage, whether we would be any better off.

Mr. WILLIS. If you would exercise, as you used to do in the beginning of the system, the power of refusing confirmation, I think you would attain that result. But it has been quite a long time since you gentlemen here have been willing to do that.

Senator BYRNES. The things to which you have referred have not been recent. The Senate confirmed their appointments just as now?

Mr. WILLIS. But they were confirmed under conditions that were certainly adverse to the getting of good men. I have noticed here in the testimony that some member of the committee, whose name I do not recall, asked for specific cases in which political pressure had been applied to the Federal Reserve Board, and I think the witness said it never had been applied. As to that I would just like to call attention to the well-known statement made by the late President Coolidge in his radio address on the night before he was reelected as President, in which he said—I look it up the other day, but unfortunately I have not got it here with me now—that this administration had always favored low-discount rates and it always would do so. That was, of course, in the nature of a mild suggestion to the then Reserve Board that higher discount rates would not be very satisfactory. Of course, that is merely an illustration.

Until you get a public opinion that is adverse to things of that kind, I do not think you will ever free the Reserve Board completely from the sort of influence that is bad for it. Of course, the President of the United States would never call in, I suppose, a member of the Supreme Court and tell him that he liked N. R. A. very well and he hoped he would get a favorable decision. I do not believe he would do that. But under existing conditions of course, Presidents have done just about that with reference to financial matters. That is the reason you have not had the independence and courage in the Reserve Board that is absolutely essential. That is one reason why I do not like to see a great increase in the power of the Reserve Board over policies, but in actual execution, the actual carrying out of policies that it decides upon. This evil is not a matter of Republican or Democratic politics; it is a fault of all parties.

Senator GLASS. Oh, yes. I have seen some notable exhibitions of courage by members of the Federal Reserve Board who were Republicans, and by members who were Democrats, also. But I agree that they have as a board exhibited a lamentable degree of timidity at times where courage was required.

Mr. WILLIS. I have just one more matter to present that I think I ought to mention and that is the effort to use this banking system as an agency of economic planning. The statement is found on page 50 of the bill, subsection (o) of section 204 [reading]:

> It shall be the duty of the Federal Reserve Board to exercise such powers as it possesses in such manner as to promote conditions conducive to business stability and to mitigate by its influence unstabilizing fluctuations in the general level of production, trade, prices, and employment, so far as may be possible within the scope of monetary action and credit administration.

Of course that last sentence is a very "saving clause"—so far as it is possible. But one might add to that that it is never within the

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scope of monetary action and credit administration, so that you would use a bank mechanism for doing something for which it was never intended. The function of the bank mechanism is that of keeping banking sound and safe and of keeping it at all times in position to perform its financial functions. It is not its duty to unstabilize or to stabilize production, trade, prices, and employment.

And we have at the present time a very serious difference of opinion among qualified authorities as to just how much it can do in any of those directions. It is ordered here, as if that were an unmistakable, unquestioned monetary power to do something which in my opinion it cannot do. And of course as to bringing the Reserve Board into areas about which it knows nothing and as to which no banking board is in position to act, you almost insure failure.

This question has been discussed a great deal in England. The director of the Bank of England has issued a very interesting book entitled "Planned Money", in which he discusses the question of just how far you can go in what the Board here is ordered to do. He is very reasonable about it. He frankly admits that while he thinks certain things can be done with success, any such program as this is out of the question. At any rate, we have not reached a point where it can be done. It is true, as I said before, that that saving clause was introduced, "so far as possible"; but you surely do not want the Federal Reserve Board experimenting. We had better wait until the condition of theory and scientific thought has reached a very much more advanced point than it has today.

That provision embodies really the essential difference in point of view between the Reserve Act and the proposed act, and in my opinion it puts forward a hazardous program for a Reserve Board to conduct, one that is fated to disappointment, certainly, and perhaps disaster.

Those, gentlemen, are the major reasons why I think that this bill, if you are going to pass it at this session—at least title II of it—needs very, very careful consideration to see which of these theories is acceptable and to harmonize the different parts of the bill so that they dovetail with one another and so that the bill is consistent with those as far as possible.

In addition to that, this measure is a very clumsily written, inexpert piece of work; and if you are going to pass it, you need to have it completely recast.

In my statement I have mentioned a few of the principal points that I think are in that class. I have been talking too long a time and I ought not to keep on much longer, but I will just call attention to a very few of them if I may.

The mechanism for the appointment of the Governor. Supposing that you are wholly in sympathy with it as it stands here and are going to keep it. I think it should be recast in such a way as to make plain exactly what you do mean by it.

At the top of page 45 of H. R. 7617 is a confused sentence which leaves in doubt when he is to be appointed and reappointed and how he is to take office.

Senator GLASS. I would suggest, Doctor, that if you discuss that in your prepared statement you could just put it into the record and we will read it.

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Mr. WILLIS. My statement covers a few of the points, but I had to make the statement bear upon the House form of the bill. Since arriving here I have added various others, but I will discontinue——

Senator GLASS. I think if you cover those details in your statement it would be more effective to put that into the record than to talk about them here. We cannot carry it all in mind; at least I cannot.

Mr. WILLIS. Very well. I have nothing else to present.

(The prepared statement referred to and submitted by the witness is here printed in full as follows:)

STATEMENT OF H. PARKER WILLIS BEFORE SENATE COMMITTEE ON BANKING AND CURRENCY MAY 29, 1935

THE PENDING BANKING BILL (S. 1715)

Mr. Chairman and members of this committee, in the following statement I have endeavored merely to set down in outline my views about the bill as to which you have asked me to testify. There are many details and many statistical analyses which should be made with reference to its operation in particular aspects, but I assume that you do not care to have me go into such minutiae, and that you merely want a general statement of my position.

I present this under two heads:

1. A survey of the banking situation, designed with a view to showing that no action whatever should be taken upon it at the present time (particularly upon title II of the bill), and

2. A survey of the measure itself designed to offer certain general criticism, founded upon the assumption that the bill is nevertheless to be acted upon presently and is, therefore, a fit subject for specific commentary.

I now turn to the matters of which I have spoken:

I

First is the question whether any such measure should be enacted at the present time. As to this I submit the following statement, the substance of which I have already published in the Commercial and Financial Chronicle of New York:

THE MEANING OF THE "ECCLES BILL"

A student of the Eccles bill must not allow his attention to be diverted by the multitude of suggestions and proposals which it contains. First of all, and before all else, it is essential to try to understand the ultimate purposes that are held in view by the measure. These are presented in three or four very definite and distinct aspects by its authors and sponsors. It is presented:

1. As a completion and logical application of the ideas embodied in the Federal Reserve Act but never fully worked out in practice.

2. As a rectification or corrective of faults and defects in the actual working of the Reserve System, which have been noted as the result of experience and which call for modification or alteration if our present banking system is to be successful in its functioning.

3. As a great advance above anything that has been attempted heretofore in the "supply and control of money", by permitting the Federal Reserve Board to vary the amount of "money" in the country in such a way as to permit "planning", or a "planned economy."

4. As a means of guarding against the arrival of panic conditions or excessive "inflation", such as may easily result, it is asserted, from the present surplus of credit now found on the books of our banks and Federal Reserve banks.

5. As a way of developing needed centralization in the control of banking, in order to prevent conflict of method and purpose and to bring about unification and consistency in the development of banking policies.

Before attempting the analysis of any of these ideas, it is worth observing that the great powers that are conferred by the Eccles bill upon the Federal Reserve Board would also, incidentally, provide for the accomplishment of the following objects:

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1. The further and, if necessary, the exclusive use of the resources of the banks for the purchase of Government bonds and obligations in the endeavor to provide funds needed in carrying out the existing program of the administration for money spending;

2. The more or less complete crushing of any independence in banking—the combination of all banks, whether chartered under Federal or State law into one centrally controlled system.

3. The withholding of credit from various types of business or enterprises and the feeding of other businesses and enterprises with a smaller amount of credit which they would otherwise probably not be able to obtain.

4. Particularly, the upbuilding of the mortgage market and the development of real-estate financing by devoting the resources of our commercial banks to that end.

5. The reestablishment of the joint operation of investment and commercial deposit banking which had prevailed before 1929 and which was partially corrected by the Banking Act of 1933.

That there are many other incidental provisions and objects which are made or served in this inclusive measure is, of course, obvious. The foregoing brief survey merely assists in focusing attention upon those that seem most outstanding.

THE ATTITUDE OF THE PUBLIC

It would naturally be expected that so great a measure as this would and should receive the careful attention of the public, with a view to its improvement, or to the reaching of a decision whether it should be adopted or not. Some study of it has undoubtedly been given by the public. This study has resulted in two major suggestions:

1. That of a special committee of the American Bankers' Association which is apparently disposed to accept the bill very largely as it stands in its essentials, but which asks for some important modifications—the chief being a division of power in regard to central banking functions which will leave to the bankers of the country a distinctly larger share than that which is allotted by the provisions of the new bill.

2. That of the special committee of the New York Chamber of Commerce, subsequently ratified by the New York Chamber of Commerce itself for the appointment of a commission to look over the entire situation and see what is needed in connection with banking.

3. That of some outstanding figures in the financial and banking world who have thought best to express themselves with a degree of frankness, either in personal interviews, testimony before committees, or in circulars or other utterances issued by their respective banks.

The reader who surveys these definite pronouncements must necessarily come to the conclusion that only in a very few instances has any positive position been assumed in regard to the proposed bill, whether for or against it. The American Bankers' Association report, for example, tacitly assumes that the general idea of the bill is to be accepted, but merely indicates changes that are thought to be necessary in connection with the administrative working of the measure. The various utterances of outstanding bankers and financial authorities have been concerned with much the same sort of questions as was the committee of the American Bankers Association. For the most part, effort has been made to select provisions that were clumsily written, partisan in nature, inclined to favor this, that, or the other scheme, or to render impossible, this, that, or the other operation, which was thought by the authors of the bill to be desirable. In hardly any of them has there been a careful review of the underlying philosophy of the whole measure. A publicist recently writing on money and banking makes the following statement in behalf of the proposed bill:

"The fundamentalists of the pre-war Federal Reserve System * * * did not believe that the volume of money can or ought to be deliberately controlled. * * * They thought that the supply of money should contract or expand automatically in accordance with the needs of industry and the imports and exports of gold. They are opposed * * * to the whole philosophy of the system in the post-war era. * * * Those who hold this view are in a very small minority."

This cavalier dismissal of the issues involved in the subject referred to would not deserve any notice if it did not represent notions that are being taken for granted by a good many hasty observers. There is, of course, nothing

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about the real question of "money", its "supply" or its "control", in the Eccles bill, nor is there the slightest warrant for identifying bank deposits with money. To do so is like the statement said to have been found in the introductory paragraphs of an Alice in Wonderland algebra that "in this book we shall regard the signs plus and minus as identical." Bank credit is not money and never can be made such, and what is really under discussion in this whole matter is whether there is any such thing as credit and any such function, desirable or otherwise, of testing the soundness and truthfulness of credit. What the Eccles bill seeks to do is to bring about a complete transformation of the underlying ideas of banking (whether pre-war or other) and to revise the entire banking system accordingly. Unfortunately, this undescriminating attitude is pretty generally accepted by the public itself, including some bankers who have been disposed to regard the controversy about the Eccles bill as little more than a debate as to whether the "money of the country" should be under the "control" of the bankers or of the politicians. This issue, if it can be called such, is, however, an exceedingly small phase of the real questions raised by the Eccles bill. The proposals made in the Eccles bill go far beyond the mere question of controlling money or credit and they raise the issue whether there is any such thing as credit at all and whether it is, or is not, identical with money.

In contrast with this attitude of limited understanding of and partial acquiescence in the Eccles measure, we have the proposals included in (2) above, which merely ask for a study of the entire proposal. The argument in favor of this latter proposal is as follows:

(1) There is no emergency today recognized that would warrant a hasty enactment of any banking measure whatever. The Comptroller of the Currency has emphatically stated that in his opinion, the banking crisis is over and the community well on the way back toward a normal condition. In his last annual report, he said, "There is little evidence remaining of the collapse in March 1933 of the banking struction of the Nation. The entire system has been rebuilt." Practically the same statement has been made by the Secretary of the Treasury, and either directly or by implication in the public utterances of the President. Judged by its own expressions, the administration recognizes that there is no call for any emergency action.

(2) There are enough observers who have expressed the greatest anxiety about the effects of the Eccles bill to make it evident that the measure should not be regarded as a mere routine proposal to be passed as a matter of Executive recommendation and without study.

(3) If for no other purpose then than for that of reconciling conflicting views and obtaining the maximum amount of support for a far-reaching proposal, we undoubtedly ought to have a nonpartisan investigation of the ideas contained in the Eccles bill;

(4) Moreover, as is generally conceded, the Eccles bill, even taking it at its face value, just as it stands, by no means covers the field of desired banking legislation. There is a well-nigh universal recognition among students of American banking that a fairly complete "codification" of American banking law is needed, and with a commission of the kind referred to, if composed of men of standing and probity, they would be able to lay down the lines along which such work ought to proceed and to assure a satisfactory result of the investigation when completed.

This is the case, then, as between hasty enactment of the Eccles measure and the proposal to entrust it to a nonpartisan commission. As to the contention that such commissions in the past have oftentimes been noncommittal, inclined to waste money and disposed to delay action, the answer is perfectly plain. All this depends on the kind of commission that is selected. It might well be a commission serving without pay, and ordered to turn in its report within a very short period of time. In any case, there is no reason whatever to suppose that unconscionable delay and unreasonable expense need necessarily be involved in the effort to get thorough and scientific advice about a matter of utmost importance. The public has not studied the subject, is in no position to do so, and is only conscious of the fact that a great technical problem is before it. What is most urgent is to afford leadership and to grant time for the careful and discriminating presentation of argument under conditions that will permit of arrival of some safe set of conclusions. To drive such a measure through Congress with "whip and spur" at the present time would be unpardonable, since there is no possible basis upon which to defend, much less to justify, it.

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"ECCLES BILL" AND THE FEDERAL RESERVE ACT

It is now desirable to devote some attention to the various arguments that have been presented for the immediate enactment of the Eccles bill, despite the general considerations that have just been presented. Among these, one of the most frequently cited is that which has been noted as coming from the advocates of the measure itself—that it completes the ideas of the Federal Reserve Act and carries the views of its framers to a satisfactory, logical conclusion. As to this, an immediate answer may be returned on the basis of general historical knowledge. This is, that there is no respect whatever in which the content of the Eccles bill can be regarded as in any sense completing the Federal Reserve Act or carrying it to its natural and logical conclusion. The obvious attempt of the Eccles bill is to overset most of the notions of the Federal Reserve Act and to make it imposible for that act to function in the way that was intended by its original framers.

The Federal Reserve Act, for example, had as a definite underlying conception, the notion that the desirable outgrowth of a central banking system was an "elastic currency" and that the attainment of such a currency should be a major object in the development of banking. The Eccles bill, on the other hand, holds that the volume of business is a reflection of the volume of media of exchange while it erroneously contends that "deposits" are "money" and should be "controlled" in their amount with reference to what is considered the ideal volume of business. The two measures are thus radically opposed to one another, without the slightest integral connection. The Federal Reserve Act, moreover, in its original drafts, sought to place the management of banking in the hands of bankers, simply giving to the Government the opportunity to be present at all deliberations, know what was going on, and express opinions or have an adequate voice in determining conclusions. "Politics" forced a compromise between friends and opponents of political control at a very early date, with the result that the Federal Reserve Board became a distinctly political body, while the choice of its successive members became a matter to be determined by purely political considerations—a decidedly diametric contravention of the original purpose of the Reserve measure. The Eccles bill places the control of Reserve credit entirely in the hands of the Federal Reserve Board, makes that Board merely a group of marionettes, dominated by a governor who is merely the political puppet of the President who may be in office at a given moment, and takes away all possibility of self-government from banks and bankers.

This review of the essential features of the proposed Eccles bill is sufficient to show abundant reason for thinking that there not only is no furtherance or completion of Federal Reserve ideas in the Eccles bill but that, on the contrary, the adoption of the Eccles bill would be a radical defeat of the major underlying motives or principles upon which Reserve legislation was founded. The effort to make capital out of regard for the Reserve System and its record is thus wholly unwarranted, without the most remote basis in fact.

IS THE ECCLES BILL A NEW PHILOSOPHY OF MONEY?

In contradistinction to those impressions which represent the Eccles bill as merely a further working out of Federal Reserve ideas, we have the opposed suggestions that it is a very original proposal whose adoption would take the Federal Reserve System out of the rut into which it has fallen and give it a new and proper application. Let us see upon what this contention is based. Apparently the idea of the Eccles bill is to centralize the discount and open-market powers in the hands of the Federal Reserve Board, or of institutions or organizations closely connected with it. Thus, the various forms of the bill already available, contemplate the placement of the open-market powers in the hands of a committee consisting of some members of the Board and certain governors of the Reserve banks, with the Governor of the Reserve Board as the chief factor in the organization. This open-market group is to decide upon the policy to be pursued in buying and selling Government bonds or acceptances—the staples of open-market operations. The Eccles bill, furthermore, seems to give to the Reserve Board the power of initiating rates of rediscount, instead of waiting for them to be proposed by the several district banks, later to be approved or disapproved by the Board itself and by this latter means to be harmonized. Finally, the Eccles bill authorizes the Federal Reserve Board to determine the amount and composition of reserves that would be ex-

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acted from member banks, by compelling the banks—and, for that matter, the Reserve banks as well—to carry larger or smaller reserves or to change their constituents so as to regulate the supply of credit available. The latter proposal has been endorsed by Mr. Eccles himself as being a weapon which the Board could use to very great advantage in cutting off or reducing the danger of uncontrolled "inflation" or expansion which, it is alleged, exists in very serious form at the present moment.

Here we have a proposal not to introduce anything new but to use familiar methods and factors in a way to bring about an unaccustomed result through the application of a familiar technique. Suppose that the Federal Reserve Board, under the new bill, should determine that it was desirable to raise reserves to 100 percent of outstanding demand deposits. Certainly there is much reason to suppose that such a step might be ordered. Representative Goldsborough, one of the chief proponents of the measure in the House of Representatives has expressly said that, while he would not wish to see such a change ordered, by a step that would cause any disorganization or disturbance to our banking system, he would look forward to an ultimate introduction of the notion under the provisions of the Eccles measure. Advisers of the Reserve Board have strongly advocated the application of the 100-percent reserve requirement, both in public and in private. Governor Eccles himself, it is understood, has disclaimed any present intention of calling it into effect, but much of his testimony and general philosophy points strongly to such a measure as the inevitable outcome of what he says he wants to do under the terms of the measure. If banks were to be ordered thus to increase their reserves against demand deposits to 100 percent of the face of such deposits, they would evidently have to displace other assets such as corporation bonds, in order to draw in claims upon banks from the buyers of such bonds, and these buyers would have to provide themselves as they could; perhaps by further discounting with banks, eventually giving rise to new credits with the Reserve banks, or in some similar fashion. The banks themselves, were they to try to comply with the requirement would, of course, find that they could do so only by rediscounting with Reserve banks, and in order to get the material for such rediscounting would have to buy Government bonds since commercial paper is not available in any such quantity.

An easier way to apply the meaning of the proposed provisions then, would be to require that 100 percent be held in reserve credit plus Government bonds, in which case the banks would have to buy the additional Government bonds as they were issued, giving credit on their own books and then immediately discounting notes collateraled by the new bonds with the Reserve System, or they would have to (as before) get the funds with which to pay for them by disposing of their corporate bond holdings and using the funds to build up their reserves, or would have to obtain the Government bonds by what amounts to an exchange of corporate issues for Governments, so that eventually they would become the holders of the amount of Government bonds needed to equal—with their reserve credits and cash—the amount of their demand deposits. In these ways, unquestionably, several "birds could be killed with one stone"—the Government bonds could be sold in new and huge amounts as a practical necessity on the part of the banks to acquire them; while the theoretic desire to rebuild the reserves of the banks to this "100-percent money" would be attained. On the other hand, such a policy would satisfy the demands of the numerous persons who have asked that Government bonds shall be made convertible directly into paper currency. This policy, said to have been seriously considered in connection with the new bill, might, of course, be subject to more or less modification; the point is, that it has been thought of and is being considered by authoritative persons and represents what must be regarded as unquestionably the gravest of dangers—the development of a situation in which the assets of the banks consist practically wholly of Government bonds, while the banks themselves become merely agencies for the making of loans stated in terms of Government paper. That such a policy would infinitely transcend in danger the issue of more "greenbacks" needs no argument and yet it seems to be a measure which either by actual design or as the result of policies inevitably resulting from what has already been attempted, would necessarily come into use.

We have here the crux of the situation which is raised by the Eccles bill. Is that bill, either directly or indirectly, the means of still further devoting the assets of the banks to the purchase of Government bonds, thereby enlarging the potential field for bond issues and thereby enabling the Government to go on with

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deficit financing for a considerably longer time without perhaps bringing about an immediate crash in our financial structure? The general philosophy underlying such measures would be the same as that which Mr. Eccles outlined in his testimony before the Senate commission investigating economic affairs in the spring of 1933. It cannot be possible that his opinions and views about banking have been very greatly changed in the 2 years that have elapsed since that time. Especially when we know his advocacy of the proposed measure and the easy way in which its terms allow themselves to produce some such outcome. The underlying notion—that the Government and its credit should constitute the foundation of the credit of the Nation and that advances made by the Government for whatever purpose should constitute the basis of the currency rather than to use for that purpose resources or wealth originating through private investment or business enterprise, the latter being necessarily reduced in importance as the scope of Government lending enterprises grow—is the inevitable outcome of what is now urged. Probably there are very few in the community who have seriously contemplated the practical application of any such theories as these, partly because they are so foreign to those which have underlain the education of bankers heretofore, and partly because of the disastrous consequences that must ensue from them to the business of a country that is not completely governmentalized or communized. We must, in short, conclude on this one ground alone that the basic thoughts of the Eccles bill not only are not a completion or further working out of Federal Reserve conceptions, and not only far from being merely a wider application of governmental supervision of banking in order to secure greater honesty and sincerity, but are also something very much broader: The embodiment of the idea of public credit as a substitute for private credit.

It was Lenin who, in discussing the subject of banking, made it clear that in his opinion the first approach to a communized state must be found in complete national control of the monetary and banking system; and in this, he followed other authorities of equal standing among Communists. The Eccles bill, as now termed, does not confessedly purport to aim at any such ideas; and it would be impossible to find a specific recognition of them in any section of the measure. They are present, however, by implication in the ways that have just been indicated; and even though they may not be extensively put into effect upon the adoption of the bill, would always remain as an imminent possibility in connection with its application.

PANICS AND DEPRESSIONS

By an amendment to the Eccles bill which was proposed in the House of Representatives, provision was made for instructing the Federal Reserve Board to use its credit powers as a means of bringing about a balanced or "planned" economy in the Nation at large. The thought underlying this amendment was that since the granting or withholding of credit greatly facilitates, if it is not absolutely necessary to, the investment of capital in the development of an industrial enterprise, the granting of power to withhold such credit must make it possible for the credit-granting authority to deprive undesirable enterprises of funds, while at the same time encouraging those that are thought to be desirable to proceed with their plans. Governor Eccles himself, in commenting upon the interpretation of the House proposal, has expressly stated that the Eccles bill does not give to the Federal Reserve Board any power over credit that it does not already possess and has asserted that the new measure would not in any way whatever enable the Board to deprive a given enterprise of the credit which would otherwise be granted to it.

Probably a case can be made out for the technical accuracy of these assertions. It remains true, however, that the proposal must have had some meaning and that if it had any meaning it was intended to indicate that the centralized-credit power of the community was to be used in checking or advancing the general activity of business so far as any such policy could check or advance that activity. Indeed, much of the testimony of Mr. Eccles himself is based upon the thought that it is possible in this way to further or advance business. In his speech at Columbus, Ohio, shortly after the Eccles bill was first made public, the Governor of the Federal Reserve Board asserted that he did not suppose it would be possible, by the use of reserve credit, completely to smooth out the business cycle, but he thought that considerable progress might be made in that direction.

How would such a result be attained? Obviously by making it harder or more expensive for business to expand under such a policy, when thought

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necessary, or by rendering it easier for the business to expand when that policy was desired. It may be remarked parenthetically that this is a power which, in the older thinking on banking, was regarded as a fundamental function of banking and which when judiciously exercised tended to prevent the over-expansion of industry leading it to so-called "boom" followed by "panic" conditions. It also has underlain the whole philosophy of "easy money" often advocated by the Federal Reserve Board as may be proven by any number of citations from their reports of recent years. What is proposed, then, is evidently to centralize in the hands of the Board, bank powers in relation to business which have heretofore been resident in the individual banks, or in those banks with the aid and oversight of the Federal Reserve banks. There is probably nothing in the Eccles bill which would authorize the Board to prevent the First National Bank of any given place to continue making loans to, let us say, the automobile industry, or that would compel it to cease making such loans; but there is ample provision in the Eccles bill which would make it possible for the Board to cut off such a bank from rediscount facilities or to render rediscount facilities more available to it.

The germ of such authority, undoubtedly, exists in the present Federal act, but subject to a system of checks and balances which control it, just as the checks and balances of our Constitution prevent the exercise of despotic power by an Executive.

The Eccles bill eliminates many of these checks and balances and thus renders what under proper conditions of use is a beneficial authority, a potential instrument of despotic financial power. It is also a fact that such a power can be wisely used only locally and that it cannot ordinarily be used to good purpose as a general policy to be applied over a large competitive area. It is seldom true that in any given line of business, all concerns are overexpanding or the reverse, and the direction of industry by means of general loan regulations is correspondingly difficult. Desirable as it may be to employ banking as a means to bring about conservatism in business enterprise such means certainly cannot be relied upon less those who use them are more fully informed and far more trustworthy in their use of such powers than those to whom the authority has, in fact, been committed. The Eccles bill, therefore, would largely take away the powers spoken of from those who have heretofore been entrusted to use them and would vest them in political or governmental authorities whose knowledge of their use—as the Reserve Board has heretofore been constituted—must be very seriously questioned. We cannot, therefore, give any credence whatever to the hope expressed by Mr. Eccles and others, that the proposed measure would result in a saner, more conservative, more restrained use of credit for the purpose of preventing the development of "inflationary" or overexpanded industrial conditions, and we must fear that mistakes of judgment in the application of such centralized credit would tend to aggravate danger which might otherwise be self-corrective.

Before leaving this subject it should be carefully noted that by no means all economists are inclined to the opinion that any use of bank credit, however wisely made, can exert any such effect upon the development of business or the arrival of "booms" or in curing of depressions, as is thus alleged. A very large school of thought holds that bank credit is the outcome or reflection of business conditions and by no means the motivating cause of changes therein. If the views of this latter school hold good, the use of powers such as those advocated by Mr. Eccles, would be likely to eventuate merely in the "pegging" of enterprises that had become greatly expanded, as in the case of the Reconstruction Finance Corporation. The result in such a case would be nothing more than to divert the resources or credit of the community into the support of unproductive undertakings, or undertakings that are uneconomically operated, with the corresponding loss and disadvantage of the business community.

THE QUESTION OF NEEDED CENTRALIZATION

A very strong point has been made in connection with the Eccles bill of the fact that under existing conditions it is unsafe or unwise to leave a large local latitude in the use of financial assets to banks which might, or might not, employ it wisely. Unwise use of such power has been pointed out as being a major and exciting cause of bank failures, the latter to be viewed as the result of hasty or ill-judged credit manipulation, resulting in stimulating or depressing industry or in "tying up" individual bank offices, by giving to

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the Federal Reserve Board and its affiliate enterprises of deposit guaranty, and so forth, the authority to simplify control and improve bank examinations, while rendering them less onerous and less expensive. Here is a proposal which naturally appeals to many bankers who have found the present agencies of supervision incompetent, self-contradictory, and costly; but would centralized control bring about the desired result? There is no definite reason to suppose so. Experience in the past has shown that bank examination is essentially a matter which must be carried on locally by men familiar with local paper and with local conditions. The condition of banks cannot be judged by rigid standards. Many a bank is in a sound enough condition for its own locality and for the community which it serves, but would be anything but satisfactory in another place a thousand miles away. Whatever faults there are in the present examination and oversight system, can be easily "ironed out" without any application of broad powers that have nothing to do with the problem of supervision by a Federal body.

There are many bankers in the United States who from the very beginning of the Federal Reserve System have felt that the organization of that system upon a district footing was unwise. Many influential bankers opposed the Federal Reserve Act on that account, and said that it would never be possible under any circumstances successfully to build up efficient discount markets on a local basis. They, therefore, antagonized the underlying thoughts of the original Federal Reserve Act. While perhaps a majority of such former advocates have changed their attitude, and since then have become advocates of the district system; by no means have all done so. It seems fairly clear that the proposal made in the Eccles bill to diminish the importance or authority of the several Reserve banks in order to add to that of the Federal Reserve Board has met with some approval. Just here it should be noted that this attitude on the part of some bankers is entirely based upon the thought that the centralization desired was to take place under banking supervision and self-government. Were they convinced that the centralized system now proposed would never be developed or operated upon a basis that was more truly financial than the present, it may well be doubted whether they would advocate the change.

Probably a good many have felt that the proposed system would gradually develop into a plan whereby the great powers vested by it in a political organization would be gradually taken over by some one of the Reserve banks, say by the Reserve bank of New York, just as the latter had during the pre-1929 period succeeded in taking to itself much more than its normal share of influence in the system. The question whether any such development could be counted upon is necessarily more or less conjectural, but there are abundant reasons for believing at the present time that the political organization at Washington will not be likely to part with the authority that it acquires unless compelled to do so by some general collapse. The hope therefore of reaching the development of a genuine bankers' central bank controlled by bankers and centralized through the membership of some institution situated, perhaps in New York, must be regarded as without adequate foundation. There is not enough basis for it to warrant those who believe in that form of transformation of our banking system to trust themselves to the indicated method of attaining it. Even if the proposed measure worked at its best, the kind of financial centralization thus hoped for would probably be rendered more distant, rather than less. If the proposed measure should lead to the disasters which many foreshadow for it, the cost of bringing about the desired consummation would be far too great to be thought of.

DO WE WANT A BANKING COMMISSION?

Enough has been said to indicate, entirely free from any partisanship for or against the Eccles bill, two things:

(1) There is a large field for difference of opinion about the actual effects of the Eccles bill and about the theories which underlie it. It undertakes to do many things that have heretofore been regarded as unsound, dangerous, and contemplated to disturb the entire basis of modern business.

(2) There is a feeling of distrust and doubt about the proposals that exist not only among the banking community, but also among businessmen, without regard to party, and which must necessarily make adoption of the measure unwise, especially in our present economic situation and necessitate its serving as a cause of disturbance in financial and economic relationships.

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Inasmuch as it is agreed on all hands that no emergency exists or, at all events, is admitted, which calls for the prompt adoption of such a measure, it would seem to be only the part of common wisdom to obtain the verdict of nonpartisan and capable men, viewed by the country as worthy of confidence, before any irrevocable step is taken. The plain dictate of common sense would be therefore the remedy which has been suggested by the New York Chamber of Commerce and by other agencies of equal weight, in the appointment of a satisfactory commission to look quickly over the entire field of banking legislation and to indicate what is needed. Such a commission need not spend much time in purely technical discussion; it could safely leave that to expert advice, to be rendered to committees of Congress or to be obtained in some other way. But there is the most cogent reason, before taking radical and extreme steps, such as are proposed in the Eccles bill, to ask for a careful weighing of the general considerations that underlie the institution of banking, with a view to focusing upon the proposals the sanest opinion in the community, if for no other purpose than that of obtaining popular assent to or support for whatever may be adopted.

Every modern country has followed this plan before making any far-reaching change in its banking system. It is the method which was employed by Great Britain in the appointment of the Macmillan Committee; in Germany by the institution of the Reichsbank Enquete, and elsewhere by appropriate bodies vested with the necessary powers. We shall act recklessly and unwarrantably if we fail to follow the example of human experience.

II

Second—I now turn to a discussion of the proposed bill as a practical matter, upon the assumption which I have already indicated—that the measure is in fact to be acted upon at this session:

The salient features of the bill are grouped under the head of "title 2, amendments to the Federal Reserve Act", and consist in a series of changes in those parts of existing law which lay down the fundamental bases of our central banking organization. These are: (1) The self-governing character of the System; (2) the maintenance of liquidity and redeemability on the part of Federal Reserve banks and through their agency; (3) the conservation of soundness and liquidity of member banks.

CHANGES IN RESERVE SYSTEM CONTROL

The new bill effects a far-reaching change in Reserve System control through two methods:

(1) Alteration of the composition of the directorates of Reserve banks;

(2) Alteration of the composition of the Federal Reserve Board and of its relation to the banks. At present each Reserve bank has 9 directors, of whom 3 (known as "class C") are nominated by the Government, 1 to be known as "chairman and Federal Reserve agent." The local board of 9 members in each Reserve bank selects its own executive officers who are headed by a governor and 1 or more deputy governors, and these men are and always have been the actual operating officers of the institution. This arrangement was the outgrowth of a compromise at the time the Reserve Act was established. Original drafts of the Reserve Act had called for the selection of local boards consisting of business men and bankers resident in the district, but at the insistence of Mr. W. J. Bryan the Government was given one-third of the directors with the chairmanship, although it never contributed a single cent to the capital of the Reserve banks.

In the same way the original Federal Reserve Board was intended to be a self-governing body, chosen particularly by the Reserve banks themselves, although with a representation of Government officials. It became an all-Government appointive board, with matters so arranged that the Secretary of the Treasury was practically in control of it.

The System has continued even under these conditions to grow more and more political as the years have passed, and there has never been a time when the Treasury Department could not, and at any time when it choose to do so did not, exercise a directive power in the management of the Reserve banks, so far at least as it was necessary to float, manipulate, and market its own securities. Under the new act it is intended to have the governors of Reserve banks replace the chairmen, thus combining the making of policy with the actual

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execution of it and placing the operation of the banks under the immediate influence of the Reserve Board at Washington.

The Reserve Board itself had always been weak and was intentionally so selected. It has grown weaker as the years have passed, and if the present changes in Reserve structure were to involve the retention of the old type of Board with its former powers, the result might not be of much importance. The proposed act, however, would have the Reserve Board practically originate the appointments of the governors, while the Board itself is to be "packed." Every obvious provision is made in the new act for inducing or compelling the older members of the Reserve Board to retire, while an inconspicuous provision, obscure in language, enables the President to appoint any governor he may please, regardless of the latter's residence or location, he being expressly exempted from the geographical restrictions which apply to other members of the Board. The President, moreover, is authorized not only to designate a governor but to terminate his designation whenever he pleases, and in one form of the bill immediately to drop him from the Board, since when he ceases to be a governor "he shall be deemed to have served the full term for which he was appointed." The structure of the new mechanism then, reduced to its lowest terms, is this:

(1) A President of the United States who appoints a Federal Reserve Board and designates a member of that Board as governor;

(2) The Board itself is given long terms of office and is geographically distributed, but the President may designate any member as Governor, removing him at will and thus change the balance of the Board completely if it should be closely divided.

(3) A Federal Reserve bank board (1 in each of the 12 districts) presided over by a board of directors, 3 of whom are Government appointees with a maximum term of 6 years, and 1 of them designated as governor, who may have an indefinite term, by the Federal Reserve Board (which means by the Governor of the Federal Reserve Board, which means by the President of the United States) and removable without notice.

(4) A reserve banking mechanism which is fully authorized to appoint clerks, pay rent, buy stationery, etc., but which in all other activities shall be controlled by the political authorities at Washington.

CHANGE IN CREDIT STRUCTURE AND POLICY

The original Federal Reserve act provided for a credit structure in which local policies were to be made by the local boards of directors and harmonized through the exercise of a nugatory or veto power of the Federal Reserve Board. It was expressly intended to give to the local Reserve banks full control over the credit conditions in their districts and to make them, so far as possible, democratic and locally responsible for what went on. From time to time, as years have passed, the Federal Reserve Board has assumed a power of domination and has been prone to dictate to the several boards of directors, as on the notable occasion when it forced a bank to reduce its rate; but the theory of the act has continued unchanged up to the act of January 30, 1934, when the Secretary of the Treasury was vested with power to use a stabilization fund of $2,000,000,000 in buying, and selling Government bonds, foreign exchange, and practically any kind of marketable paper that he saw fit. Under the proposed bill, a committee controlling open-market operations on the part of the Reserve banks is established to supersede the present committee, which represents all the Reserve banks and which determines open-market policies, subject to the oversight of the Board. The new committee would consist of the Governor of the Reserve Board, who is chairman of the committee, 2 members of the Reserve Board itself, and 2 governors of Reserve banks. Meetings of this committee are to be held when the Governor of the Reserve Board may call them and it is to have power to direct open-market operations of the several Reserve banks. Put in plain language, this means that an appointee of the President of the United States, selected as he may see fit and accompanied by certain satellites is to have control of the open-market operations of the System and to prescribe such operations on the part of every one of the Reserve banks.

Along with these changes in the credit structure effected through the modification of the open-market committee goes the opening of the rediscount privilege to any "sound assets of * * * a member bank", the Board itself being the sole judge of "soundness" and the ultimate authority as to operations of

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the Reserve bank. The meaning of this provision evidently is that the Governor of the Reserve Board, appointed by the President of the United States, shall have power to operate Reserve banks on a basis of rediscount which shall admit any assets, bonds, stocks, commercial paper, mortgages on real estate, that may be owned by a member bank, provided that the Board, constituted as heretofore indicated, has designated them as "sound."

In addition to these far-reaching changes of structure, it is specified that the Federal Reserve Board, "in order to prevent injurious credit expansion or contraction", may, when and as it pleases, change the Reserve requirements of the member banks throughout the country. The language of this provision is obscure, but apparently would imply that it may release member banks in a favored Federal Reserve district from all or any part of existing Reserve requirements, at the same time that it maintained and increased them in others.

DEBAUCHING THE CURRENCY

It would have been strange if the new central banking bill had stopped without seeing what it could do toward a further change in our currency system designed to provide "enough money." In order to bring about this desired situation, the new bill specifies that the existing system of placing special collateralled security, consisting of commercial paper or Government bonds, in the hands of the Reserve agent or chairman to be held by him for protection of the Government—the idea of collateralling the notes is to be completely abandoned. Instead of being notes which at first were based upon commercial paper and later upon commercial paper protected by Government bonds—and still later upon Government bonds themselves with a 35-percent gold reserve—our Federal Reserve notes are now to have no special protection whatever, but are to be a general liability of the Federal Reserve bank issuing them, while the reserve of the Reserve bank held against them consists of irredeemable gold certificates, and the assets of the Reserve bank may consist of paper rediscounted by the institution on the basis of "any sound assets" owned by any bank in the country. There is thus no reason why we should not have an issue of legal tender reserve notes limited only by the volume of assets owned by the banks and safeguarded by a reserve which may be controlled in amount at the will of the President of the United States and the Federal Reserve Board; and which, in any case, has behind it only irredeemable gold certificates representing gold stored in the Treasury and paid for at any price the Secretary of the Treasury may choose to name.

FREEZING OUR BANK PORTFOLIOS

The new bill also provides for a more effectual freezing of our bank portfolios than we have yet been able to accomplish. It authorizes national banks to invest their entire capital and surplus if they chose to do so, in real-estate mortgages, which mortgages are not to exceed 60 percent of the actual value of the real estate offered for security, although under easily attainable conditions they may be raised to 75 percent of the value of the real estate. The banks' own premises are not to be included in the limit thus placed upon the real-estate mortgages and, accordingly, it would seem that the provision is definitely made for the possible issue of an aggregate of loans based on real estate and equal to the capitalization of the member banks. This figure, as given in the current Federal Reserve bulletin is approximately $5,000,000,000. Take this provision in conjunction with the power given to the Reserve Board to exempt member banks from reserve requirements and to discount anything they may have in portfolio, and it is clear that something close to a dispensation of Providence would be necessary to prevent complete freezing of the remaining assets of the banks of the country should there be any enterprises that desire to make further loans for working capital.

TECHNIQUE OF NEW BILL

The analysis of the new measure up to this point has touched only upon the high spots in it, and has, for want of space, necessarily limited itself to a view of the more fundamental provisions of the measure in question. We ought not, however, to confine ourselves simply to a technical analysis of specifically dangerous elements in such legislation.

The tone of the proposal and its interpretation in the light of actual experience is far more important than the actual provision. It is an old saying that,

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even the worst of laws, through good administration, can be made tolerable and workable.

The Federal Reserve Act as originally drafted had many flaws. Some of them were due to inexperience in central banking; others to political compromises which were made necessary in order to secure the adoption of the measure at all. The passage of time has resulted in aggravating these errors and the multitudinous amendments that have been made to the Federal Reserve Act in the score and a half of modifying laws that have been passed by Congress, has defaced the original measure in essential particulars, and has greatly lessened the safeguards against maladministration which were originally set up.

It is fair, however, to add that the 20 years which have passed since the adoption of the Federal Reserve Act have not resulted in a material change in the admitted purport and underlying thought of the legislation. Even those who have found its restrictions irksome and likely to prevent the attainment of their desires and even the ignorant and ill-advised administrators whose lack of knowledge of central banking has made them restive under the restraint, which in other countries would have gone as a matter of course as a result of long-established custom and well-recognized caution, have always made their onslaughts upon the System under the guise of an effort to improve it and to make its provisions more adaptable to the actual needs of the community.

The new bill, however, taken in conjunction with the act of January 30, 1934, must be regarded as a complete repudiation of the entire conception, not only of the Federal Reserve Act, but of central banking as it is practiced today in central banking countries. It substitutes politics for knowledge, guarantees for salability of assets, and irredeemable gold certificates for coin.

III

Apart from this general review of some of the major features of S. 1715, there are a few that need particular attention. In this statement, however, I will confine myself entirely in such further comments to title II which has to do with the proposed changes in the Federal Reserve Act: Title II covers pages 38–51. As to these pages I beg to note the following points:

(*a*) On page 38, line 25, it is provided that the Governor of the Federal Reserve Board shall end his term as a member of the Board when he ceases to be Governor. This would permit an Executive to change the entire composition of the Board by naming successive members Governor and then dropping them one after the other. If the proposed structure of the Federal Reserve Board be retained (as it should now be) some safeguarding language should be introduced to prevent an Executive from thus changing the composition of the Board in such a way as to get rid of persons whom he disliked. The present proposal is, of course, wholly out of harmony with the provisions contained in the bill for pensioning members of the Board at the end of the long term of service. The changes introduced in H. R. 7617 do not satisfactorily cover this point.

(*b*) On page 39, lines 9 ff., the offices of governor and chairman of the board of directors of each Federal Reserve bank are combined. The new officer to be known as "governor" is to be appointed periodically, by the board of directors, subject to the approval of the Federal Reserve Board. This is a highly unsatisfactory arrangement; the annual term of appointment is too brief, while the later provision on page 40, prohibiting directors from serving more than two consecutive terms, tends to make the managements of each bank transitory and ineffectual.

(*c*) On page 41, lines 16 and 17, the Federal Reserve Board is given power to waive the requirements relating to the amount of capital required of banks entering the System. This introduces an element of favoritism and, if many small State banks should enter the System, may weaken greatly the capital structure of the organization. This provision should be stricken out. The provision is itself misleading because there is no provision regulating the use of Government capital in recapitalizing a bank which has an insufficient amount of capital. The entire section needs to be rewritten in the light of the present ownership of large blocs of capital stock by the Reconstruction Finance Corporation.

(*d*) On page 41, line 23, membership in the Federal Reserve Board is to be confined to persons "well qualified by education or experience, or both, to participate in the formulation of national economic or monetary policies."

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This is too vague a requirement to be of any value whatever. It practically is notice to disregard the precedent heretofore observed, and at one time incorporated into the act, calling for actual knowledge of banking on the part at least, of some members as a prerequisite to holding a place on the Board.

(*e*) On page 42, line 7 ff. These are merely surplusage, unless the holding of office on the Board is in some way safeguarded against an Executive who might adopt the methods already indicated in (*a*) above for changing the membership of the Board. They should be stricken out unless change is made in the form of the provision.

(*f*) Page 43, line 9 ff. The same comment should be applied to this provision as to the preceding provisions on the same topic.

(*g*) Page 43, line 22 ff. The provision that the Board may assign to designated members certain duties, functions, service, etc., but that such assignment shall not include the determination of any national or System policy, seems to be out of harmony with the provision at the top of page 42, where the only qualification of a member of the Board is that he shall be able to formulate such policies. The meaning of this provision is far from clear, and if the authors of the bill had in mind any definite internal organization which is intended to authorize, the meaning should be made very much clearer.

(*h*) Page 44, lines 11 ff. The provision for an open-market committee included under these lines should be completely reset. The paragraph itself is exceedingly clumsy and self-contradictory, even if it be desired to retain the general structure of the committee which is there suggested. For example, the terms of members of the committee are to expire at the end of each calendar year, but there is no specification of when successors shall be chosen. On page 45 the committee is directed to aid in the execution of such other duties as the Board may prescribe, a provision which apparently would enable the Board practically to substitute a committee for itself in important particulars, while, strangely enough (p. 45, 1. 12), details of open-market operations are subject to regulations prescribed by the Board. This section needs complete rewriting in order to get an intelligent picture of the structure of the organization it is intended to create.

(*i*) Page 45, lines 18 ff. Any Federal Reserve bank may discount "any" commercial, agricultural, or industrial paper, subject only to such regulations as to "maturities" and other matters as the Board may prescribe. Apparently here the Reserve bank is given sole power of determining what commercial, agricultural, and industrial paper is. The bank (p. 46, 1. 2) may then make advances on promissory notes secured by "any sound assets." There is here no canon or determination of soundness nor any indication as to who shall fix the condition under which the advances are to be made.

(*j*) Page 46, lines 5 ff. Any kind of Government bonds may be bought or sold without regard to maturity. This apparently means that they may be bought or sold by Federal Reserve banks without regard to maturity. Apparently here the Reserve bank is authorized to engage in trading in Government bonds, and without any restriction or control additional to that which may be inferred with regard to any of its other operations. This paragraph should be completely rewritten.

(*k*) On page 46, lines 13 ff., is found a complete change in the base of Federal Reserve notes. The old base of secured note issue is ended and the notes instead of being Government obligations are now made bank obligations. In spite of this fact they are given a legal-tender quality. That is to say, privately owned institutions are allowed to issue legal-tender paper, an anomalous condition.

(*l*) On page 48, lines 22 ff., the Federal Reserve Board is given power to "change the requirements as to reserves." Apparently this means the percentages of reserve, but in fact it includes both the place where reserves are to be kept, their amount, and their composition, as well as their percentage relationship to outstanding deposits. This provision entirely deprives the reserve requirement of any meaning. It would be far better to relieve the banks of any reserve requirement whatever.

(*m*) On page 49, lines 7 ff., national banks are here again authorized to increase the amount of their loans on real estate. This provision carries further a bad phase of the Federal Reserve Act which, unwisely, authorized real-estate loans. The provision ought to be entirely stricken out; but if it is to be retained it should be carefully writen in accordance with the best existing practices with regard to appraisal and the extension of accommodation, such as are employed by savings banks.

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STATEMENT OF ROBERT HARRISS, NEW YORK COTTON EXCHANGE, NEW YORK, N. Y.

Senator GLASS. Please state your name, residence, and occupation for the record.

Mr. HARRISS. Mr. Chairman and gentlemen of the committee, my name is Robert Harriss. My address is care of the New York Cotton Exchange, 60 Beaver Street, New York. My principal business is the cotton business. I am interested in the production of cotton and the merchandising, exporting, and financing of it. I am also a partner in Harriss & Vose, who do a general commodity brokerage business.

I am not a banking expert. However, formerly I was one of the principal stockholders in the North Texas National Bank of Dallas, Tex. This bank was one of the larger banks of the Southwest. I have also been a stockholder of some of the larger banks of New York, New England, and in the South.

Senator BYRNES. Do you occupy any position on the New York Cotton Exchange?

Mr. HARRISS. Yes, sir; I am governor of the New York Cotton Exchange, a member of the cotton exchange, and a member of the New York Commodity Exchange. I have prepared a very brief statement here. As I say, I am not a banking expert, but I have had considerable dealings with banks for a quarter of a century.

Senator TOWNSEND. Have you studied this bill?

Mr. HARRISS. I have studied the Nye-Sweeney bill. That is the one I was asked to give my opinion on, Senator Townsend.

Since the depression started in 1929, I have given considerable study to the banking and currency question and have conferred with many of the foremost economists and bankers of this country as well as Europe.

In the early part of 1930 Mr. George LaBlanc pointed out to me why there could be no sound recovery until we had banking and currency reform. Mr. LaBlanc was formerly senior vice president of the Equitable Trust Co., and president of the Equitable Eastern Banking Corporation, and president of the Interstate Trust Co., all New York banks. The Equitable Trust Co., at the time he was senior vice president, did the largest foreign-banking business bank, I believe, in our country, if not in the world.

Senator TOWNSEND. At what time was that?

Mr. HARRISS. I believe he went with the Equitable Trust Co. in about 1915 and retired from the Equitable in the Seaboard merger and accepted the presidency of the Interstate Trust Co. of New York.

Senator TOWNSEND. Do you know what date that was?

Mr. HARRISS. That was along about 1928 or 1929—shortly before the depression.

At that time Mr. LaBlanc pointed out to me that the depression or the deflation was due to the huge inflated war debts; that these debts had to be faced and adjusted before there could be sound recovery.

Since 1930 I have personally been associated with groups that were and are advocating banking and currency reform.

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Senator BANKHEAD. Do you belong to any monetary reform organization?

Mr. HARRISS. I am a member of the Committee for the Nation; I am vice president of the Sound Money League; I am a member of the National Monetary Conference; and also a member of the National Union for Social Justice.

In the early part of 1932 Senator Elmer Thomas came to New York. There we had lengthy conferences with the leading bankers and economists, as well as with Governor Harrison and Dr. Burgess, of the New York Federal Reserve Bank. Senator Thomas at that time urged that these people cooperate in a program of currency expansion in order to restore values and economic recovery. He prophetically pointed out that unless this were done we were headed into economic and banking disaster. However, his plea fell on deaf ears.

Also, in the early part of 1932 I appeared before the House Ways and Means Committee. I then urged the payment of the adjusted-compensation certificates in order to expand the currency, get off the ruinous gold basis, and bring about a revaluation of the gold dollar. Later in 1932 I attended the Democratic convention in Chicago and urged that the Democratic platform declare for a program of banking and currency reform.

I believe it is now apparent that the Federal Reserve System has outlived its usefulness; that in the interest of our country we should have—and we are going to have—banking changes or reforms.

I am substantially in agreement with the fundamentals of the Nye-Sweeney central banking bill. The present banking and currency system is too much under the control of those self-interested, or the bankers. In the welfare of our country it is not advisable that the control of banking and currency rest in bankers or private hands. This because the expansion or contraction of the currency and credit may often be influenced either directly or indirectly by prejudice or selfish reasons instead of in the interest of the Nation. At times, as at present, it may be influenced by fear. Today, although our banks are in a more liquid condition than they have been in years and there is much idle money and the interest rates are low, yet, as we know, it is almost impossible to obtain loans or credit with the banks unless the loans are made against Government bonds or against stocks or commodities that are immediately liquidable.

Yet one cannot blame the banks very much for not making loans. They are naturally afraid to loan the farmer because they know agriculture is not on a sound and profitable basis. They also have much reason to fear making loans to industry because, with few exceptions, industry is not on a sound and profitable basis. We cannot expect them to finance and make loans to the railroads when the best of our great trunk lines are not making money or else are running at a loss. We cannot expect them to finance and make loans to the contractors or builders of our country when there are tens of thousands of unoccupied homes and office buildings that will not sell for enough to pay the mortgages. I believe this deplorable situation was caused by an inflation of the debt structure, and that it will continue until we have what some may term radical changes in our banking and currency system.

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During the past 5 years we have tried many palliatives and experiments, some constitutional and some not, to try to end this financial and economic depression. The Government formed the Reconstruction Finance Corporation which some believe is a form of central bank. The formation of the Reconstruction Finance Corporation may possibly have been advisable as an emergency. However, I am opposed to the Reconstruction Finance Corporation in principle because in the final analysis it means that the Government itself is competing with private banking. In fact we might say that they are actually in the banking business. It is stated that the Reconstruction Finance Corporation owns 27 percent of the stock of our national banks.

In desperation and in order to try to restore economic and financial recovery we have resorted to the A. A. A.—curtailing agricultural production; the N. R. A.—curtailing industrial production, and making codes, regimentation, doles, and fabulous governmental borrowing and spending. My opinion is that these have not brought about recovery nor can they bring it about. In fact, I believe if continued they may end in disaster. I do not believe we can prosper by a policy of raising and producing less.

The Government debt is now approximately 30 billions of dollars. The average interest rate on same is approximately 3 percent. The interest on this debt compounded for the next 60 years will amount to more than 140 billions of dollars. This, then, with the principal, will exceed more than 170 billions of dollars. I am an owner of some of these bonds. Yet I do not think it is fair or honest for us to pass such a crushing debt of bondage and tax on to our children, nor do I believe it possible for our country to prosper and compete when the people have such a load of Government debt and taxes.

Additional Government borrowing can only mean more taxes; more taxes will only lead to worse business, and worse business will only lead to more unemployed; more unemployed will lead to more relief; more relief will lead to more Government bonds or borrowing, and thus the vicious circle will continue.

As mentioned, I favor the fundamentals of the Nye-Sweeney banking bill. I am opposed to any central bank that can be controlled or dominated by the politicians or by any administration. It is only natural that if a central bank can be dominated or controlled by the politicians or by any administration, Democratic or Republican, it may be run for party or selfish interests instead of for the welfare of our country. This, of course, would be just as serious a mistake as leaving the banking and currency under private control.

I believe the Nye-Sweeney banking bill would overcome both of these grave dangers—either private or political control; that it would leave the control of the central bank in the hands of the people so that it could function for the national welfare and in the interest of the people.

I do not believe that it is fair to brand as radicals, inflationists, or visionary, men those who favor a Government central bank. I believe the real or dangerous inflationists are those who have inflated or acquiesced in the further inflation of the Government debt.

As we know, many countries in Europe have central banks. As a matter of fact, the Bank of England is construed by many as a

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form of central bank. It might be mentioned that England, with only a small part of the gold and a fraction of the great resources of our country, has managed her banking and currency so well that conditions in the British Empire are prosperous as compared with the conditions existing in our country.

It could also be mentioned that the country bordering on our south—Mexico—has a central bank which has been functioning so well that there is little unemployment and no depression in Mexico—a country that has little compared to our great Nation.

Some will try to frighten us regarding a Government central bank by saying that it will lead to the issuance of "greenbacks." They will not tell you that Abraham Lincoln had no gold or silver against which to issue his greenbacks. They will not tell you that those greenbacks proved to be good money. They enabled Abraham Lincoln to save the Union. These greenbacks have also saved the taxpayers of our country more than 12 billions of dollars, calculated at 5 per cent compound interest. There are still in circulation today 346 millions of these greenbacks that are doing splendid work.

They will not tell you that today, under Treasury control, there is approximately $9,500,000,000 of gold and silver, and that there is outstanding only approximately $5,000,000,000 of actual currency or coin. In other words, there is existing under Treasury control more than $4,000,000,000 of absolutely sterile gold and silver. In fact, the situation is even worse because our people are being actually taxed to carry this sterile gold and silver. This seems unbelievable, but it is a fact.

I should like to bring to your good attention what Benjamin Franklin said in his autobiography in reference to the issuance of money [reading]:

> About this time there was a cry among the people for more paper money, only 15,000 pounds being extant in the Province, and that soon to be sunk. The wealthy inhabitants opposed any addition, being against all paper currency, from an apprehension that it would depreciate as it had done in New England, to the prejudice of all creditors. We had discussed this point in our Junto, where I was on the side of an addition, being persuaded that the first small sum struck in 1723 had done much good by increasing the trade employment and number of inhabitants in the province, since I now see all the old houses inhabited and many new ones building, whereas I remembered well that when I first walked about the streets of Philadelphia, eating my roll, I saw most of the houses in Walnut Street, between Second and Front Streets, with bills on their doors, "To be Let"; and many likewise in Chestnut Street and other streets, which made me then think the inhabitants of the city were deserting it one after another.
>
> Our debates possessed me so fully of the subject that I wrote and printed an anonymous pamphlet on it entitled "The Nature and Necessity of a Paper Currency." It was well received by the common people in general; but the rich men disliked it, for it increased and strengthened the clamor for more money; and they, happening to have no writers among them that were able to answer it, their opposition slackened and the point was carried by a majority in the House.

My friends there who conceived I had been of some service, thought fit to reward me by employing me in printing the money; a very profitable job and a great help to me. This was another advantage gained by my being able to write.

> The utility of this currency became by time and experience so evident as never afterwards to be much disputed; so that it grew soon to 55,000 pounds, and in 1739 to 80,000 pounds, since which it arise during the war to upwards of 350,000 pounds, trade, building, and inhabitants all the while increasing,

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though I now think there are limits beyond which the quantity may be hurtful.

It is said that Thomas Edison gave about as much attention to the study of money as to science and invention. With your permission I would like to quote from an interview given by Mr. Edison on his inspection of Muscle Shoals [reading]:

> If the currency is issued, $30,000,000, for financing the finishing constructions of Muscle Shoals work, it will be the proper thing to do. Once the currency method is tried in raising money for public improvements the country will never go back to the bond method.
>
> Make it perfectly clear that I'm not advocating any changes in the banks and banking. Banks are a mighty good thing. They are essential to the commerce of the country. It is the money broker, the money profiteer, the private banker, that I oppose. They gain their power through a fictitious and false value given to gold. Gold is a relic of Julius Caesar, and interest is an invention of satan.
>
> Gold is intrinsically of less utility than most metals. The probable reason why it is retained as the basis of money is that it is easy to control. And it is the control of money that constitutes the money question. It is the control of money that is the root of all evil.
>
> Gold and money are separate things, you see. Gold is the trick mechanism by which you can control money.
>
> Gold is not money until the people of the United States, and other nations, put their stamp of approval on it. It is not the gold that makes the dollar. It is the dollar that makes the gold. Take the dollar out of the gold and leave it merely yellow metal, and it sinks in value. Gold is established by law, just as silver was, and gold could be disestablished, demonitized by law, just as silver was. When silver was demonetized the former so-called dollar became worth about 50 cents.

On Monday the United States Supreme Court decided that the Congress had not the right to delegate power to individuals to create codes and regulate business. How can we reconcile the delegation of the constitutional powers of Congress to private individuals of the greatest privilege of all to create and regulate the value of money?

In conclusion, I do not believe our trouble is one of over-production, but it is rather of under-consumption and mal-distribution due to an antiquated banking and currency system. I believe the real road to prosperity is a full agricultural and industrial production—lower tariffs and expansion of world trade. Yet I do not believe that these can be attained without a modern central bank, a bank not dominated by politicians or private or selfish interests, but a bank run in the interest of the country—a banking and currency system that is in accordance with the Constitution, that Congress has the right to coin and regulate the value of money.

For these reasons I favor the prompt passage of a central banking bill having the underlying principles of the Nye-Sweeney banking bill.

Senator BULKLEY. Do you feel that if we should elect directors of the bank in the same way we elect Senators, we could keep it free from politics just the same as we always do in the Senate?

Mr. HARRISS. Senator, I would rather take a chance on that than what we have.

Senator BULKLEY. I just wanted to make sure that that would insure being kept free from politics.

Mr. HARRISS. I believe the Senators and Congressmen on the whole have done a pretty good job.

Senator BULKLEY. Yes; and never have been affected by any political consideration at all?

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Mr. Harriss. I expect at times they have, Senator. But these men would be elected for long terms, for 12 years, and I think they would be more independent of the popular cry than you gentlemen here.

Senator Byrnes. You are in favor, I judge, of the election of members at the time that Representatives are elected?

Mr. Harriss. Yes, sir; for a period of 12 years.

Senator Bulkley. And the issue of currency would be committed to that central bank?

Mr. Harriss. I should think they should have full control of it, both the issuance of currency and the contraction of it.

Senator Bulkley. Would that be a constitutional delegation of power, inasmuch as the Constitution reposed that right in Congress?

Mr. Harriss. I am not a lawyer, but it would seem to me far more constitutional than what we have now. It is now in private hands. This would be a Government-owned bank.

Senator Bulkley. We have got it in private hands now, you say?

Mr. Harriss. It is dominated by them.

Senator Bulkley. Not under the control of Congress?

Mr. Harriss. I do not think so, Senator.

Senator Bankhead. At least, you think they are not controlling it?

Mr. Harriss. I think it has been run and dominated pretty well by the Federal Reserve Bank of New York.

Senator Bankhead. On a credit system by private banks?

Mr. Harriss. Yes; but I think the great question is the control of the expansion and contraction of the currency. That is the fundamental.

Senator Glass. We are obliged to you.

(Witness withdrew from the committee table.)

Senator Byrnes. Is Mr. Kennedy here?

Mr. Kennedy. Yes, sir.

STATEMENT OF EDWARD E. KENNEDY, SECRETARY NATIONAL FARMERS UNION, KANKAKEE, ILL.

Senator Glass. Please give your name, address, and occupation to the official reporter.

Mr. Kennedy. Mr. Chairman and gentleman of the committee, my name is Edward E. Kennedy; I am secretary of the National Farmers Union; my home is at Kankakee, Ill.

I want to bring to the committee the viewpoint of the farmers as represented by our organization with respect to the Nye-Sweeney banking bill. I do not come before this committee as a banking expert, but one, rather, who represents an industry that has been persecuted by the system that has made possible the deflation of American agriculture beginning in 1920.

At that time I was living on an Iowa farm. I was operating a farm of about 335 acres, feeding about 4 loads of cattle every year, and also about 2 loads of hogs for market. In 1920, when the deflation was put on by the Federal Reserve Board, I owed a local bank about $13,500, and I had hoped and expected, in carrying on my farming operations, to be able to repay that debt in the same kind of dollars that the debt was contracted in. By the end of 1921 I was compelled to pay, insofar as I could, the debt with 3 bushels of corn for every 1 for which I had contracted, and 300 pounds of pork or

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300 pounds of beef for every 1; and, of course, it was impossible, under those circumstances, to make the payments. That was the condition not only of one but the condition of thousands and hundreds of thousands—yes—and millions of farmers throughout the United States.

I want to bring to the attention of the committee the fact, if I may, that one of the major changes in the agricultural industry since 1920 has been the almost continuous decline in the value of land and buildings, farm implements, and livestock, from 1920 down to 1934.

Going back to 1910, the value of all farm property increased from $41,354,000,000 in 1910 to $78,436,000,000 in 1920, or an increase of about 90 percent.

During that period when the value of farm property increased about 90 percent, the mortgage indebtedness of the farms of the United States increased from $3,320,000,000 in 1910 to $7,857,700,000 in 1920, and in 1930 the mortgage indebtedness had risen to $9,241,390,000, or very nearly 300 percent.

From 1920 to 1933 the value of farm property decreased to $35,812,000,000, or a decline to $42,626,000,000, or over 54 percent.

At the beginning of 1934 the total value of all farm property was $37,027,000,000, or 3 percent higher than on January 1, 1933; and this 1934 figure is still 10 percent, or $4,327,000,000 lower than the value of farm property in 1910. This notwithstanding the fact that our total mortgage debt as of 1930 was approximately 300 percent higher than 1910.

The agricultural mortgage debt has decreased from 1930 down to 1934 approximately 8½ billion dollars. This, of course, is not because the farmer has been able to pay his debts; he has not been able to pay them. This decline in the mortgage debt is because of foreclosure, bankruptcy, and surrender of farm property.

Taking another angle of the deflation of farm values which come within the figures I have given you, the value of all livestock on owner-operated farms dropped from $8,815,000,000 in 1919 to $3,072,000,000 in 1934. The value of farm machinery on the owner-operated farms dropped from $3,156,000,000 in 1919 to $2,300,000,000 in 1934. This represents a loss on owner-operated farms of $5,743,000,000 in the value of livestock and over $856,000,000 in the value of farm machinery and equipment from 1919 to 1934.

In support of the principle of the Nye-Sweeney bill, that the Government of the United States should own the facilities that provide the currency and credit for the American people, I want to cite to you an instance that happened in 1920. On May 23, 1922, Congressman Phillip Swing, of California, in the House of Representatives, had this to say [reading]:

> Mr. Chairman and gentlemen of the committee, this proposal to add an additional number to the Federal Reserve is here because there is an urgent need that agriculture and its interests be heard by the Board. I cannot understand how men can continue to deny that the deflation adopted by the Federal Reserve Board was deliberately aimed at the farmers of this country. I was present at a meeting of the bankers of southern California, when W. A. Day, then the deputy governor of the Federal Reserve Bank of San Francisco, spoke for the Federal Reserve bank and delivered the message which he said he was sent to deliver. He told the bankers there assembled that they were not to loan to any farmer any money for the purpose of enabling the farmer to hold

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any of his crops beyond harvest time. If they did, he said, the Federal Reserve bank would refuse to rediscount a single piece of paper taken on such a transaction. He declared that all the farmers should sell all of their crops at harvest time unless they had money of their own to finance themselves, as the Federal Reserve bank would do nothing toward helping the farmers hold back any of their crop, no matter what the condition of the market.

Mr. Cooper of Wisconsin interrupted Congressman Swing and said, "Did the gentleman from California hear that?" Mr. Swing answered, "I did. I think I was the only person present that was not a banker. This was, in a way, confidential advice given by the Federal Reserve bank for the guidance of the smaller banks, many of whom were members." One of the bankers asked Mr. Day this question: "If you say to us we cannot loan the farmers money to hold crops, to whom may we loan money to hold crops until they can be taken up by the market in an orderly way according to the demand of the consumers?" "Oh", said Mr. Day, "of course, we will have to loan money to middlemen to take up the crop and hold it until the market is ready for it."

It is beyond question that the deflation began on the 18th day of May 1920, at the meeting of the Federal Reserve Board, which not only brought about the deflation that we are still in but it was first applied to the farming sections of America, and the deflation bore down the value of farm products, bore down the value of farm lands, and the banks of the country foreclosed on the farms and the farmers lost their homes and it destroyed buying power, and it has progressively increased unemployment until today we have eleven and a half million people unemployed in the United States.

It is the belief of the Farmers Union that the principles of the Nye-Sweeney bill should be enacted into law to place the ownership of the central banks and the control of the currency and credit of the United States that is used as the economic lifeblood of the Nation out of the hands of those who use it for profit and put it into the hands of the Government, where it can be used for service to maintain equitable and just price levels; price levels that are not fluctuating from year to year and from month to month to increase and multiply the debts of the farmers who are unable to pay their obligations on the basis that they contract them. It is for that reason that the National Farmers Union, not only at its last convention but at previous conventions, has endorsed whole-heartedly and unanimously the principle of a central bank owned by the Government of the United States. We are supporting the Nye-Sweeney bill.

We believe, and I think it is generally accepted, that deflation or contraction of credit, the withdrawal of currency—particularly credit money which is being used as a medium of exchange—has been taken down from around $22,000,000,000 to around $15,000,000,000. That is a loss of $7,000,000,000 in the means by which wealth circulates and the exchange of goods is carried on and commodities are distributed. We believe that that power has been so great in the hands of private bankers or Federal Reserve banks to have destroyed agriculture and employment by destroying money, and everyone also agrees that if we were to expand the currency sufficiently to do the money business of the Nation, we would again bring price levels back so that the American farmer would have an income from the products of his farm enough higher and far above his debt level and the level of his fixed charges so that he could go into the market and buy the products of the now idle labor; the power of the Federal Reserve banks is too great a power to rest in the hands of private individuals or private corporations, because the welfare and the

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security of 126 million people depend on having a sufficient medium of exchange to distribute the goods and services that the American people produce.

I want to say just one thing more in connection with this matter, and that is that if the situation that has obtained here for the last 5 or 6 years particularly continues, if the situation is that the Federal Reserve banks and our present banking system cannot expand the credit and make it available to agriculture, make it available to small businesses, make it available to the people who must depend upon production, must depend upon their labor for a living—if they cannot under the present system expand the credit, expand the currency, then the system has failed.

On the other hand, if it is because they do not want to do it, because they are afraid that they cannot make loans to the farmer—which they cannot, because the farmer is not receiving a price that covers his cost of production and he is not getting enough above the debt level to make him a good credit risk—if that is the situation, either that they cannot or they will not provide a medium of exchange, and they have a monopoly on the control of the volume of currency and controlling the volume of credit—if they cannot or if they will not do this, then the Government ought to take over the Federal Reserve System and operate it under the provisions and under the principles of the Nye-Sweeney bill.

Senator Glass. The committee is obliged to you.

We will adjourn now until 10:30 tomorrow morning.

(Whereupon, at 4:20 p. m., an adjournment was taken until tomorrow, Thursday, May 30, 1935, at 10:30 a. m.)

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BANKING ACT OF 1935

THURSDAY, MAY 30, 1935

United States Senate,
Subcommittee of the Committee on
Banking and Currency,
Washington, D. C.

The subcommittee met, pursuant to adjournment on Wednesday, May 29, 1935, in room 301, Senate Office Building, at 10:30 a. m., Senator Carter Glass presiding.

Present: Senators Glass (chairman of the subcommittee), Bulkley, Byrnes, Townsend, and Couzens.

Also present: Senator Fletcher of Florida and Senator Norbeck of South Dakota.

Senator Glass. The subcommittee will come to order. Before we start the hearing, at the request of Senator McAdoo, who cannot be present this morning, I would like to put a telegram into the record from Mr. A. P. Giannini protesting against the proposed one-eighth assessment for insurance of deposits.

(The telegram referred to and submitted by Senator Glass is here printed in full as follows:)

San Francisco, Calif., *May 29, 1935.*

Hon. Wm. G. McAdoo,
Care of Vera Ward, Apartment 516, Albans Towers.

I am heartily in favor of the reduction of the assessment rate for deposit insurance as covered in title 1 of the banking bill from one-eighth to one-sixteenth of 1 percent. The one-eighth percent rate was written into the bill by the House and constitutes a very substantial increase over what the Federal Deposit Insurance Corporation, who should know best about these matters, had recommended. I consider the one-eighth percent an unjustifiable burden to place upon the earnings of banks at this time.

A. P. Giannini.

Senator Glass. I also place in the record, at the request of Senator Fletcher, a letter from former Senator Owen of Oklahoma, suggesting an amendment to the pending bill.

(The letter referred to and submitted by Senator Glass is here printed in full as follows:)

Washington, D. C., *May 29, 1935.*

Hon. Duncan U. Fletcher,
Chairman Committee on Banking and Currency,
United States Senate.

My Dear Senator Fletcher: The Supreme Court decision of Monday, May 27, on the National Recovery Act makes it important that the powers granted to the Federal Reserve Board by the proposed Banking Act of 1935 submitted by you should have a clear mandate instructing the Federal Reserve Board as to what executive use shall be made of the powers granted.

While the purpose of the act is generally understood, as a matter of surmise or conjecture, there is need of a plain declaration of the policy and the purpose for which such great powers are now proposed to be conveyed to the Federal Reserve Board.

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I submit for your consideration a declaration of such purposes and proposed mandate as follows:

"It is the purpose of the Federal Reserve Act as herein amended, to regulate the value of money; to furnish the people at all times with a supply of sound credit and currency, adequate for the acievement and maintenance of maximum business activity and employment; to create conditions conducive to the restoration of the value of property, labor and services and to the restoration to normal of governmental revenues, thus enabling the Government, without public distress, to establish and maintain a balanced budget; therefter to establish and maintain a dollar of uniform, permanent debt-paying purchasing power by regulating the supply of money and credit.

"The Federal Reserve Board and the Federal Reserve banks shall use the powers granted to them to make effective the purposes herein set forth."

There is no mandate in the bill introduced in the Senate, and the mandate inserted in the House could easily be interpreted as an instruction of Congress not to expand credit but to establish "business stability" on the present depressed level with 20,000,000 people on relief and a hundred million people in distress.

The officials of the Federal Reserve Board have been advising the President, and did so in my present, "that the banks have more than ample credit" or money with which to furnish the business interests of the country with needed capital. It is true that the banks have excess of over 2 billions and could expand loans 20 billions without violating the laws which limit loans. The banks could restore the working capital destroyed by them when they contracted private loans 20 billions. The banks could furnish the working capital to private business enterprises, but the banks prefer to lend their credits to the United States against Government bonds rather than to private industry at higher rates of interest. The fact that the banks could supply capital but refuse effectually closes this door of relief until the fear of the banks to loan and of business men to borrow is removed. This fear can be removed most speedily by a clear-cut declaration of policy and purpose by the Government of the United States through the mandate which I submit to you. Upon the passage of such a mandate the confidence of the banks and of business men would be greatly stimulated and would increase day by day because it is perfectly obvious that under this mandate working capital destroyed by the banks would be soon replaced either by the Reserve banks or by the member banks themselves.

The Reserve Board could expand the bank deposits by purchasing bonds, Federal, State, and municipal, and other sound bankable assets to the extent necessary to restore the working capital destroyed by this depression. They could restore the demand and time deposits very rapidly by buying such bonds and sound assets.

I respectfully request you to submit this suggestion to the Committee on Banking and Currency of the Senate for its consideration.

Yours faithfully,

ROBERT OWEN.

Senator GLASS. Mr. Willard Hamilton, president of the Florida Bankers Association, will please take the stand.

STATEMENT OF WILLARD HAMILTON, PRESIDENT FLORIDA BANKERS' ASSOCIATION, ORLANDO, FLA.

Mr. HAMILTON. Mr. Chairman and gentlemen of the committee, since coming here from Florida I have developed a little hoarseness, and Mr. Andrews of Pensacola has agreed to read my remarks.

Senator GLASS. Very well. That will be satisfactory, sir.

(Mr. James W. Andrews, cashier, American National Bank, Pensacola, Fla., read the statement of Mr. Hamilton as follows:)

Mr. Chairman and members of the committee, in appearing before your committee in behalf of the Florida Bankers Association on the 1935 banking bill, I wish to state that while our committee is a small one it is truly representative of the bankers of all sections of Florida. Mr. J. W. Andrews is cashier of the American National Bank of Pensacola and represents the banks of northwest Florida. Mr. G. E. Lewis is president of the Lewis State Bank of Tallahassee and represents the banks of north central Florida. Mr. George Avent is president

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of the Florida National Bank of Jacksonville, and Mr. Rodgers represents the banks of northeast Florida. Mr. H. B. Oliver is vice president of the First National Bank of Miami and represents the east coast. Mr. C. D. Dyal is president of the Florida National Bank of St. Petersburg and represents the west coast, and myself, Willard Hamilton, president of the Florida Bank at Orlando, and president of the Florida Bankers Association.

While I am well aware of the volume of testimony that has been presented to your committee, I would like to comment briefly on title I of the bill.

The proposed bill which you have under consideration is of the utmost importance to country bankers. It is the opinion of Florida bankers that the assessment of one-eighth of 1 percent on total deposits at this time would be ruinous to many banks, particularly in view of the fact that the majority of Florida banks have made less net earnings to date in 1935 than they did in a similar period in 1934, which period was by no means a prosperous one for Florida banks. Due to this lower earning ratio, the payment of one-eighth of 1 percent into the Federal Deposit Insurance Corporation would, in my opinion, be a strain on practically all banks. In addition to the above facts, banks are faced with further declining earnings for the balance of 1935.

To illustrate, I would mention a specific case of one small bank in Florida whose average deposits are $4,000,000, upon which the assessment would amount to $6,000 per year or 6 percent upon the capital of that particular bank.

I strongly urge that you gentlemen consider these facts and if any assessments are written into the bill, that it will not be in excess of one-sixteenth of 1 percent on the total deposits.

Mr. Rodgers, who is president of the Florida Bar Association, as well as a director and member of the executive committee of one of Jacksonville's largest banks, would like, with your kind permission, to comment briefly on title II.

Gentlemen, I thank you.

The statement is signed by Willard Hamilton, president, Florida Bankers Association.

Senator BULKLEY. Has not business generally been better in Florida this year than last year?

Mr. HAMILTON. Generally speaking; yes.

Senator BULKLEY. To what do you attribute the reduced earnings of banks?

Mr. HAMILTON. I would say, principally the lower interest rate on Government securities.

Senator GLASS. The committee is obliged to you, Mr. Hamilton.

(The witness withdrew from the committee table.)

STATEMENT OF W. H. ROGERS, PRESIDENT FLORIDA BAR ASSOCIATION, AND MEMBER OF THE EXECUTIVE COMMITTEE OF THE FLORIDA NATIONAL BANK, JACKSONVILLE, FLA.

Senator GLASS. Please give your name, Mr. Rogers, and your position, to the official reporter.

Mr. ROGERS. My name is William H. Rogers, of Jacksonville, Fla.; director and member of the executive committee of the Florida National Bank, and president of the Florida State Bar Assocaition.

Senator GLASS. You understand, Mr. Rogers, the pending bills, and we will be very glad to hear anything you have to say.

Mr. ROGERS. I appreciate your courtesy in giving us a few minutes for the presentation of our views at this late stage in your hearings. I shall confine my remarks to title II of the pending bill. I do not come before you as a technical banking expert nor as one who is letter perfect in the language of this bill. I have read the bill, however, and heard it widely discussed in my state and have read in the newspapers a substantial number of the statements with regard to the bill which have been made before your committee and elsewhere.

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I come before you as one of a delegation which has been officially requested to appear here by the executive committee of the Florida Bankers Association to register grave concern which has been aroused in Florida by the implications of this title as we have read it and understood it.

I realize that many thorough, able, and lengthy expositions have been presented to your committee. I will, therefore, not take your time by attempting to reiterate what you have already heard from so many sources. We do feel, however, that we would be untrue to our responsibilities in Florida if we did not go on record with this committee in protest against the passage of this vitally important legislation, without the most careful consideration.

As we understand this title, it undertakes to alter radically banking practice as it has grown up in this country over a long period of years. It not only changes private banking practice but greatly alters the relationships of the private banks and the Federal Reserve banks to the Federal Reserve System.

As I recall, the Federal Reserve System was established some 20 years ago on the basis of recommendations of a very capable commission which gave years of study to American banking needs. On the basis of the recommendations of this commission, Congress gave careful and deliberate consideration to the proposals advanced and ample opportunity was given for a Nation-wide discussion.

Senator BYRNES. Do you refer to the Aldrich-Vreeland Commission?

Mr. ROGERS. Yes, sir.

As a result, it was decided by the Congress that we did not need in this vast country a central banking system, but rather a regional banking system in touch with local requirements and conditions.

As I read the proposed bill, it does not merely modify the Federal Reserve Act as we have known it for the past 20 years. It substantially repeals the Federal Reserve Act as we know it and, for all practical purposes, establishes a central bank under another name.

I may say that this statement was prepared before Mr. Owen D. Young appeared before your committee yesterday.

Let me enlarge on this very briefly. The bill before the Senate would lessen the authority of the governors of the Federal Reserve Banks by making their selection subject to the approval of the Federal Reserve Board every year. I think it is fair to say that the Federal Reserve governors would not have the courage and independence of action which they now enjoy if they should owe their positions to the favor of the Federal Reserve Board. In the next place, this bill would give to the Federal Reserve Board unlimited power to raise and lower reserves, absolute power to fix rediscount rates, and the tremendous power to compel the Federal Reserve banks to buy Government securities in any amount, whether they individually desired to do so or not. Under the bill as it is written, the Federal Reserve governors would, of course, be consulted, but if their judgment differed from that of the Board, they would have no choice but to carry out the Board's orders. If this does not constitute, in substance, a central banking system rather than a regional system, then my long years of interpreting legislative language have been in vain.

But however all that may be, whether I correctly apprehend the true significance of this bill or not, at least I observe that the bill is

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most controversial in its nature. I note that there actually exist directly conflicting views as to its significance and effect.

Moreover, there has been little if anything in the presentation before Congress, so far as has come to my attention, that indicates the existence of any emergency calling for the precipitate passage of this legislation. It involves numerous problems vital to the people of the country as a whole. Would it, therefore, not be the part of wisdom to postpone action on title II of the bill for more mature consideration by Congress and by the people?

I am not unfamiliar with the intricacy and gravity of the problems that must confront you in the consideration of this measure. Only a few years ago I was privileged to serve as the chairman of a commission which revised the Florida laws of dower, descent, distribution, wills, and administration. For this comparatively simple matter we took 2 years' time, spending more than 6 solid months solely in deliberation and drafting. For a matter as serious and as vital to the welfare of the whole country as this pending measure undoubtedly is, I respectfully urge that no less deliberate consideration should be given to it than was given to the Federal Reserve Act in its original enactment.

If, however, it is your judgment that a grave condition of affairs precludes deliberate action, then we would certainly recommend that the bill be modified (1) so that a substantial number of the governors of the Federal Reserve banks, the most experienced, practical men in the System, and who are in closer contact than any others with local needs, should be members of the Open-Market Committee, and (2) that Congress should limit the powers of the Federal Reserve Board to raise or lower reserves by establishing some moderate limit beyond which reserve requirements could not be altered.

In making the foregoing recommendations our delegation in no way questions the motives of the proponents of this bill. We are not considering personalities nor any particular administration. We have arrived at these conclusions on the basis of what we regard as established American principles of government, not lightly to be changed. We see nothing in the present emergency which would seem to us to justify establishing in the permanent law of the land an autocratic centralized control in Washington of the money and credit of the people, as opposed to the existing system with its checks and balances. Under our traditional system vitally important policies are formed, with the participation of the heads of the 12 Federal Reserve banks, who are closely in touch with local necessities and of the business men who are the directors of those local banks in every section of the country.

Senator Glass. Do any members of the committee desire to ask any questions of Mr. Rogers?

Senator Townsend. How many banks have you in Florida?

Mr. Rogers. I think I will have to ask Mr. Hamilton to answer that.

Mr. Hamilton. Two hundred and forty.

Senator Townsend. Do you think you represent the sentiment of most of those banks?

Mr. Hamilton. I think, undoubtedly, in all sections of the State.

Senator Glass. You prefer a statutory reserve, flexible, as I understand it, to the power conferred by this bill on the Federal Reserve Board to raise or lower reserves as they may please?

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Mr. ROGERS. My idea was that there ought to be a limit, so that in some administration we would not have an unwarranted change.

Senator GLASS. Do you concur with the preceding witness as to the proposed assessment on banks for insurance deposit purposes?

Mr. ROGERS. I am not right in the midst of banking insofar as it comes to detailed management, but my knowledge and information of our Florida banks is that the vast majority of them are not able to pay dividends, are not making more than their fixed charge-offs; and it seems to me that if the present fund is sufficient for the present moment, it might be very advisable to go lightly on the banks at the moment. Perhaps in more prosperous times the charge could be raised on a sliding scale.

Senator GLASS. What is the attitude, if you know it, of the Florida Bankers Association as to compelling the insured banks to become members of the Federal Reserve System by July 1, 1937?

Mr. ROGERS. I do not think I can answer that, Senator, for the banks generally.

Senator COUZENS. Do we have any more witnesses here representing Florida banks?

Senator GLASS. No. I will ask you, Mr. Hamilton, if you have had sufficient contact with the bankers of Florida to know what their attitude is on that particular question.

Mr. HAMILTON. I should say that they would desire to have a little longer time; that is, most of the State banks.

Senator GLASS. The committee is obliged to you, Mr. Rogers.

(The witness withdrew from the committee table.)

STATEMENT OF MORTON BODFISH, EXECUTIVE VICE PRESIDENT UNITED STATES BUILDING AND LOAN LEAGUE AND ASSISTANT PROFESSOR OF ECONOMICS AT NORTHWESTERN UNIVERSITY

Senator GLASS. Give your name and address to the official reporter, please.

Mr. BODFISH. My name is Morton Bodfish. I am executive vice president of the United States Building and Loan League, which is the national organization of savings, building, and loan associations. I am also an assistant professor of economics at Northwestern University and was a member of the original Home Loan Bank Board.

My statement, Mr. Chairman and gentlemen of the committee, deals entirely with sections 206 and 210 of the bill. These sections have a bearing on the real-estate mortgage credit policies of the banks. We are naturally somewhat interested in those policies, as they not only affect our institutions in a competitive sense, but we feel that the mortgage lending policies that are sponsored by the Federal Reserve System have a real bearing on the year-in and year-out soundness of our banking system.

It is universally agreed that both the banking system and the mortgage credit system in the United States need study and perfection, in light of the recent credit collapse. Much progress has been made through the insurance of deposits and savings accounts, elimination of security affiliates, and the establishment by State and Federal law of restrictive general policies for the operation of both types of institutions.

I refer to banking institutions and mortgage credit institutions.

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Outstanding in the recasting of credit systems in the country has been the policy that short-term or commercial credit institutions should not engage in long-term mortgage or capital credit activities. This sound principle has been observed elsewhere and explains in some part the stability enjoyed by the banking structure of other countries, notably Great Britain and Sweden. Section 210 of the proposed Banking Act of 1935, supplemented by section 206, proposes to continue and encourage the mortgage activities by banks which violated the above-mentioned banking principle, and which, in the judgment of many of us, was a factor in the recent over-expansion and collapse of credit. This over-expansion in long-term credits led to numerous failures in the banking field, and to a discouraging freezing in the mortgage credit field. Economic historians will certainly record the banking failures as the major factor causing unprecedented price declines, rapid credit liquidation, business failures, and acute general depression. Everything practicable should be done to prevent a recurrence of these conditions.

Mortgages have always played a dominant role in the banking difficulties in this country. It is generally felt that the failure of State bank guarantee systems was largely the result of real-estate mortgage lending activities on the part of the less experienced bankers, particularly in farm mortgages. The dramatic bank failures of the recent depression in Detroit and Chicago and many other localities were convincing evidence that extensive mortgage lending was not sound banking. The depression experience clearly indicates that a bank failure leads to loss of confidence and difficulty in other types of financial institutions.

The banks are adversely affected when savings or investment institutions encounter difficulty. It would therefore seem proper that public policy should more and more restrict the activities of savings institutions—such as building and loan associations, savings banks and insurance companies—to those which have been proved by experience to be appropriate and safe, while at the same time drawing similar rigorous statutory limits about the field of activity of commercial banking institutions. While examples of the satisfactory results of such a policy in foreign countries could be cited, it is necessary only to point to the New England territory, where the separation of commercial banking from savings banking is considered "theoretically desirable" and is largely carried out. There we have had a comparatively stronger and more stable financial structure than in other parts of the country. The concept of division of labor or specialization is as useful, as sound, and as vital in the field of finance as it is in the field of industry and trade. A great and sound step in public policy was taken in the divorcement of security merchandising from commercial banking. It is the judgment of many that equally compelling logic and experience call for similar action in separating banking from long-term mortgage credits.

The primary function of the national banking structure has been to serve the commercial credit needs of the Nation. Many thoughtful bankers and observers doubted the wisdom of the so-called "McFadden Act", which substantially accelerated the participation of national banks in the mortgage field. The records from 1920 up to the beginning of the recent banking difficulties indicate a sweeping expansion in mortgage loans. A question again arises as to whether

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the country and its financial structure would not be in a better position if we developed strong but entirely separate managements, directorates, and trustees, each functioning in individual lines of financial activity. Commercial banking and mortgage financing seem to be distinct and different, and specialization rather than department-store activity should be encouraged as a matter of public policy. Commercial banks deal primarily with manufacturers, jobbers, retailers, or men who own business and business institutions. The problem of mortgage credits is quite different, dealing with a more personal risk, an entirely different repayment arrangement, a different field of law and business practice, and an entirely different type of security.

Following this thought further, it would seem that, if banking institutions of the country are to be encouraged to make longer term investments, then the most needed public service which they can render and which they are best, if not exclusively, equipped to render, is that of capital loans to large and small businesses. I have in mind here financing running from 1 to 3 or possibly even to 5 years. This is a field unserved by private capital at the present time and one more appropriate than long-term mortgages for the employment of demand or time deposits of essentially commercial banking institutions. Such loans offer a profitable outlet, and recent investigation has clearly indicated the need of such intermediate credit for business.

Senator GLASS. Right on that point, do you mean loans merely to the capital structure, or capital working loans?

Mr. BODFISH. Mr. Chairman, I am thinking more of working capital loans that do not meet the requirements of 60 days, 90 days or even 6 months liquidation. I was very impressed some time ago by a study that was made in the Department of Commerce in which they interrogated, through the mails, some 16,000 or 18,000 small business men, and the study seemed to develop this one rather striking fact: that prior to the banking crisis and the resulting strict supervision we have had since then, these small businesses were supplied with advances that would run anywhere from 1 to 2 years as a practical matter. Sometimes they are on shorter-term notes, yes, but there was a renewal policy and the like. That study developed that that kind of accommodation where there seemed to be any possibility that it would not be liquidated in 90 days or 6 months was not available. So my thought was that if we are going to stretch any into the capital field it would be better to encourage the banks a little more along that line than real-estate purposes.

Senator GLASS. I asked you the question because Governor Black, when he was before the Banking and Currency Committee on the question of direct loans to industries in certain exigencies, drew a sharp distinction between loans to working capital and loans to set up new enterprises.

Mr. BODFISH. May I continue?

Senator GLASS. Yes.

Mr. BODFISH. Some of us have given considerable study to the problem of building a mortgage credit structure which would better serve the needs of property ownership, and at the same time resist the acute conditions recently experienced. A very cornerstone of this thinking was the common-sense proposition that, if long-term, nonliquid mortgage loans are to be safely made, they must flow from long-term savings or investment capital, rather than from funds of

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depositors who expected money on demand or, at most, on short notice.

The Banking Act of 1933 moved in the direction of restricting banking institutions to commercial credit activities—sort of a general admonition about going too far in the real-estate field—while at the same time a long-term mortgage credit system was being developed through Federal and State legislation affecting building and loan associations and other types of long-term, trustee, or savings institutions.

There I refer, of course, to the Federal Home Loan Bank Act, and the Home Owners' Loan Act of 1933, in connection with which we have had a great deal of State legislation also in the last 2 or 3 years, and, of course, title IV of the new National Housing Act.

The program was varied and sound, and it is believed that the instrumentalities for furnishing adequate home mortgage credit have been created. They will function adequately at such time as real-estate prices, employment, and other conditions urge citizens to use credit extensively for the building or buying of homes. There is statistical evidence of doubled lending activity today on the part of the trustee institutions. It is my considered judgment that the Congress might better encourage and aid those institutions to greater activity than to desert a sound banking principle in regard to mortgage lending to employ temporarily idle banking capital.

Commercial banking institutions have large sums today at interest costs ranging from nothing to 2 percent. These funds are piled up for three reasons: (1) because the public feels their funds to be safe, as a result of the confidence established through the F. D. I. C.; (2) because of the universal feeling on the part of the public that their funds are available on demand or when they want them; and (3) because of the small present demand for ordinary commercial or business credits. It is emphasized that institutions which cannot directly or impliedly promise immediate availability are not receiving a very substnatial flow of savings regardless of rate. These funds in commercial banks which are obviously demand funds in the minds of the public must be so husbanded and employed that the bank can respond to any demand should less favorable circumstances develop. If such deposits bought at demand prices are invested in real-estate mortgages in large amounts, the result is not only a perilous and deceptive banking structure, but also a situation in which the savings or long-term investment institutions are unfairly placed at a distinct disadvantage in carrying out their normal functions.

It is possible under the proposed Banking Act of 1935 that a substantial portion of the 20 billions of dollars of real-estate mortgages now held by savings, building and loan associations, insurance comcanies, and savings banks might temporarily at least be transferred to the commercial banking structure. It is questionable whether the savings, building and loan association, the savings banks, or the insurance companies can function or expand in face of competition for prime mortgage investments from commercial banking institutions whose cost of capital is today 2 percent or less.

Through the F. D. I. C. the Government of the United States has assumed a moral obligation to the bank depositors of this country. The Congress and the Government must either make certain that safe and sound management policies are followed in the insured banks,

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or face the alternative of paying off the depositors in cash. It is frightening to speculate on the amount of money and the burden on the public credit which would be caused by a future real-estate deflation of only one-half the intensity of the recent one, if the banking structure should acquire the bulk of the long-term mortages. It is not adequate to merely provide loan facilities on such long-term assets in order to meet withdrawal demands of depositors. In the next credit or real estate deflation period, we would find our banking system substantially weakened by long-term, nonliquid real-estate investments, and we would ultimately have to rebuild a sound and separate mortgage-credit system, either through encouraging private or cooperative enterprise, or through direct Government intervention.

Again, the rates which depositors have accepted for commercial bank savings convincingly suggest that they expect to get their money, either upon demand or upon too short notice to justify its investment in long-term real-estate mortgages. It is no real solution merely to transfer long-term frozen assets from a primary lending institution to another institution, even though it be a reserve institution, especially in times of Nation-wide credit stringency. Real-estate loans by their very nature do not have and will not have an organized market or market liquidity.

At the time of the consideration of the National Housing Act, I ventured to state the opinion neither legislation nor insurance arrangements could make long-term mortgages so attractive or so liquid that they could find a cash market at practically face value in times of money stringency. I still think this observation is sound, and yet to be disproved. I believe we can so reconstruct our financial arrangements that the Government, either directly or through the Federal Reserve System, need not assume this responsibility.

While admitting that the United States is over-banked, both in numbers and in dollars—incidentally I looked up the per capita commercial deposits and find they are practically twice those per capita of commercial banks in Great Britain, substantially in excess of those in Canada, and the ratio runs from two times on up, while we have comparatively much lower per capita assets in long-term savings or investment institutions, while admitting that the United States is over-banked, both in numbers and in dollars, it would seem unwise to embark upon any program which would discourage the sound but effective functioning of the thrift and savings organizations. There is much public and private good in providing savings institutions in which the middle classes, and the persons in the humbler walks of life, may be encouraged and rewarded in the form of 4-percent rates on their systematic or accumulated savings. Such institutions have rendered great public service in the past, and have supplied most of the real-estate credit for homes and residential properties, and their work should be strongly supported and encouraged. The proposed legislation will have an adverse effect on the long-term development of the savings institutions and conflict with the Federal Home Loan Bank Board program sponsored by the Government. From the point of view of Government, the jurisdiction and leadership of the Federal Reserve Board should not be expanded into the field of mortgage credits, which is the important and prime responsibility of the Federal Home Loan Bank Board.

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A commercial bank best serves its community by giving it uninterrupted banking service and furnishing credit to those types of business activity for which the bank is intended and equipped.

Commercial banks have never made any consequential volume of construction loans in this country other than short-term advances to construction companies and reliable builders.

The point I am making there is that in the main, construction loans are made by savings institutions and by private mortgage operations direct and do not find their way into the banking system until they become matured and seasoned paper. The reason I make that point is that one of the arguments made, rather effectively, I think, for the extension of those mortgage-lending powers in banks, is that the construction activity is greatly needed now and credit is the only thing that is holding it back. I do not believe an expansion of commercial banking and mortgage lending powers is the answer to construction credit.

Building activity has not been deterred for lack of reasonable safe credit. The price of present properties in relation to costs of construction, vacancies, unemployment, and general unwillingness to incur debts on the part of prudent citizens and conservative businesses explain the lack of volume of construction at the present time. Of course, there are speculative builders and others who would build office building upon office building and hotel upon hotel, and apartment upon apartment if the now regretted 100 percent mortgage credit of 1927–29 were available. Certainly this is not the type of credit that banks or any other type of financial institution should be encouraged to extend even in the interests of more construction.

It is a recognized phenomenon of the business cycle that, following the crisis-depression stage, idle funds accumulate until low interest or complete lack of earnings tempt them into the field of long-term or capital investments. Historically, a large portion of these funds have been needed in the ordinary financing of business when recovery really commences. It would seem to be short-sighted public policy to press bank funds into real estate credits under such conditions.

Furthermore, the savings institutions of the country are able to meet current mortgage demands. Today two-thirds of the building and loan associations are actively making mortgage loans. In addition to the associations, insurance companies have reentered the mortgage market and savings bank participation is increasing in the section of the country which they serve. The problem of these institutions is to obtain sound mortgage risks. The activity and the difficulty of obtaining good loans are attested by active advertising for loans except in a few areas, mortgage recordations and lowering interest rates and loan terms which are a direct evidence of a developing competitive drive for prime mortgage business. In my judgment, another 6 months will see the doubling of this evidence and activity.

So far as building and loan associations are concerned, cash on hand, improved mortgage collections, increased savings and the resources of State and Federal Reserve arrangements put them in a position to lend a billion dollars in the coming 12 months. These institutions loaned over half a billion dollars in 1934. Their resources, together with those of other specialized mortgage lenders, should adequately take care of the mortgage need.

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I refer, of course, to the residential field. I have no opinions or solutions as to the large unit mortgage credit regarding hotels, real-estate bond operations, and the like.

One of the pressing arguments to liberalize the power of commercial banks to make real-estate loans falls when one looks at present restrictions and finds that, if they would, without any change in the act, the commercial banks are authorized to make an additional three billion dollars of such loans. These loans are not limited to 5 years but include any long-term loans insured under title II of the National Housing Act. This indicates, to my mind, at least, that prudent bank managements are not making any volume of real-estate loans, and present authorizations are ample for them to more than double their volume if they consider it sound banking policy.

While necessary and useful at one time, the principal pressure for Government loans—the argument that is made is that the only reason this should be done is because of pressure upon Government lending instrumentalities—in the farm and home field is a result of the unusually favorable terms offered by the Government agencies rather than a clear-cut shortage of mortgage credit for sound risks. Certainly, neither banks nor any other lending institutions should be expected to substitute for the mortgage-relief activities of the H. O. L. C. and the F. C. A., where unusual risks were taken for reasons of broad public policy.

The whole trend in mortgage practice is toward long-term obligations ranging from 12 to 20 years. This is sound, as it provides for repayment of the entire indebtedness in an orderly way and within the income or capacity of the average citizen. These mortgages and all other mortgages, regardless of their legal terms or conditions, are essentially long-term frozen paper which can only be liquidated slowly and over an extended period of time. It does not seem that discount arrangements or other devices can be developed which will safely permit the investment of anything but long-term funds in such securities. The distinction between long- and short-term credits is essentially practical and real. The alteration of the Federal Reserve System to better handle stress or emergency situations should not lead us to broad alterations which would encourage unwise banking.

It should be recalled that when the F. D. I. C. insures deposits it is insuring not only ultimate solvency but it is guaranteeing to a numerous group of creditors that it will pay them on extremely short notice in case of a bank closing because of inability to meet demand deposits or general withdrawals.

It seems to me that past experience indicates that publicly known borrowing under such circumstances does not solve the situation in stress periods. The real solution is a contract or arrangement with those supplying the capital that they cannot withdraw all their funds except through orderly liquidation of the long-term securities in which they are invested. This is the essence of the savings, building and loan associations and cooperative bank plan of operation. If there is a lesson to be learned by English experience which is so often referred to by public leaders in the present day, it is one of no mortgages in the commercial banking structure and broad encouragement of the so-called "building society movement." The active construction and favorable interest rates on mortgages which prevail in England at the

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present time are attributable to a strong and virile development of savings, building and loan associations. It would seem wise to follow or pattern after that experience rather than encourage or risk a repitition of our own recent experience in the banking and mortgage credit field.

Therefore, Mr. Chairman, we urge the committee to seriously consider the proposal which is made in this bill to further broaden and encourage the participation of the commercial banking structure of this country in real-estate mortgage credit.

That completes my statement.

Senator Glass. We are very much obliged to you.

The subcommittee will adjourn, now, until tomorrow morning at 10:30 o'clock.

(Whereupon, at 11:30 a. m., the subcommittee adjourned until tomorrow, Friday, May 31, 1935, at 10:30 a. m.)

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BANKING ACT OF 1935

FRIDAY, MAY 31, 1935

United States Senate,
Subcommittee of the Committee on
Banking and Currency,
Washington, D. C.

The subcommittee met, pursuant to adjournment on Thursday, May 30, 1935, in room 301, Senate Office Building, at 10:30 a. m., Senator Carter Glass presiding.

Present: Senators Glass (chairman of the subcommittee), Bulkley, McAdoo, Townsend, and Couzens.

Senator Glass. Mr. Vanderlip, please take the chair in front of the official reporter.

STATEMENT OF FRANK A. VANDERLIP, FORMER PRESIDENT NATIONAL CITY BANK, NEW YORK

Senator Glass. Mr. Vanderlip, you testified before the House Committee, and we have your testimony there available in print, and would not ask you to repeat that, but it has occurred to some of us that since the House acted on the bill you might desire to make some supplemental statement to the committee. We shall be very glad to hear from you.

Mr. Vanderlip. I dictated after breakfast this morning, without the aid of a lawyer or an economist, just a very brief summary of my views. I thought if you cared to have me do so, I would present that, and then you can question me or I can develop points.

Senator Glass. Very well, sir.

Mr. Vanderlip. Congress has been advised by high financial authority to set up a commission to study monetary legislation and go home, in the interests of recovery. I do not agree with that view. Congress has already shown signs enough of abdicating. The Constitution has put specific obligations upon Congress. The Supreme Court has clearly reminded Congress that it cannot delegate its obligations. It is time for Congress to buckle down to business and pass, not a bill that someone else has written for it, but a measure it will devise out of its own understanding. I am afraid it will not get much help from economists, from bankers, or from any other class. This is a job that Congress has got to do for itself.

The trouble with the measure that you now have before you is much deeper than the objections which bankers have belatedly been raising. These banker objections were first raised before you weeks after the measure was presented. They are sound in themselves when they raise questions of political control, when they point to the fact that this measure implements the means of inflation, when they

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demonstrate that the bill will lead the Reserve System further into illiquidity. The banks are stuffed today with 12 billions of Government bonds, and this bill creates a political power which can compel them to add to that illiquid load.

The fundamental misconception of the measure is that it puts the Government into banking, instead of taking the currency out of banking. The regulation of currency is a Government function, not a banking perquisite.

This bill sets up the theory and the method of a managed currency. With the theory, and with the necessity for currency management, I am in accord. But this bill creates a mechanism political in its character, when it should be as nonpolitical as the Supreme Court. The open-market operations necessary to a regulated currency are improperly made a factor in our credit-banking machinery. Under it, commercial banks are compelled by a political body to manipulate their portfolios in accordance with the view of that body instead of in accordance with the credit needs of the communities they serve.

If you are going to regulate the value of money—and I believe you must—how are you going to do it? First, you must have a measure of value. Recent history is replete with illustrations of the fluctuating value of gold. Gold no longer moves from one country to another in answer to the balances of foreign trade.

Look at the news in today's papers. The Bank of France in 5 days loses 5,000,000,000 francs, $325,000,000 of gold, not in the slightest degree in answer to foreign-trade balances, but wholly as the result of speculative movements and panic pressure. The monetary base of the French currency is seriously attacked, and the results may be of the gravest political and social importance. We see here the stability of government itself threatened by deflation. Deflation may be as dangerous as inflation—and both are supremely dangerous.

It is the first duty of Congress to pass a constitutional measure. My opinion is that the bill before you is unconstitutional in that it passes to a political body both the executive powers of currency management and the policy as well. It sets no limit on the range of value that regulation may create. Congressman Spence on May 4 presented the reasoning as to the unconstitutionality of this measure with great force. I myself urged it to the House Banking and Currency Committee and to Governor Eccles, and I urge you to consider this phase.

I believe title II should be fundamentally rewritten. Congress should mandate the objective in regulating the currency. Congress cannot delegate policy; it can only delegate the executive administration of a policy. Inevitably this means that the only true measure of value, a price index, should be adopted by Congress as the guide, and a dollar having stable value measured by a definite price level should be the objective.

By this means you can create an effective barrier against run-away inflation, and without danger of run-away inflation you can raise prices to a level where it is possible to meet debts that were created at a higher price level. The Supreme Court having declared a general farm-mortgage moratorium as unconstitutional, there is no other way left except through currency action to meet the situation of the beleagured mortgaged farmer.

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That covers briefly the main points that I would elaborate if you care to have them elaborated. I believe the measure is unconstitutional. I have been saying that for weeks. I believe it is unconstitutional because the policy management is delegated, and I think that is improper. It is delegated to at least a semipolitical body, and I think that is unwise.

Senator COUZENS. Would it make any difference as to what kind of a body it was?

Mr. VANDERLIP. No. It should be an absolute mandate as to policy.

Senator GLASS. Mr. Vanderlip, would you prefer to have the Congress write in the statute the reserve requirements, whether they be flexible or whether they be stationary, or should that be delegated to what you term this "politically appointed body"?

Mr. VANDERLIP. You have already passed a measure which permits the Board to change those reserve requirements. I believe if you are going to have a stable value to the dollar it is necessary to have the power to change the reserve requirements, because an expansion of bank-credit currency or buying medium could run away with the situation, and the banks are in a position now where, if there were a demand, with $2,300,000,000 of surplus reserves, they could inflate the credit terrifically.

Senator GLASS. Yes.

Mr. VANDERLIP. So Congress might well put limits on it, if it chose, but I should think a nonpolitical body charged with the responsibility of regulating the currency, so as to maintain a price level, might be left free to change those reserves.

Senator GLASS. What would you call a nonpolitical body?

Mr. VANDERLIP. A body organized as nearly as possible along the lines of the Supreme Court—a body appointed for life. Perhaps their terms should terminate at some advanced age, but they should not be removable by the President, and should not be subject to political pressure, and certainly not subject to business pressure.

Senator GLASS. Would have the Secretary of the Treasury and the Comptroller of the Currency on such a board?

Mr. VANDERLIP. Most emphatically not.

Senator GLASS. You would want to see the members of a board such as you describe men of large experience with an understanding both of the philosophy and the technique of banking?

Mr. VANDERLIP. Yes, sir; large experience and great integrity.

Senator GLASS. And courage.

Mr. VANDERLIP. Distinctly courage. The qualifications, in a sense, are the same as the qualifications for the Supreme Court—a knowledge of banking and currency instead of a knowledge of law, but men of irreproachable character, of deep understanding, and of courage and integrity.

Senator COUZENS. Do you have any particular number in mind?

Mr. VANDERLIP. I have thought five would be sufficient. That has nothing to do with the philosophy of the idea.

Senator COUZENS. No. Then you would remove any of the 12 Federal Reserve Banks from any connection or influence with the board.

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Mr. VANDERLIP. I would cut the whole currency function out of the banks, and on the other hand I would not have the open-market operations necessary in regulating the currency inflicted on the banks. I would have the Federal Reserve System returned to what it was originally organized for.

Senator GLASS. The open-market provision was never intended to be used as it has been used.

Mr. VANDERLIP. Never.

Senator TOWNSEND. Would you put the open-market transactions in this commission?

Mr. VANDERLIP. Yes, sir; so far as the regulation of the currency is concerned. Of course, the banks, in the ordinary course of their business, will have certain open-market operations, but they should not have the objective of regulating the currency, the responsibility, nor the opportunity.

Senator GLASS. Should they have the objective of financing the deficits of the Government?

Mr. VANDERLIP. They should distinctly be protected from pressure to do that. The deficits of the Government should be financed from the investment funds, not from demand deposits.

Senator GLASS. And by taxation.

Mr. VANDERLIP. Most assuredly by taxation, and mainly. I think this bill will further unsettle confidence in the liquidity of the banks. I do not approve of the long-term real-estate mortgages being injected into bank portfolios. I do not approve of what somebody may call a sound security being rediscountable, and a basis for currency issue. The thing is absurd.

Senator COUZENS. I do not quite understand how you would operate this board to regulate the purchasing power of the dollar.

Mr. VANDERLIP. I would give to this board—I have called it a monetary authority—the exclusive power of currency issue. They would, in the first instance, take over all the gold and all the silver. I am sorry there is silver to take over, but it is there and has got to be provided for. They would issue their circulating notes. Their other powers are all in this bill. First, they should be able to buy and sell in a free open market, gold and silver bullion, just as is being done in England today, and will continue, in my opinion, to be done for a great while to come. The talk of England stabilizing to gold is "moonshine", I believe. Then, having taken the right of currency issue away from the Federal Reserve banks, but wanting them to continue to be able to rediscount for member banks, I would have it obligatory upon the authority to rediscount for Federal Reserve banks, with their signature, the rediscounts they had in their portfolio from member banks. That would enable them to go on in the function for which the bank was organized, ability to rediscount proper paper—not merely sound paper, but short-time paper, self-liquidating paper, I believe. Then, the other powers would be to buy and sell short-term Treasury paper, having not over a year to run, bankers' acceptances, and foreign exchange. The balance sheet would be the simplest thing. There could never be more than one item on the liability side—the notes outstanding. On the other side there would be gold and silver, Federal Reserve rediscounts, short-term Government bonds, bankers' acceptances, and foreign exchange. Those are the levers by which you could manage the currency.

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Senator COUZENS. The manipulation of those would be the method that you would use to maintain the purchasing power of the dollar, is that correct?

Mr. VANDERLIP. Yes, sir. Whenever current prices were below the mandated level they would have to manipulate by increasing the currency, or any of these methods; but, so much more important to me, whenever prices got above that mandated level they would have to restrict the currency.

Senator BULKLEY. Mr. Vanderlip, how rapidly do you think you can get an effect on prices by those manipulations?

Mr. VANDERLIP. Very rapidly, because this manipulation includes the making of the price of gold. You make the price of gold in dollars——

Senator BULKLEY. But we did change the price of gold, and did not get a very prompt effect on prices.

Mr. VANDERLIP. We got quite a prompt effect on the basic commodities, and there is a very important point. It must be the basic commodity price index that is used. If you take the general commodity price index of 784 articles, it moves too slowly.

Senator BULKLEY. Excuse me right there. Would you ignore that general list of 784 articles?

Mr. VANDERLIP. Yes, sir. It would follow slowly, and not always accurately, but I would manage it on the basis of about 35 basic commodities having a world market, and there you will eventually get stability of the exchanges. England is doing that today. It is really managing the pound according to the Bank of England basic commodity index, and is keeping the domestic prices level. There is a third of the commercial world in the sterling area now. If we came into the same theory of management of our currency, against a similar price index, there would be the way open for stabilization. You cannot have stabilization between countries that have budget deficits, or that have not the exports to balance their imports, and so forth. You would settle, under this plan, international balances with gold, just as we have always settled them, but you would have to buy the gold in the open market. To me it is so proved that it can be done, by what England has done, that it seems to me almost axiomatic.

Senator COUZENS. Do you think that we can postpone dealing with title II until later, until we go further into this matter, or do you think the circumstances are such that it needs to be treated with now?

Mr. VANDERLIP. You certainly can postpone it rather than pass a bad title II. There can be no question of that—and this is a bad title II.

Senator GLASS. Mr. Vanderlip, Dr. Miller in his testimony before the committee made a suggestion to which I would like to draw your attention and with respect to which I should like to ask for your comment. He suggested that this central board that we speak of in this bill, or that is spoken of in this bill, or the central monetary board that you advocate, should be designated or denominated "a board of governors of the Federal Reserve System"; that instead of having a governor appointed by the President or designated by the President, the Board itself should be a board of governors of the Federal Reserve Banking System, with statuory authority to select its own chairman to preside over its deliberations. What would you say as to that?

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Mr. VANDERLIP. It seems to me that misses the essential point. You do not want your managing board of a regulated currency to be also the managing board of the Federal Reserve Banking System. That suggestion applied to the Federal Reserve Board, exclusively related to the Federal Reserve banking, would be all right; but it is fundamental, it seems to me, to take currency out of the banks.

Senator GLASS. You suggest an entirely separate and distinct board to manage the currency exclusively.

Mr. VANDERLIP. Yes, sir. That is its full duty, and I suggest that its powers be mandated. That is the responsibility of Congress; and if it is not done, and such a bill passed, I believe it is unconstitutional.

Senator BULKLEY. Do I understand that you are advocating doing, as nearly as we can, exactly the same thing England is doing?

Mr. VANDERLIP. Precisely so. England is doing these things without any law. We could not undertake to do it as England is doing it, because we have no such control over the banking system. There there are only really five banks. And we have not the knowledge that the English bankers have, frankly.

Senator BULKLEY. Who determines the course in England now?

Mr. VANDERLIP. The Chancellor of the Exchequer in conference with the Governor of the Bank of England.

Senator BULKLEY. Just those two?

Mr. VANDERLIP. I should say that those two were the authoritative voices.

Senator BULKLEY. And everyone else follows them voluntarily; is that right?

Mr. VANDERLIP. Yes, sir.

Senator TOWNSEND. Mr. Vanderlip, did I understand you to say that you think this bill, as it is now written, is unconstitutional?

Mr. VANDERLIP. Yes, sir. The bill as first written had no objective at all. I roared a good deal about that, and whether that did any good or not I do not know, but they then wrote in an objective that was taken from the new Canadian banking act. A few words were changed, to make it even less intelligible, and that is set up as the mandate. Now, the Board could take any action you can conceive of, and nine Supreme Courts could not tell whether it came within that mandate or whether it did not.

Senator GLASS. They could not even tell by a 5-to-4 decision? Mr. Vanderlip, I have been very much interested in your testimony this morning. I am sure all the committee has, and we are greatly obliged to you for coming down and giving us the benefit of your advice.

I notice that you still advocate the short maturities.

Mr. VANDERLIP. Yes, sir.

Senator GLASS. In order to bring about liquidity. As I recall, in 1913 you wanted to have shorter maturities than we finally agreed to.

Mr. VANDERLIP. Yes, I did.

Senator BULKLEY. Have you indicated your position with respect to the additional facilities for real-estate loans?

Mr. VANDERLIP. Yes, sir; in many speeches, before committees, and in letters. Of course, you have some banking legislation ahead of you sooner or later. I believe we must eventually see that we must divide banking, so that we have strictly demand deposits in commercial banks, and investment banks that take care of these long-term things. There is the greatest need for some facilities for

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long-term real-estate mortgages. Do not think that I am against that at all.

Senator BULKLEY. But you are against mixing it up with commercial banking?

Mr. VANDERLIP. Tremendously against it. I know it will add to the illiquidity of the banks, and I think that they are far from liquid today. Let the banks try to sell these Government bonds.

Senator McADOO. You mean gradually or all at once?

Mr. VANDERLIP. Either way.

Senator McADOO. Mr. Vanderlip, I did not have the pleasure of hearing your testimony, I was unavoidably detained. But on this question of real-estate loans, would you mind stating briefly, for my information, what your attitude is about that? As the law now stands national banks may make 5-year mortgage loans on real estate.

Senator GLASS. Within a certain limit.

Senator McADOO. Within a certain limit, of course. The suggestion has been made here that that period be advanced to 10 years, I believe, or a longer time, for amortization mortgage loans, with monthly amortization payments.

Mr. VANDERLIP. I thought the bill permitted 20-year amortized loans to be taken into the banks.

Senator McADOO. I do not think so.

Senator GLASS. Certainly.

Senator McADOO. Twenty-year amortized loans?

Senator GLASS. Yes.

Mr. VANDERLIP. Twenty years. I am against taking them in at 5 years or 20 years, or any other date, in a portfolio against demand deposits.

Senator McADOO. I am in agreement with you about that, but I am speaking, of course, with respect to time and savings deposits. Do you make the same objection to that? In California, for instance, banks have the right, under State law, to conduct a savings business and a commercial banking business and a trust business, all in one.

They may do that now to a limited extent under the Federal charters, but would you take the position that real-estate loans should not be made against the savings funds of those banks?

Mr. VANDERLIP. Certainly not.

Senator BULKLEY. Those are segregated assets.

Senator McADOO. They are segregated, of course.

Mr. VANDERLIP. I would take the savings banks entirely out of the commercial banking.

Senator McADOO. They are segregated, of course, under the existing law. The savings departments are kept separately.

Senator TOWNSEND. It is not always done.

Senator McADOO. I am speaking of our State law.

How long a time do you think, on amortized loans, real-estate mortgages might run safely in the savings departments of the banks?

Mr. VANDERLIP. European experience is 20 to 30 years. All this great house building going on in London today is, in the main, against 20-year amortized loans, and they are amortized from the first week.

Senator McADOO. You mean they are weekly payments?

Mr. VANDERLIP. Weekly payments.

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Senator McAdoo. Of course, that makes them much more liquid than if they were monthly payments.

Mr. Vanderlip. Not very much more.

Senator McAdoo. I mean to say it is a more continuous inflow.

Mr. Vanderlip. Yes.

The Chairman. We are very much obliged to you, Mr. Vanderlip.

Senator Couzens. Have we any other witnesses this morning?

Senator Glass. I have asked Mr. James, of the Federal Reserve Board, to come before the committee.

STATEMENT OF GEORGE R. JAMES, MEMBER FEDERAL RESERVE BOARD, WASHINGTON, D. C.

Senator Glass. Mr. James, the committee has expressed a desire to hear something from other members of the Federal Reserve Board as to the pending bills now being considered, the Senate bill, and the bill as amended by the House. Since you are, in point of service, one of the oldest members of the Board, I thought we would like very much to hear some comment from you on the bill, as to the desirability of immediate legislation of this description, or its deferment to a future session of Congress, or as to the desirability of the proposal as it stands.

Mr. James. Senator, since I have had nothing whatsoever to do with the preparation of the bill, I am somewhat reluctant to offer the committee any suggestions. I would be very glad to answer any questions.

If I had any thought to put in the record it would be an expression of a feeling that I have that the public may be expecting a great deal more from the banking authority, which may or may not be set up by this bill, than it is possible for that authority to accomplish. I think there are distinct limitations as to what can be accomplished through the orthodox central banking operations. The experience of the last 12 years that I have served on the Federal Reserve Board indicates to my mind that there are very distinct limitations as to what can be accomplished, for instance, by raising the discount rates or lowering the discount rates, or by open-market operations.

With the law as it is now, it is perfectly obvious that an open-market operation can be indulged in by the Federal Reserve System so long as it is a case of buying, and making money easy in the market. I am rather at a loss to know where they would find the customers if they wanted to sell any appreciable amount of these securities, in making a reverse movement in the said operation. So, I think it might be well to say that I regard the possibility of control of prices and volume of business and employment through open-market operations and other manipulations of the currency, as a very limited factor in what would be necessary to bring about the stability which I understand is the objective.

I am not in accord with the idea of joining the offices of Governor and Federal Reserve agent, or eliminating the chairman of the Board and agent. I think there is a well thought out and well defined purpose in the original act, which to my way of thinking, is very essential in the proper conduct of the Reserve System. The Federal Reserve banks have two important functions, as I see it. One, of course—and the one in which the public has perhaps the greatest interest—is the authority or privilege of issuing currency. There is a protec-

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tion under existing arrangements for the currency on behalf of the public that I think is quite desirable and fully justified. I think the present law, which defines eligibility, is quite all right insofar as the kind of paper that is to be used behind the currency is concerned, and it is in that connection that I would like to see this dual set-up in the Reserve banks. The collateral behind the currency is a special responsibility of the chairman and agent looking after that side of it. The governor of the bank is, of course, the chief executive of the bank when the bank is performing its ordinary bank functions, making loans, extending credit to the member banks, and carrying on other activities in the bank. But, as I see it, the governor is the servant or employee of the board of directors, and it is to the board of directors that one should look for the proper conduct of any bank.

I am rather inclined to believe that the proposal to limit the terms of office of directors in a Federal Reserve bank to two terms of 3 years each is a mistake. I never have seen a banker that wanted to change his board of directors every 6 years. If you have a good board of directors, you had better keep them. It takes 6 years, and a lot longer than that, to learn very much about Federal Reserve banking and Federal Reserve matters, as I see it. At least it took me 12 years to learn what little I know, and I have still a lot to learn.

Senator GLASS. You can learn all you want to know now in 6 months, can you not?

Mr. JAMES. No; I would not say that, Senator. I am nearly 70, and I have not begun to learn all I want to know yet.

There is one other thing that I would like to advocate, and that is that the smaller banks, what are known as the little country banks, might be protected by a slight change or amendment to the present Federal Reserve Act which would allow them to continue to collect exchange. It seems to me that the small country bank has really performed and is performing, and will continue to perform, a service that is absolutely essential for those smaller districts, and it seems to me likewise vital to them that they be permitted to collect their exchange charges in order to live. There are quite a few banks that I know of now that are making no loans. They are performing a banking service. They are collecting checks, and are living off this little exchange.

Senator GLASS. Does not that mean, Mr. James, that they are living off the commerce of the country without performing any particular service in return?

Mr. JAMES. Senator, I think perhaps custom has made it—well, I might say justifiable, through long practice. I do not mean to say that all banks should be charging exchange, but I do know that the city banks in many cities charge their customers when they deposit checks on out-of-town banks. They say that is an interest charge, because, in giving them immediate credit for an out-of-town item, they are advancing funds, and therefore they are entitled to an interest charge. The little country bank has not any such chance, and in the Federal Reserve System——

Senator GLASS. He has not any such ingenuity to evade the law, either, has he?

Mr. JAMES. I would not like to answer that question, if you please. But it has been advocated among some of the men in the Federal Reserve System that I have talked to about this matter. It is one

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that has been heavily on my mind for the last 10 years, at least—that the charge might well be passed on to the customer, to the depositing customer, as a service charge. But, as you know, throughout the South, at any rate, for the last 100 years or more it has been customary for the city merchant to take care of the exchange charges when they came to him, and I assume that he is able to pass that charge on to the consuming public somewhere. He usually does, in the conduct of his business.

Senator GLASS. I recall very distinctly when we passed the Federal Reserve Act that the chairman of the Ways and Means Committee of the House complained that the bank in his town, in which he was interested, got 90 percent of its profits out of charging exchange for collections.

Mr. JAMES. I think, Senator, I could find you any number of banks which, if denied the exchange charge, would fail to show any profit. They would just be sunk. That is the trouble, as I see it, with the little bank today. I am not talking about the large bank. If my suggestion amounts to anything, it would be to the effect that banks having bank deposits, due to bank accounts, be exempt from the prohibition against exchange charges.

Senator GLASS. You know the existing law, Mr. James, authorizes the Board to permit the banks to charge the cost of collecting checks, and in 20 years you have not been able to find an actuary who could even estimate what the cost is. In other words, if a bank in my town, I being a newspaper publisher, for example, had 100 checks which were given me for the subscription price of my paper, and it would cost that bank, perhaps, 10 cents in postage to collect these checks, why should they be permitted to charge 25 cents on each of the 100 checks?

Mr. JAMES. I think Senator, the law itself, as it now reads, puts a limitation on it, so far as the law is concerned. May I read that section of the law?

Senator GLASS. Yes.

Mr. JAMES (reading):

> *Provided further*, That nothing in this or any other section of this act shall be construed as prohibiting a member or nonmember bank from making reasonable charges, to be determined and regulated by the Federal Reserve Board, but in no case to exceed 10 cents per 100 dollars or fraction thereof, based on the total of checks and drafts presented at any one time, for collection or payment of checks and drafts and remission therefor, by exchange or otherwise; but no such charges shall be made against the Federal Reserve banks.

Senator GLASS. That is an amendment to the law. That was not the original provision of the law. At the time we undertook to put a stop to this imposition of at least $200,000,000 upon the commerce of the country, we permitted the banks to charge the actual cost, and the actual cost was so inconsequential that we were never able to get an actuary who could estimate what it was.

Mr. JAMES. My suggestion was that the law as now written be amended by adding the following:

> except by banks which have no balances due to other banks.

Senator COUZENS. May I ask you if you have studied title II of the bill?

Mr. JAMES. Yes.

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Senator COUZENS. Have you reached any conclusion as to immediate action on it? Do you think the consideration of title II is necessary at this time?

Mr. JAMES. No.

Senator COUZENS. You have not reached any conclusion?

Mr. JAMES. I do not think it is necessary.

Senator GLASS. Mr. James, you stated at the outset that you had nothing to do with the preparation of the bill. Do you know of any member of the Board, except the Governor, who did have anything to do with the preparation of the bill?

Mr. JAMES. No.

Senator GLASS. You did not see the bill until it was printed and sent up.

Mr. JAMES. No.

Senator COUZENS. Have you studied it since it has been printed?

Mr. JAMES. Yes.

Senator COUZENS. Have you reached any conclusions about it that you would care to state to the committee?

Mr. JAMES. I have felt all along that——

Senator MCADOO. You are speaking of title II now?

Senator COUZENS. Yes.

Mr. JAMES. I have felt all along that the provisions which are seemingly the objective of the bill, are already provided. It may be that it might have needed some minor clarification in one or two parts of the act as amended heretofore, but so far as needed authority for carrying out the functions of the Federal Reserve System is concerned, I do not really feel that there is any great need for additional legislation at this time.

Senator GLASS. Have you discovered anything in the proposed legislation to get us out of the depression that may not be done under existing law?

Mr. JAMES. No, sir. I have a feeling, Senator, that the Federal Reserve System has been very much maligned by many writers and many speakers, who seem to attribute our economic evils and ills to a failure on the part of the Federal Reserve System. As I see it, the Federal Reserve System has functioned 100 percent, and if the bankers had not stepped off the reservation, so to speak, and gotten out of the realm of banking into promotion and the creating of deposit liability against prices rather than values, we never would have had quite as much trouble as we have had.

Senator GLASS. The Federal Reserve System has been prepared, and has had a willingness, has it not, to do business with anybody that wanted to do business with the System?

Mr. JAMES. Yes; anybody that was qualified to do it. As I see it, the creation of the Federal Reserve System was for the purpose of providing adequate currency and a reservoir of credit to meet the needs of agriculture, industry, and commerce. There never has been one minute since I have been a member of the Federal Reserve Board, over 12 years, that the Federal Reserve System was not right there to do that very thing, and did do that very thing.

Senator COUZENS. But they did not have any authority to prevent the run-away market in investment securities during the period from 1927 on.

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Mr. James. There, Senator, I think that might be a debatable question, as to whether they had the authority or not. They did not exercise it, if they had it.

Senator Glass. But they have it under the Banking Act of 1933.

Mr. James. They have it under the Banking Act of 1933, as I read it, yes.

Senator McAdoo. What is the chief function the Board can perform under the Banking Act of 1933, which you think will enable it to control speculation, for instance, or the unwise investments by those banks?

Mr. James. It would have been possible for the Board to have gone further than it did in the early part of 1929, when it advised the public, if you recall, that banks were not within their prerogatives when they were discounting at the Federal Reserve Bank and lending their money in the call market. The warning was, as far as the Board felt, under the law, it could go.

Senator McAdoo. You have not answered my question, but in view of your answer I want to ask if you think that by the use of the discount rate alone you could have materially affected that speculative situation.

Mr. James. No, sir; you could not.

Senator Glass. But under the Banking Act of 1933 you have complete control of that situation?

Mr. James. Absolutely.

Senator Glass. Of the member banks as well as the Federal Reserve banks?

Mr. James. That is right. That is as I interpret the law. I am no lawyer.

Senator McAdoo. Are you speaking particularly of the power conferred by that act on the Federal Reserve Board to decrease or increase the reserve requirements of the member banks?

Mr. James. Yes; and more direct action, Senator, if you please.

Senator Glass. That act not only authorizes, but it makes it mandatory upon Federal Reserve banks to keep themselves apprised of the transactions of member banks in speculative investments, and to report any member bank which, in its judgment, exceeds the bounds of prudence, and authorizes the Board to suspend any offending bank from the facilities of the Federal Reserve System.

Mr. James. That is my interpretation of the act, exactly, Senator.

Senator Couzens. In view of the act of 1933 existing at the present time, you do not think there is any necessity for title II? Is that a correct statement of your view?

Mr. James. In the main, yes. There are some other features.

Senator Couzens. What are the other features? You put in a qualification that disturbs me. "In the main", you said.

Mr. James. There are certain things that we were talking about in the beginning. There are some minor adjustments necessary.

Senator McAdoo. The Senator asks what those are. What are the minor adjustments to which you refer? Can you specify?

Mr. James. The one that we were just talking about a few moments ago.

Senator Townsend. That is not in the act now?

Mr. James. No; that is true.

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Senator TOWNSEND. Is there anything in title II that you think ought to be put into law at this time?

Mr. JAMES. Not of necessity or urgency; no.

Senator COUZENS. Do you think that there is or is going to be any general public sentiment for a central bank?

Mr. JAMES. I do not just get your question, Senator.

Senator COUZENS. I say, do you understand that there is any sentiment or do you know of any sentiment anywhere generally throughout the country for the establishment of a central bank?

Mr. JAMES. Why, yes.

Senator GLASS. Among intelligent people?

Mr. JAMES. Well, now, Senator——

Senator GLASS. When I say "intelligent people", I mean people who are acquainted with the philosophy and technique of banking.

Mr. JAMES. I can see no justification for a central bank—if I may be regarded as reasonably intelligent. I think we have got the facilities here, if we merely exercise them within the realm of common sense. There is no trouble about getting along with them.

Senator GLASS. I take it from your testimony, Mr. James—and if I am mistaken, I would like you to point it out—that you advocate a measure of local self-government that now is possessed by the regional Reserve banks?

Mr. JAMES. Yes.

Senator COUZENS. You do not believe that it is desirable to have a central authority in Washington which can control open-market operations?

Mr. JAMES. I think we have that now, Senator.

Senator COUZENS. That has not been the testimony. The testimony has been that a decision of the Open Market Operations Committee, or whatever it may be called, is not mandatory upon the 12 banks. Is that true?

Mr. JAMES. As far as being mandatory is concerned, that may be true; but I am judging from my own experience; and knowing the open-market committee and how it has operated in the past I should say that the Federal Reserve Board has a dominating influence.

Senator COUZENS. Do you know of any instances where the committee's action was not adhered to or was defied?

Mr. JAMES. Oh, yes.

Senator COUZENS. Then it has not been a dominating influence on those occasions, has it?

Mr. JAMES. I do not get you exactly, Senator.

Senator COUZENS. I say, it has not dominated in those cases where there has been resistance on the part of anyone of the 12 banks?

Mr. JAMES. I do not know that there has ever been the kind of resistance that you speak of. The committee has recommended certain things in the past that the Board did not agree with, and because of the failure to agree the recommendations of the committee were not carried out.

Senator MCADOO. Suppose, on the other hand, that the Board's view, if carried out, would have been beneficial to the country; then the Board was powerless to enforce it?

Mr. JAMES. Well, experience has shown, Senator, that the Board has, with the committee, always attempted to reach agreements before action was taken.

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Senator McAdoo. But in case of disagreement, and assuming that the Board's position which caused the disagreement, if carried into effect would have been of benefit to the country, no authority now exists in the Board to enforce its view or views. That is correct, is it not?

Mr. James. That is a correct statement.

Senator Bulkley. Has the policy declared by the Board always prevailed?

Mr. James. Yes.

Senator Bulkley. Always?

Mr. James. Yes.

Senator Glass. Does not the law textually provide that open-market operations shall be carried on only under rules and regulations adopted by the Board?

Mr. James. That is right.

Senator Glass. The only reservation at all being that any individual regional bank may, if it pleases, upon written notice to the Board, decline to engage in a specific open-market operation?

Mr. James. In that case, Senator, if the Board chose to do so and it became absolutely essential to carry out the policy, the Board has the authority to request or direct a particular reserve bank to rediscount for some other bank. That provision is there.

Senator McAdoo. Mr. James, there seems to be an idea which prevails in many quarters that if the Federal Reserve Board should have the concentrated authority to deal with certain things it could probably prevent catastrophes like the panic of 1929. For instance, if endowed with absolute power over rediscount rates, regardless of the views of the various Federal Reserve banks. That is one. Second, through open-market operations in which the Board would have absolute power to prescribe and require the performance of its policy by all the Federal Reserve banks. And, third, the question of reserves. Do you think that if the Board had absolute power over those three things it could, for instance, have prevented the great speculative wave with the resulting panic of 1929?

Mr. James. No, sir.

Senator McAdoo. You do not?

Mr. James. No, sir.

Senator McAdoo. To what extent do you think it could have been an influence and perhaps have mitigated the asperity of the catastrophe?

Mr. James. Through the exercise of the powers you have mentioned, none at all. But under the Bank Act of 1933 they certainly have authority to stop the use of a lot of bank credit in the market.

Senator McAdoo. I just wanted to bring out that point.

Senator Glass. You have testified that there has been no serious friction between the Board and the Open Market Committee. Why should it now be assumed that hereafter there is to be very serious friction and disagreement between the Board and the Open Market Committee?

Mr. James. That possibility does not appeal to me at all, Senator.

Senator Couzens. Have you any record of any interference in the deliberations of the Board by any public officials or bankers?

Mr. James. If you mean persuasive influence, rather than interference, I should say yes.

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Senator COUZENS. Which is the more undesirable, persuasive influence or interference, as you interpret "interference"?

Mr. JAMES. Whichever happens to be the most effective if you are against it, Senator.

Senator MCADOO. Do you mean persuasive influence with a club or with a "big stick", for instance?

Mr. JAMES. They never used any club on me, Senator; I will say that.

Senator MCADOO. Might the persuasive influence to which you refer have been accompanied by a big stick in the background?

Mr. JAMES. If they had a stick they kept it pretty well hidden. I did not see it when they came in.

Senator MCADOO. Perhaps you possessed the degree of intelligence required to be a member of the Board.

Mr. JAMES. I do not know about that.

Senator COUZENS. Mr. Miller testified that the activities of the Board have been on a number of occasions affected by governmental and banking influence.

Mr. JAMES. I think that might reasonably be said to be correct. I do not mean to say by that that there was any big stick, or anything of that kind, but there was perhaps persuasive influence that modified the views of some of the Board members.

Senator MCADOO. The bigger the man who undertook to exercise that persuasive influence, the more effective it was?

Mr. JAMES. It would not have made any difference to some of us.

Senator GLASS. On one occasion the President of the United States publicly announced that speculative investment on the stock exchange was not unreasonable and need not produce any apprehension.

Mr. JAMES. Was it not just a little while after that that the Board made its pronouncement of warning?

Senator GLASS. I think so.

Mr. JAMES. Yes, sir.

Senator MCADOO. That would be a warning to the President of the United States as well as any others?

Mr. JAMES. The trouble is that they would not listen. You can lead a horse to water but you cannot make him drink.

Senator GLASS. Dr. Miller, when he was before the committee, suggested that the Federal Reserve Board be denominated in the statute the Board of Governors of the Federal Reserve System, with authority to select its own chairman; the implication being that that would put every member of the Board on an equal footing with every other member, instead of having a Governor designated by the President, and a Vice Governor. What would you say as to that suggestion?

Mr. JAMES. Out of my experience I should say that it would be more or less immaterial. I have not found that the Governor appointed by the President and confirmed by the Senate——

Senate MCADOO. He is not confirmed by the Senate as Governor, is he?

Senator COUZENS. Yes.

Senator MCADOO. Then the law has been changed as to that.

Senator GLASS. No; the law has not been changed. He is confirmed by the Senate but he is not appointed by and with the advice and consent of the Senate.

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Senator McAdoo. That is what I am getting at. As it stands today, the Governor, as a member of the Reserve Board, is confirmed by the Senate, but he is designated Governor by the President alone and the Senate has nothing to do with that.

Senator Couzens. Oh, yes; it has.

Senator McAdoo. He is confirmed as a member of the Board, by the Senate.

Senator Couzens. He was confirmed as Governor, though. Eugene Meyer was so confirmed.

Mr. James. As a member of the Board, however, not as Governor. What I have in mind is that as to the particular members today, insofar as carrying on the work of the Board is concerned, one has the same standing as another; and the fact that the President should be the man chosen to pick out the gentleman who is to sit at the head of the table and do most of the public relations work is not objectionable to me. It does not make very much difference which one of them is chosen for that particular job, because that is all he does; and I think perhaps he is a little bit handicapped because of the numerous duties and interruptions that come to him from time to time, preventing him from giving the amount of thoughtful consideration to those problems that perhaps some of the other members of the Board are able to give. One suggestion that I understand my colleague recommended is that the Secretary and the Comptroller, the ex-officio members, be eliminated from the Board; and I think that would be a good move if for no other reason than in the 12 years I have been a member of the Board neither of these officers has had the time to give to the consideration of problems of the Federal Reserve Board and to become acquainted with what they were and what the responsibilities were. It is very rarely that they attend meetings. I do not like a divided responsibility, if I can help it. I think the ones that are carrying the responsibility ought to have the authority to do the act.

Senator McAdoo. Their function as ex-officio members apparently is restricted to their appearance at meetings of the Board when you have some important question of policy to decide and where they vote. That is about the way it works out in practice, is it not?

Mr. James. That is practically the way it works, Senator.

Senator McAdoo. I recall that when I was Secretary of the Treasury, as chairman of the Board I was able to attend in the beginning almost every meeting, and was glad to attend. It was in the formative period and it was very important to know everybody's mind upon the problems. But afterwards when the European war broke out and we became more and more involved in big questions that were brought to the country, I found it impossible to attend the meetings of the Board. I think it is a legitimate and very reasonable objection that these ex-officio officers who have very extensive duties to perform outside of the Board have not the time to devote to the business of the Board, and therefore it would not seem to me necessary at all that they should be members.

Mr. James. It is that thought that is in my mind when I state that it would be well to leave them off—not because they have used any influence as far as I am concerned, one way or the other, but because in matters of this kind it seems to me essential that all the members be thoroughly posted and know about the problems.

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Senator McAdoo. It is not a question of the personality of the men; it is a question merely as to whether or not they can perform any useful service as members of the Board because of their official character.

Mr. James. That is it. The control of economic forces sufficient to prevent the speculative debacle that we went through would have covered a long period of time. If by monetary control, through some body like the Federal Reserve Board, if any action could have been taken, we would have had to start back in 1908. It is for that reason, largely, the length of time involved, that I have reached the conclusion that a managed currency or economy can never successfully operate, for the reason that the authority which creates the management would never let it function, regardless of what that authority that created the management may have been.

Senator McAdoo. You do not think there are any prescient minds in the country that can do the impossible?

Mr. James. No; I do not.

Senator Bulkley. Do you mean that you cannot conceive of a board being set up that would be quite independent of some other authority?

Mr. James. No; because if they were sufficiently potent in exercising their authority, the authority which created them would step in and interfere before they had functioned through.

Senator McAdoo. You mean that Congress would likely do that?

Mr. James. In the case of the United States, yes. If it were in a monarchy, it would be the monarch. That is what happened with John Law. He did a very good job, as I see the story.

Senator McAdoo. He was beheaded after that.

Mr. James. Along came a high-pressure salesman with a diamond, if you recall, and it was the diamond that upset the apple cart. When the old Regent felt that he ought to have that diamond, and there was no provision in the budget with which to buy it, he gave an order on John Law to go and get the money and Law turned the check back.

Senator Glass. We are very much obliged to you.

The subcommittee will recess until 10:30 o'clock next Monday morning.

(Whereupon, at 11:55 a. m., a recess was taken until Monday, June 3, 1935, at 10:30 a. m.)

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BANKING ACT OF 1935

MONDAY, JUNE 3, 1935

United States Senate,
Subcommittee of the Committee
on Banking and Currency,
Washington, D. C.

The subcommittee met, pursuant to adjournment on Friday, May 31, 1935, in room 301, Senate Office Building, at 10:30 a. m., Senator Carter Glass, presiding.

Present: Senators Glass (chairman of the subcommittee), Byrnes, Bulkley, Townsend, and Couzens.

Present also: Senator Peter Norbeck of South Dakota.

Senator Glass. Will Mr. Langford, president of the Georgia Bankers Association, take the witness chair, please?

STATEMENT OF H. GRADY LANGFORD, PRESIDENT GEORGIA BANKERS ASSOCIATION, ATLANTA, GA.

Senator Glass. Please state your name and whom you represent.

Mr. Langford. My name is H. Grady Langford, president of the Georgia Bankers Association, Atlanta, Ga.

This statement is presented in obedience to the wishes of the recent forty-fourth annual convention of the Georgia Bankers' Association, voting unanimously to request the privilege of filing its views with your body. The association is represented here by two former presidents—W. S. Elliott, vice president Bank of Canton, Ga., Robert F. Maddox, a director of the First National Bank of Atlanta; by its present president, H. Grady Langford, who is now addressing you; by its vice president, Lee S. Trimble, vice president of the Georgia Railroad Bank & Trust Co. of Augusta; by its secretary Haynes McFadden; likewise attending in company with the committee named is R. E. Gormley, superintendent of banks of Georgia, and James S. Peters, president Bank of Manchester, Ga., also a former president of the Georgia Bankers' Association.

From this enumeration you will see that every class of banks is represented with due regard to size and location. I am president of the Bank of Meansville, Ga., which has capital of $25,000 and is located in a town of 300 inhabitants.

There are 224 State banks in Georgia, of which 25 are members of the Federal Reserve System, and there are 58 national banks in the State.

With the permission of your committee I now wish to request Mr. W. S. Elliott, who is chairman of our legislative committee, to present our testimony in the form of a prepared statement.

(The witness withdrew from the committee table.)

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STATEMENT OF W. S. ELLIOTT, VICE PRESIDENT AND CASHIER, BANK OF CANTON, AND CHAIRMAN OF THE LEGISLATIVE COMMITTEE OF THE GEORGIA BANKERS ASSOCIATION, CANTON, GEORGIA

Senator GLASS. Please state your name, address and occupation for the record.

Mr. ELLIOTT. W. S. Elliott; vice president and cashier, Bank of Canton, Ga., and chairman of the legislative committee of the Georgia Bankers Association.

We approve the proposal to continue the Federal Deposit Insurance Corporation beyond July 1, 1935, with a maximum insurance for any one depositor of $5,000, as proposed in the original bill introduced in the Senate. We are opposed, however, to placing the assessment against total deposit liability at one eighth of 1 percent, and making the collection thereof mandatory, as provided in the bill which recently passed the House of Representatives. This assessment is not only unnecessary, in view of the requirements of the F. D. I. C., as shown by the record since it was organized, but the collection of this amount will work a definite and serious hardship on contributing banks. The dearth of safe, profitable loans, the low rate of investment yield and the rising cost of operation under the recovery program—these factors have made it difficult, if not impossible, for the average bank to earn any sort of return upon its capital funds. According to figures compiled by the Federal Deposit Insurance Corporation, undivided profits of approximately 14,000 insured banks showed no increase during the last half of the calendar year 1934, but registered a decline of $651,000. On June 30, 1934, the figures were $470,668,000, while on December 31, 1934, they stood at $470,017,000, while the combined surplus of the same banks declined $47,330,000 during the same period. Reserves against contingencies, and so forth. declined during the last half of 1934 in the sum of $77,039,000, according to the same report. Relatively few banks are paying dividends on their common stock. The charge of one eighth of 1 percent upon total deposit liabilities will be a real burden, at this time. It is respectfully suggested that one sixteenth would be adequate and fair to the banks; if a higher figure should be insisted upon, it is felt that one twelfth, as proposed in the original bill, would be more than sufficient and that discretionary power should be vested in the corporation to collect only a portion of the annual amount. Eventually, a better plan of assessment may be worked out, equitable so far as the banks are concerned and based upon some sort of actuarial figures. Until the necessity for a larger assessment is clearly apparent, it is suggested that the amount be held to the lower figures.

Compulsory membership in the Federal Reserve System—We oppose the requirement in the Senate bill (S. 1715) that Federal Reserve membership be required of all banks who continue in the F. D. I. C. after July 1, 1937. This provision was stricken from the original bill by the House Committee on Banking and Currency, and the bill was passed by the House with that provision omitted. We respectfully urge upon your committee that compulsory membership provision be not included in the bill when reported to the Senate. It is impracticable for many small banks to comply with the requirements of Federal Reserve membership, especially because of capital

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structure and for other reasons which it is not necessary to mention here. Moreover, joining the Federal Reserve System will entail a substantial loss in exchange on checks which is an important item of income for many small banks and in some cases would result in closure of the banks, should this income be taken away, as it will be if the banks join the system and are forced to remit at par. These small banks perform valuable services in their respective communities many of them, yes, most of them, have been conducted along sound lines for many years. Few of the persons connected with their management entered into the speculative orgy that was such a potent factor in the embarrassment of some of our larger business institutions. The small bank has played an important part in the development of America during the past 75 years and its record compares most favorably with that of other financial organizations. According to the summary gotten out by the F. D. I. C., as of December 31, 1934, there were 1,250 insured banks, not members of the Federal Reserve System, with capital of $100,000 or less; 2,613 with capital over $100,000 but not over $250,000; 1,781 with capital over $250,000 but not over $500,000. This means a total of 5,644 nonmember insured banks with a capital not exceeding $500,000, out of a total of 7,682 insured nonmember banks. These banks have reasons for not entering the Federal Reserve System; they have compelling reasons which have kept such a large number of them out of the system. In our own State of Georgia the toal number of insured banks is 260, of which 58 are national banks, 25 State bank members of the Federal Reserve System, while 177 insured banks are not members of the Federal Reserve System. We feel, Mr. Chairman, that it is not right to force these banks into the Federal Reserve System against their will and better judgment. They are doing very well outside the system. They have carried on for many years, most of them outside the System.

Senator BULKLEY. What are the compelling reasons that keep them out of the system?

Mr. ELLIOTT. One of the reasons, as I just stated, is the fact that they would lose the exchange on their checks if they joined the Federal Reserve System.

Senator BULKLEY. Are there some other reasons also?

Mr. ELLIOTT. There is one other thing; the capital requirements. The capital requirements would be higher in the Federal Reserve System. There are other reasons that a small bank cannot take advantage of some of the benefits of the Federal Reserve System as the larger banks can who have large pay rolls and can ship out to Federal Reserve banks free of charge, and the little bank has few calls of that kind. Consequently it is not able to use the benefits of the system as now constituted, like the larger banks can do. Those are some of the reasons that keep the smaller banks from joining the Federal Reserve System.

Senator BULKLEY. Do many of the banks have a capitalization too small to go into the Federal Reserve System?

Mr. ELLIOTT. A great many of them have capital as low as $15,000. We have quite a number of banks in our own State with only $15,000 capital.

Certainly we should not force them to join when, according to some of those high in official circles, our federalized system of banks is yet

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so far short of perfection. The Federal Reserve System should not be built up by forcing banks to join; rather should the building-up process start from the inside of the system, and such changes made as will cause membership in the system to be attractive to banks now on the outside. Many national banks and State member banks would welcome liberalizing changes which would make their own membership more tolerable. It is significant that only 980 State banks, out of more than 8,600 insured State banks are members of the Federal Reserve System.

It should be pointed out that forcing 7,600 nonmember insured banks to join the Federal Reserve System as proposed in the original banking bill could easily cause such a large number of closures and a consequent burden upon the F. D. I. C. as would seriously imperil the Federal insurance system itself.

Title II of the banking bill—with the great mass of testimony which has been given to your committee in opposition to the enactment of title II of the pending bill Georgia banks are in substantial accord. We are concerned, as all banks in the Nation must be concerned, over the centralization ideas and the political implications contained in title II. We feel that the Federal Reserve banks should be permitted to preserve their regional characteristics and the directors thereof should be permitted to elect local men as their officers without dictation from the Federal Reserve Board; that Federal Reserve banks should have the right to decide as to their participation in open-market transactions; that they should have a right to their own judgment in the determination of rediscount rates affecting their own territory; and that the Federal Reserve Board should not be given the unlimited power to raise or lower the reserve ratio as proposed in the pending legislation.

Unified banking as the goal—title I of the banking bill is filled with provisions which point toward the supplanting of State control of State-chartered institutions and substituting Federal control and regulation for all banks. Requiring the rendering and publication of reports to the F. D. I. C.; giving the F. D. I. C. power to fix fidelity and burglary and robbery coverage for all insured banks, thus doing what State banking departments have been doing well as a rule; giving F. D. I. C. power to impose penalties upon noncomplying banks, some of which run as high as $100—these provisions duplicate or exceed the powers now exercised by State supervisory authorities and subject the State bank to double trouble and expense in connection with matters of routine regulation. No doubt the regulatory offices of the F. D. I. C. will be increased from time to time, until the State departments of banking will be completely overshadowed, and State banks will be driven, as a matter of self-defense, to acquiesce in the abolishment of their own State banking departments. This will be unfortunate, in our opinion. The time is not ripe for the abolishment of the dual system of banking. Even if we should admit that all banking would better be directed from Washington (which we do not admit) the time is not ripe for closing down all State-chartered institutions. Under authority contained in title I State banks who are members of the Federal Reserve System may be required to make three sets of reports and submit to three examining agencies—namely, State banking department, Federal Reserve Board, and F. D. I. C.

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Many bankers see in the liberalizing of loans on real estate a source of danger, and a signboard pointing toward inflation. This will be true if banks take full advantage of the possibilities offered in title II of the bill and expand real-estate lending unduly. It is not believed, however, that commercial banks will be in any hurry to load their portfolios with real-estate paper, notwithstanding the possibility of passing it on to the Federal Reserve System. Today many banks are holding real estate which was once the basis for some of their loans; others have real-estate paper which they have had to charge down materially to the detriment of their surplus and profits. A couple of years ago Federal supervising authorities viewed real-estate loans in a bank as something to be eliminated. It will require a good deal of persuasion, in our opinion, to place many real-estate loans in commercial banks; but, to say the least, the great encouragement given to this type of nonliquid paper is not calculated to emphasize conservatism as a feature of this bill.

On behalf of the bankers of Georgia and of the members of our committee, Mr. Chairman, we desire to express to you our appreciation of the opportunity given us this morning to present our views on this legislation. The superintendent of banks of the State of Georgia, Mr. R. E. Gormley, is present with out committee and has some figures relating to the earnings, and so forth, of State banks in Georgia which may be of some interest to the Banking and Currency Committee. With your permission, Mr. Chairman, I will ask Mr. Gormley to present his statement at this time.

Senator GLASS. Would it be satisfactory for him to present his statement for the record? We have a good many witnesses to be heard, and we want to close the hearings; at least the committee does.

Mr. ELLIOTT. That would be agreeable with me.

Senator GLASS. Just hand Mr. Gormley's statement to the official reporter.

(The statement of R. E. Gormley, of Atlanta, Ga., referred to and sbmitted by Mr. Elliott, is here printed in full as follows:)

STATEMENT OF SUPT. R. E. GORMLEY, ATLANTA, GA.

I speak in behalf of 224 State banks in Georgia. Twenty-five of these banks are members of the Federal Reserve System. I appear before you more specifically in the interest of the other 199 nonmember banks, and to urge the Senate bill be amended to conform to the House bill, as amended by the House Banking and Currency Committee, by striking subsection (y) of paragraph 23, requiring Federal Reserve membership after July 1, 1937, in order to retain membership in the Federal Deposit Insurance Corporation and that a more equitable premium rate for insurance be fixed.

The 199 nonmember banks referred to have capital stocks totaling $8,746,000. Their gross earnings in 1934 were $3,550,000, of which $513,000 was received from exchange. Their net earnings before charge-offs in 1934 was $728,000. Membership in the Federal Reserve System will eliminate practically all of the revenue now received from exchange. Based on figures of 1934 the net income of 199 nonmember banks would be reduced in case of enforced membership in the Federal Reserve System to less than $250,000, or a net return, before charge-offs, on invested capital of $8,746,000 of about 3 percent.

These nonmember banks have loans to Georgia agriculture and industry totaling $40,000,000. These banks are performing a necessary exchange service in the rural districts, and are and will in the future afford the fairest and most intelligent distribution of credit possible to the rural communities. The total deposit of the nonmember banks is $67,000,000. Based on a one-eighth of 1 percent rate, the per annum cost of insurance to these banks will approximate

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$84,000. With enforced Federal Reserve membership and deducting the cost of insurance at the rate of one-eighth of 1 percent, the net income of nonmember banks in Georgia would in 1934 have been reduced to approximately $150,000 on invested capital of over $8,000,000. The earnings of these banks in 1934 were better than in the three preceding years.

Senator GLASS. Is Mr. Stern here?

Mr. STERN. Yes, sir.

STATEMENT OF J. DAVID STERN, EDITOR, PHILADELPHIA RECORD, PHILADELPHIA, PA.

Senator GLASS. The subcommittee has been advised that you desire to be heard on the pending bank bills, and we will be very glad to hear what you have to say.

Mr. STERN. Thank you very much, Senator.

Credit is the coin of today.

Therefore, control of credit is as inherent a function of sovereignty as control of coinage. That is the reason I am for the Eccles bill, which gives the Federal Reserve Board, appointed by the President of the United States, control of the credit volume of the Nation.

It would be as absurd for the Government to grant private citizens the right to coin money as to allow the bankers to continue to dictate the credit policy of the Federal Reserve System. This political paradox has come upon us as gradually as the substitution of credit for cash currency since the Civil War.

Quoting from Woodward and Rose—

> In 1860 cash in circulation was $9.76 per capita, demand bank deposits $9.85 or almost even. In 1880 cash per capita, $13.96; deposits, $44.30. In 1900 cash, $17.10; deposits, $111.57. In 1930 cash, $29.76; deposits, $485.57, or 16 to 1.

But these figures do not tell the whole story. Before the Civil War checking accounts were used only by large concerns for major transactions and had comparatively slow velocity, while cash currency bore most of the burden of the usual business and household transactions.

Today bank deposits or credit dollars represent 85 percent of our medium of exchange. Cash currency is merely a supplementary medium of exchange. The control of the purchasing power of the dollar depends upon the volume and velocity of bank credit in relation to the volume of trade.

Since credit volume and velocity control the value of the dollar, it follows that credit volume and velocity also control the value of the cash dollar, no matter what may be its monetary base. This has been proven again and again as the futility of the Warren and Fisher schemes of varying the gold content of the dollar has become so apparent.

The Constitution reserves to the Federal Government the right to coin money and "to regulate the value thereof." The Government cannot fulfill this function of regulating the value of the cash dollar unless it controls the volume and velocity of the credit dollar, which is the intent and purpose of the banking bill of 1935.

The 12 regional banks of the Federal Reserve System afford a credit reservoir for the Nation. By varying their discount rate, as well as by open-market operations in Government securities, they can vary the credit level in the nonmember as well as in the member banks of the Nation. Here we have a system with 12 intake and 12 outlet valves

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to the reservoir. If 6 of the regional banks open their intake valves and the other 6 regional banks open their outlet valves, they neutralize each others' efforts and defeat the very purpose for which the Federal Reserve System was created.

Therefore, central control of the open-market transactions and rediscount policies is essential to credit control and stabilization of the purchasing power of the dollar at any agreed credit level.

This great economic crisis is the test of efficiency of democracy. If we continue with an irrational system because we haven't awakened to the obvious fact that credit dollars have displaced cash dollars, democracy is doomed.

History bears witness to the persistence of old errors and the bitterness with which the victims of those old errors denounced anyone who tried to correct them.

Copernicus and Galileo are conspicuous examples. Pasteur was laughed off the platform when he attacked spontaneous generation. Today we have with us the advocates of the gold standard. What makes their disillusionment more difficult is that their error is not so old. The gold standard did work and gold did control the value of monetary units when cash currency was the main medium of exchange. It was only when a great credit structure gradually grew atop the gold base that the gold base became relatively unimportant in the price equation.

Persistency of error is based on a natural psychological tendency. The believer refuses to see anything which contradicts his preferred belief.

Thus man had seen the masts of ships appear above the horizon before the hull, and he had seen the curved shadow of the earth on the moon for thousands of years before he accepted these evidences of curvature of the earth.

So monetary conservatives with gold payments suspended in every country except France, Switzerland, and Holland, and with France in the throes of an economic catastrophe, refuse to see any evidence that the gold standard won't work, that credit control has taken its place, that the value of a monetary unit can be measured only in terms of commodity indices and that governments, if they are to survive, must throw off tradition and "can't"—

I sincerely believe that this bill is a great forward step toward modernization and rationalization of our monetary system.

As far as I can discover the main argument against this bill is that it places national credit under political control.

Well, what of it? Political control is certainly safer than private banker control, judging by past experience.

Why shouldn't the administration control national credit as it controls the Army, the Navy, and the Department of Justice? Who wants the Army placed under control of the munition makers to expand or contract as it suits their selfish ends?

They have private armies in Europe, but it hasn't worked out so well for democracy. There's no more room for private control of national credit in a democracy than there is for a private army.

The hand that holds the purse strings rules the roost. Bankers, who can tell the Government how many bonds it can sell, exercise a supersovereignty as surely as the Fascist leader threatens a subservient government with his armed forces.

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Uncle Sam, hat in hand, making terms with the bankers, presents a humiliating spectacle—which should be resented by every true American. This bill will cure that.

The Federal Government should have as much right to say what percentage of the national credit it will take for its own use as it has to say what percentage of our individual incomes it will take in the form of income taxes.

"Supposing the Government misuses this great power over credit, what then?" ask the pessimistic conservatives.

The answer is twofold. If the Government expands or contracts credit unwisely, it will defeat its own ends by impairing credit and business—on the same principle that the Government can dry up sources of taxes by overtaxation.

Just as the power to tax is the power to destroy, so the power to expand or contract credit is the power to avoid or create economic chaos.

But if costly mistakes in credit control are to be made, it is much better that they should be made by the Government than by the bankers. At least we could vote the bungling Government out of office.

We can't do that with the bankers. The same bankers who are responsible for the terrible blunder of uncontrolled inflation which came to its disastrous climax during the fall of 1929, still control our Federal Reserve System and its credit policy.

What is more exasperating, they have the nerve to come down here and argue against this bill, the nerve to tell you gentlemen that credit control is safer in their hands than in the Government's.

Such self-assurance is sadder than it is funny. It bespeaks an utter lack of comprehension of this great power and the responsibility it involves.

National credit control is the keystone of economic stability. It belongs to the Government of the people, by the people, for the people.

(The witness withdrew from the committee table.)

STATEMENT OF CHARLES S. HAMLIN, MEMBER FEDERAL RESERVE BOARD, WASHINGTON, D. C.

Senator Glass. I assume that you are familiar with the pending proposals for revision of the Federal Reserve Act, and the committee will be glad to hear from you.

Mr. Hamlin. Gentlemen, I want to say that I am very glad to come here today at the request of the committee and to express my views on the pending legislation. I shall not try to go into the intimate wording of various amendments. I think I can make myself clear as to the general subject matter.

After an experience of 21 years in administering the Federal Reserve Act I can only say that my respect and admiration for it has increased year by year. The great principles underlying that act, the discount of commercial paper, the massing of reserves, the issue of Federal Reserve notes and, last but not least, open-market power, I think have demonstrated to the country the necessaty for its creation and altogether the success with which it has been administered.

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To my mind, without the open-market power the Federal Reserve System would be purely an emergency system; but I shall speak on that a little later.

I find, however, in reading the various speeches and letters that have been written for and against the proposed bill or bills that there is a great deal of hysteria. I find the air filled with adjectives of fear—perhaps you might say hatred, despair—and some, of course, of comfort. It reminds me of Milton:

> Thick as autumnal leaves that strow the brooks
> In Vallombrosa.

I think it is the duty of any student looking into this matter to rake away these superincumbent leaves and get down to the bottom and find just what these proposed changes in the act are and whether they are consonant with the principles of the act as originally framed and as broadened by Congress.

The original Federal Reserve Act, as you all know, was somewhat enlarged by the provisions for advances to member banks. The scope of it was enlarged by permitting the issue of Federal Reserve notes to banks on the pledge of gold or other collateral, or both. Therefore, I think, in considering whether any proposed amendment is consonant with the principles of the act, we must take the act as originally enacted and as Congress subsequently has broadened it.

The principal cry that I hear throughout the country is that this will make the Federal Reserve Board a central bank. That seems to be the most terrible epithet that can be applied to this proposed legislation. I can remember, back in 1912, I think it was, when the Aldrich Monetary Commission prepared an act for a central bank and when the term was almost a benediction. Now the words "central bank" seem to be used to terrify people. It would almost make a mother take her children and go down into the cellar as if to avoid a zeppelin raid.

Senator Glass. Was it not so used, Mr. Hamlin, in both the Democratic National Convention and the Progressive National Convention, and in the platform written by Theodore Roosevelt, as well as the platform on which Mr. Wilson was elected?

Mr. Hamlin. I am not very fresh on that, Senator.

Senator Glass. Was there any declaration even in the Republican platform in favor of a central bank?

Mr. Hamlin. My recollection is that the Democratic National Convention declared against a central bank. As I understood it, however, it was a direct blow at the Aldrich monetary plan.

Senator Glass. It declared in terms against the Aldrich bill or a central bank.

Mr. Hamlin. I understood that to mean the Aldrich bill or any bill like it which established an operating central bank in Washington.

Senator Glass. Or a central bank. And the platform upon which Mr. Theodore Roosevelt was nominated as a Progressive candidate declared in equal terms against the centralization of credit in Washington and against the proposed Aldrich bill.

Mr. Hamlin. Well, my point simply is that the words "central bank" require an explanation of their meaning when you say them as an epithet or an argument against anything.

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Senator GLASS. We have been discussing it ever since the days of Mr. Jefferson and Mr. Hamilton.

Mr. HAMLIN. Yes; that is true.

The Federal Reserve Act established 12 regional banks with the Federal Reserve Board as the supervisory, controlling authority. As a matter of fact, each one of those Federal Reserve banks essentially is a central bank with autonomy of its own. It has practically all the powers that any central bank in Europe has. In fact, in 1932 Congress extended the power so that the Federal Reserve bank, under certain circumstances, could make a direct loan to individuals. It seems to me that these banks are essentially central banks in their power; but the Federal Reserve Board of course has supervisory control over those 12 autonomous banks, but it has certain centralized powers, if you wish to call it that.

You cannot have control over 12 autonomous banks unless you have some kind of centralized power. That does not make it a central bank; and I can see nothing in this proposed bill that would turn the Federal Reserve bank into a central bank.

Senator GLASS. You make no distinction between 12 regional banks representing business interests of 12 defined territories of the United States, and a central bank here in Washington? Is that so?

Mr. HAMLIN. No; I should say there was all the difference in the world. The centralized power in the Federal Reserve Board to my mind does not create a central bank in any sense of the term.

Senator GLASS. It does not now, no; because it has a supervisory power within the meaning of the law. There is such a thing, however, as our amending the act so as to make it a central bank.

Mr. HAMLIN. Well, the Federal Reserve Board now has power not very much different from the central banking power. It has power to regulate the issue of Federal Reserve notes. It has the power given by the act of 1933 to close the discount window for abuse of the privilege. It has power, which I will speak of in a few minutes, of ordering one Federal Reserve bank to discount the paper of another Federal Reserve bank.

Senator GLASS. It has had that from the beginning, but that requires a certain number of votes of the Board to do that.

Mr. HAMLIN. Yes.

Senator GLASS. In other words, it is a power that must be very cautiously exercised.

Mr. HAMLIN. Absolutely.

Senator GLASS. Under the statutory restrictions?

Mr. HAMLIN. Yes. It has, of course, as I have said, the open-market powers of which I shall speak in a moment.

To my mind, the opposition against these proposed bills is really based on a fear that the Federal Reserve Board is not sufficiently independent to be trusted with those powers—not only the powers which it has, but the powers which it is suggested be added to it; and in my discussion of these amendments I shall base my opinion on the understanding that the Federal Reserve Board, if in the judgment of Congress it is not sufficiently independent, will be made independent; and I believe, if the people of this country felt that the Federal Reserve Board, which I shall show, I hope, is independent in fact, is also independent in law, I believe that two-thirds of the opposition to these amendments would disappear.

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The point is raised that this is not an opportune time for making changes in the law, and that theory has been advanced by a great any bankers.

I understand fully how bankers are fearful of regulations, fearful of power being applied to them, and you can naturally, perhaps, sympathize with the view. But the question arises, why should we now postpone legislation if legislation is necessary? I believe we ought to decide these questions today, because I think the Federal Reserve Act needs some of the amendments suggested in this bill. I think that without the broadening of the open-market power it will destroy the opportunity of major policies designed by the Board. I believe that it is absolutely necessary that some control over reserves be given to the Federal Reserve Board, and that control was asked for, I think, 15 years ago. We asked and almost beseeched Congress to give us that power. I realize that that power, under the Thomas amendment, can now be given with the consent of the President of the United States; but it seems to me that that is a burden which should not be placed upon the President of the United States; that a board of men sworn to do their full duty, men supposed to be of good judgment, could safely be entrusted with that power. Any limitation on that power, limiting the increase in reserves by any percentage Congress wishes, would be perfectly satisfactory, at least to myself.

Senator Glass. But that is not the limitation provided in this bill, is it?

Mr. Hamlin. I think not, Senator. But I am going to say that that is one of the things that I should be very glad to see provided, so that there should be some reasonable limitation.

Various questions have come up. The first amendment that I want to speak of is the power given to the President, of the appointment of the Governor of the Board.

I cannot see that this bill in anyway is a radical step in what it does as to the power of the President to appoint a Governor. The President now, of course, can designate any member of the Board as Governor, and from time to time can change that designation. In the proposed bill, or in the bill of Governor Eccles that was passed by the House, the President is given the power to appoint from any Federal Reserve district a Governor, whether or not there is a member already serving from that district. That is the only change that I can see in that regard.

Then it is further provided that if the Governor should cease to be designated, he may resign free from the 2-year limitation on accepting any employment in a member bank.

Senator Glass. Is there a pressing emergency for that alteration in the law?

Mr. Hamlin. I do not think that there is any pressing emergency because, as I say, I consider that it is a very slight advance, if it is at all, over the present law. I think the provision as to qualifications of members of the Board should be looked over very carefully, and I assume that the Senate committee will take care of that. I think they are a little exclusive. But so far as the Governor goes, that matter could go along perfectly well. I do not regard that as one of the essentials at all of the problems now before us.

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Next, as to the appointment of a governor by the local board of directors. To my mind that is a grant of very great autonomy to the Federal Reserve banks. At the present time, as you know, the Federal Reserve Board has its chairman appointed by it at each Federal Reserve bank. He has an office there, and an office for the Federal Reserve Board. The chairman presides at all meetings, and we have two other directors to help him and to help the Board.

Under this proposed bill the chairman is absolutely withdrawn. One of the class C directors is withdrawn, and the governor may be appointed by the directors, and he is given supreme executive authority over the bank. I think that is a tremendous grant of autonomy to each Federal Reserve bank.

Some say that the fact that the Board under the law would reserve the right to confirm the appointment of governor would make that governor, as one man said to me, the office boy of the Board. I cannot see that at all. I do not care whether you confirm once for all or once every 2 or 3 years. I cannot see that that cuts down the power of the Federal Reserve bank in any sense. The fact that the President has to have many of his appointees confirmed by the Senate to my mind does not cut down or destroy his appointing power. Neither would it make the officer confirmed the office boy of the Senate. The Board has in a sense power nor over that matter, because it has the absolute power to fix salaries of every officer. In one case the Board refused to fix any salary of a governor—that was a good many years ago—because they felt that on the whole he did not measure up to the required standard.

But I cannot see anything radical there except a radicallly increased grant of power or autonomy to ever Federal Reserve bank.

Then there is the matter of the consolidation of the Rederal Reserve agent and the governor. That I think is vital in the sense of economy and simplicity. I think that if the Federal Reserve agent is abolished and the collateral for Federal Reserve notes done away with, it would save the System about $500,000 a year. But that of course is not a grave emergency, although I think on the whole it would be a very advisable step.

Senator Townsend. In what way would that saving be brought about?

Mr. Hamlin. If the policy of collateral for Federal Reserve notes were abolished, you would abolish a tremendous amount of work, and of course save the salaries now paid to Federal Reserve agents; and I think it is estimated that the whole thing would be a saving of somewhere near half a million dollars. If you desire that exactly I can give it to you in extenso.

Senator Townsend. You might furnish it for the record.

Mr. Hamlin. The question comes up with regard to the open market powers. As I said at the beginning, without open market power the Federal Reserve System is practically an emergency system. It has to sit still until banks come to it. Through the exercise of the open market powers it can go to the banks and can make its discount rates effective. What do you mean by making the discount rates effective? If you feel the discount rate is too low and you put it up, it does not follow that the banks will impose any higher rates upon their individual customers or in this case will raise the rates to the individual customers. You go into the open market and

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sell bonds. You take out the money from the reserves of the member banks, and it tends to make them cautious and it tends to make them raise the rates to their individual customers. On the other hand, if you wish to lower rates, you do it because you wish to see the benefit of that reduction percolate through the country so that the borrower of the bank can get his money at a lower rate.

Senator GLASS. Did you ever know it to so percolate?

Mr. HAMLIN. I think, Senator, it does; yes.

Senator GLASS. I have never known it.

Mr. HAMLIN. We have no uniform discount rate, but I think it does percolate through the country.

Senator GLASS. I have been observing it for 21 years and I have never known it to percolate.

Mr. HAMLIN. Well, that is the theory.

It is an interesting fact that under the original Federal Reserve Act our counsel advised us that the Board had power to order the banks to buy or sell securities. As a matter of fact, we never exercised or tried to exercise that power, but went along and got together between the banks and the Federal Reserve Board and we got along very successfully as a whole. Then came the Banking Act of 1933 which specifically gave the right to each Federal Reserve bank, through its directors, to decline to participate. As a sovereign board it has to enter into treaties with 12 other sovereign bodies, and although most of the time we were able to get together harmoniously, yet from time to time there did occur clashes where the policies of the System were sadly interfered with.

Senator GLASS. Do you think a central board here would know better than a regional bank what its local conditions are and whether or not it should be compelled to participate in an open market transaction?

Mr. HAMLIN. I think that if there is not some power, that is, a right to determine that question, it would be very difficult to agree on the carrying out of any major policy.

Senator GLASS. You have said that your counsel advised you that you have had that power all along.

Mr. HAMLIN. Yes; but of course that depended on a somewhat involved construction of the act, and as a matter of fact we did not exercise it.

Senator GLASS. I should think it would be a very much involved construction of the act.

Senator BULKLEY. What are the instances where the Federal Reserve banks refused to cooperate in the policy of the Board?

Mr. HAMLIN. There are two instances that I wanted to point out to the committee. The first was in August 1931 when conditions, as you all remember, were very bad. Prices were dropping; liquidating was going on, and the Board made up its mind, and in a conference the Federal Reserve Bank of New York concurred that a major policy was absolutely necessary, and the open market committee were called together. Governor Meyer, who was then Governor, went before the committee for 2 hours explaining that under existing conditions nothing but a major stroke would help this situation, and perhaps that would not; but that it was vitally important that the System should make a bold stroke and buy, say, 300 millions or 400 millions of Government securities, hoping that that might turn the

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tide. For 2 hours he discussed the matter with the governors. We then came together in a conference and we found, after their meeting by themselves, that a motion to amend that power which had been asked for by the Governor of the Federal Reserve Bank of New York, cut down the power from $300,000,000 to $120,000,000. The 20 millions was an unexpended balance. Practically the vote was 300 millions cut down to 100 millions, which naturally would destroy the effect because it would cease to be a major operation.

Senator GLASS. Did not the subsequent purchase of two and one-half billions of Federal Reserve securities demonstrate the utter futility of the policy which you proposed to adopt?

Mr. HAMLIN. I am not sure of that, Senator. A bold stroke of that kind, involving three or four hundred millions of dollars, one day, might have had a great deal of cumulative benefit. No one can tell. But the policy of the Board was to build up the reserves of the member banks by these bold strokes. No one can say now whether that policy, if it had been increased intensely, would have accomplished anything or not.

Senator GLASS. It was increased in intensity to the extent of two and a half billion dollars.

Mr. HAMLIN. But I am perfectly satisfied that the purchases that were made of Government securities helped to stop the precipitate deflation that was going on, but, of course, it cannot be measured.

Senator GLASS. The idea was that it would enable the member banks to pay their indebtedness to the Federal Reserve banks, and that thereupon the member banks would proceed to liberalize their own loaning policies. Did they do it, or did they keep on intensely providing liquidity?

Mr. HAMLIN. We kept on intensely helping them to do it, and that help is there now.

Senator GLASS. Your purpose was, as I understood it at the time, as I have said, to enable the member banks to pay their indebtedness to the Federal Reserve banks, the supposition being that thereupon the member banks would proceed to loan, and to loan, and to loan, in a very much more liberal measure than had theretofore prevailed. But, as a matter of fact they did not do anything of the kind, and they did not do it because public confidence had been badly impaired, and every member bank was intent upon being in as liquid a condition as it could be. Isn't that a fact?

Mr. HAMLIN. I think that is true in large measure, Senator. I know of no way that you can force a customer to go to a bank to borrow, but there are ways in which you can make it easy for a bank to make a loan.

Senator GLASS. You can make it easy for a customer to borrow when you reduce your discount rate to 1½ percent.

Mr. HAMLIN. Yes.

Senator GLASS. Which is perfectly ridiculous.

Mr. HAMLIN. That was the purpose of our purchase of Government securities, to help the general credit situation, that is to say, to give the borrowers of the country an opportunity to get money at lower, more favorable rates. The fact that that policy has not succeeded in that is something, of course, beyond the power of the Federal Reserve Board.

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Senator GLASS. I know; but that takes us back to the immortal declaration that we should take our steps in the light of experience. Was it Mr. Jefferson, or somebody of that type, now out of date, who said that?

Mr. HAMLIN. We certainly have had the experience, and we are still having it.

There is one point I want to make, that I trust the Senate committee will not advocate cutting down the members of the Federal Reserve Board to five. I think that is one of the propositions which has been laid before it. I believe that the appointive members should rather be increased to 7, because with the new autonomy given to the Federal Reserve banks, the members of the Board have got to increase their visits to those banks and keep in closer touch with them, and that will take up so much time that I should prefer to see it increased to 7 rather than reduced to 5. My point is that somebody should be given absolute authority to determine this matter of open-market policy. Governor Eccles has submitted a way of doing that with five governors bound to render an opinion to the Board before the Board makes any major change. I think that would work out very satisfactorily.

Senator BULKLEY. Before we get too far away, I want to get a better understanding of that difference of opinion that you just related between the Board and the banks. What was the result? Was the operation restricted at that time to $100,000,000?

Mr. HAMLIN. Yes.

Senator BULKLEY. When were further purchases resumed after that?

Mr. HAMLIN. Very shortly after that; but this was a major operation. It was voted down 11 to 1 by the Board of Governors, and at that time, while we had been told we had power, we had rather gone along in a spirit of cooperation, and usually that was perfectly successful. There was another instance. I think it was in——

Senator BULKLEY. Right there, you accepted the view that you did not have the right to compel them to make those purchases?

Mr. HAMLIN. We acted under that view, that it was a very doubtful question.

Senator BULKLEY. How was the matter next revived after that?

Mr. HAMLIN. Then, of course, the banking bill of 1933——

Senator BULKLEY. Before that, there were some considerable purchases, were there not?

Mr. HAMLIN. Oh, yes.

Senator BULKLEY. How did that come about?

Mr. HAMLIN. It came about by voluntary cooperation.

Senator BULKLEY. At the suggestion of the Board?

Mr. HAMLIN. We have our regular open-market meetings, and we make suggestions, and the Governors make suggestions. They come together, and they let us know what they think the policy should be, and the Board, of course, has the power to disapprove it, but in most cases we have got together very satisfactorily.

Senator BULKLEY. The Board simply acquiesced in that $100,000,000 limitation at that time, and then revived the subject a little later.

Mr. HAMLIN. Yes. It was the best we could do at that time.

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Senator BULKLEY. What did you do next?

Mr. HAMLIN. The next clash, I should say, was in 1933, after——

Senator BULKLEY. But how did you revive the question of getting more bonds purchased by the System?

Mr. HAMLIN. We got together, and we bought from time to time.

Senator BULKLEY. You say "we bought." You mean the Federal Reserve banks?

Mr. HAMLIN. The Federal Reserve System bought from time to time, as the result of a cooperative movement between the Governors and the Board.

Senator BULKLEY. When did you get past that $100,000,000 operation, and go into a larger scale of buying?

Mr. HAMLIN. I should say very shortly. I think it was in February. We began and went right ahead. I merely cite that as one case where there was a conflict of authority, to show the necessity of having somebody with final authority.

In 1933 the matter came up again. I think it was in the fall of 1933. I attended a meeting at the Federal Reserve Bank of New York of the executive committee. Governor Harrison reported that the Federal Reserve Banks of Boston and Chicago had passed resolutions absolutely declining to participate in any further open-market purchases unless in cases of grave emergencies, and the Governor at that time was very much worked up. He felt that we should go ahead strongly and vigorously, and pointed out that if New York did it alone—and New York, I think, was somewhat inclined to do it—it would pull its reserve ratio down to 47 percent, leaving the reserve ratio of Chicago and Boston at 70 percent. The Governor delivered an oration worthy of Demosthenes. He nearly drew tears to my eyes, when he told us it was the duty of the Board to force Boston and Chicago into line. I agreed with him entirely. I said, "I don't know how we can do it, but I will go back and see what can be done."

Then he made a very interesting suggestion, that the Board might be able to do that if New York were to take practically this whole issue—the Board could require Boston and Chicago to rediscount for New York, and thus equalize on the reserve ratio. But I merely cite that as an instance of the desirability of having somebody who can absolutely finally determine this question.

Senator GLASS. Does not the existing law authorize the Board to make rules and regulations for open-market transactions?

Mr. HAMLIN. Yes.

Senator GLASS. And is not the sole reservation that reservation that authorizes a Federal Reserve bank, upon written notice, to decline to participate in an open-market operation?

Mr. HAMLIN. Yes; and the question arises whether, under the power to regulate, we could issue an order to the banks to make open-market purchases.

Senator GLASS. I do not think you can. That is not regulation. Let me ask you this, Mr. Hamlin, before you leave that topic of increasing the appointive members of the Board. Would you drop the ex-officio members from the Board?

Mr. HAMLIN. In my opinion, I should like at least to see the Secretary of the Treasury retained as a member of the Board. Of course, Mr. Owen Young has given sufficient reasons for that, I think, for the

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next 2 or 3 years, but beyond that the Secretary of the Treasury, under the Federal Reserve Act, has absolute, supreme power over the Federal Reserve banks as fiscal agents, and he is a large depositor, and it seems to be very desirable to have some link between a board, we will assume, to be made absolutely independent, and the fiscal branch of the administration.

Senator GLASS. That is a pretty broad assumption, is it not?

Mr. HAMLIN. That is a pretty broad assumption, but I have always had that feeling. I think the Secretary of the Treasury should come to our Board and tell us exactly what his policies are, and we should exchange views with him and know precisely what he is doing, and I think the best way to bring that about is to have him remain a member of the Board.

Senator TOWNSEND. Does the Secretary of the Treasury do that now?

Mr. HAMLIN. Oh, yes. He consults with the Board.

Senator TOWNSEND. And outlines his policies?

Mr. HAMLIN. And tells us, in a general way, his policies.

Senator GLASS. How many meetings has the present secretary attended?

Mr. HAMLIN. I should say three or four, but he has been ready at any time the Board has asked him, to answer any questions that he could. He has always been ready and eager to come before the Board, and I have found him very frank and square in all his relations with the Board.

Senator GLASS. What have you to say of the suggestion by Doctor Miller that the Federal Reserve Board should be made a board of governors of the Federal Reserve System, with authority to select their own chairman and chief executive officers?

Mr. HAMLIN. I think that is a solution that will make the Board certainly independent in law. I shall try to show in a moment that they have been independent in fact. I think that would undoubtedly satisfy the people that the Board is independent in law as well as in fact. There is no personal feeling about this. I could say, if that were the law, that I should take pleasure, as the first Governor appointed by the President, in nominating Governor Eccles as the first chairman of the Board. But I think that probably would satisfy the people that we have an independent Board in law as well as in fact.

Senator GLASS. What people would it satisfy?

Mr. HAMLIN. I think the people of the United States.

Senator GLASS. I do not agree with you.

Mr. HAMLIN. There is another reason why I think that the present is the time for bringing about some amendments in this law, and that is broadening the eligibility features of the law. We have had complaints and protests and earnest requests from all over the country that some types of what you call finance paper should be made eligible. I have always felt that under the original Federal Reserve Act it would be possible to construe the act so as to admit certain types of finance paper, but the Board never has been able to agree on that proposition. It came up first with cotton factors' paper, and for years that matter was before us. The cotton factor borrows from the bank, and gives his note. The bank pays him the money, and he devotes every dollar of that money to the business of raising and producing cotton, and yet his note cannot be presented to a Federal Reserve bank for rediscount.

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Senator GLASS. You mean under the decision of the Board it cannot be?

Mr. HAMLIN. Yes. In 1923 we appealed to Congress, and Congress changed the law, and made cotton factors' paper eligible. It seems to me that same principle could be well extended to other forms of paper. Take installment paper, which has turned out to be, I think very good, sound paper. The individual purchasers could give their notes to a bank. That would be eligible, but the practice is, to save trouble, to go to a finance company, and the finance company gives them the money and gives its note to the bank with these other notes as collateral, and the bank cannot rediscount that with the Federal Reserve Bank. It seems to me, on the principle of cotton factors' paper, which we must take now, as a broadening of the scope of the Federal Reserve Act, much of that paper could be made eligible.

Senator GLASS. What is excluded from your definition of eligible paper? You are given complete power to define the eligibility of paper within the law. What is excluded from your definition of eligible paper, except investment securities and notes executed for purchasing and carrying speculative stocks?

Mr. HAMLIN. Well, we have had to define that as broadly as we could, but we have had to rule, in a great many cases, against the eligibility of paper.

Senator GLASS. You mean you have ruled?

Mr. HAMLIN. We have ruled, and I think now it is perfectly safe to give the Board the power to broaden slightly the eligibility features of the law, founding that opinion on the cotton factors' decision, which Congress finally settled.

Senator GLASS. And to make it without limitation, as this bill does, and not to apply to the commerce and industry and the agricultural interests of the country?

Mr. HAMLIN. Any limitation, of course, which Congress saw fit to place upon that power would be reasonable. I am not arguing as to that, but the power, perhaps subject to reasonable limitations, should be given to this Board, which I assume, now, is an independent Board.

Senator BULKLEY. Do you favor any limitation other than sound assets?

Mr. HAMLIN. No. The Federal Reserve Board years ago asked Congress—I can almost say begged Congress—to give it the power to buy the sound assets of any bank in trouble. This bill would simply permit a loan on the sound assets. Fifteen years ago we were willing to take the risk of buying the sound assets to help the bank. I believe that that is a proper provision in this proposed bill. You could put in any limitation on it that you deemed advisable, but the subject-matter, I think, is sound and reasonable.

Senator COUZENS. Under what construction of the law did you decline to take this so-called "finance paper"—the installment paper you refer to?

Mr. HAMLIN. On the ground that the proceeds of the note were not directly used for agricultural or commercial purposes. That is, the note was discounted at the bank, and the bank gave the money, in this case to the cotton factor, and he loaned it to the producer. The producers could have given their notes direct to the bank. That would have been proper agricultural paper, but because it was first

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given to a cotton factor to be loaned by him, we were obliged to rule that that was ineligible.

Senator GLASS. In other words, the cotton factor was to make a profit out of the transaction instead of the bank.

Mr. HAMLIN. In a certain way. He acted as the agent for all these people who needed help, and the fact that he took the money and loaned it to them made that piece of paper ineligible. But, as I have said, Congress has changed that, and that is now eligible paper, and on that principle I think the Board should be permitted to go further.

Senator COUZENS. When you decline to accept and rediscount the paper for the financing of radios, automobiles, and refrigerators, under what law do you refuse those rediscounts? Are they not to help agriculture, industry, and commerce?

Mr. HAMLIN. These are all, I suppose, related to finance companies, who do the financing for the installment purchasers.

Senator COUZENS. Yes.

Mr. HAMLIN. We do it on the theory that when a bank discounts the note of a finance company, they give the money directly to the finance company. It is the finance company that then distributes it for agricultural purposes, and we found, under the law, that we could not hold that that was eligible paper.

Senator COUZENS. What part of the law? That is what I am trying to get at. What part of the law prohibited you from rediscounting this paper, which was in aid of commerce?

Mr. HAMLIN. I would have to ask our counsel to explain that, Senator.

Senator COUZENS. Certainly I cannot understand it. I am not urging it, but I just do not understand how you reached the decision.

Mr. HAMLIN. The original law provided for notes the proceeds of which have been or are to be used for agricultural purposes, as in this case. I have always thought that was broad enough to cover this finance paper, but it is a question of very grave doubt, and that is the reason we went to Congress as to cotton factors' paper, and I think that is the reason this bill would give that power to the Board, which I thought it always had, but I believe it is a very doubtful question.

Senator GLASS. Was not the opinion of your counsel based upon the fact that the finance company was doing a banking business within itself, and was not a member of the Federal Reserve System or subject to the restrictions or the privileges of the Federal Reserve System?

Mr. HAMLIN. The finance company was just like any farmer or anyone else borrowing from a bank. The Board held that he was borrowing in order to relend.

Senator GLASS. Did he not constitute a bank without the system?

Mr. HAMLIN. That is possible, but Congress said, in the case of the cotton factor, no; and his paper was made eligible.

Senator GLASS. Congress said that very definitely, and if you want it to be definite in the statute, that is one thing. But if you want it to be unqualified, without limit, that is another thing.

Mr. HAMLIN. Any limitation that Congress saw fit to place upon it would be perfectly reasonable.

With respect to this power to order purchases or sales in the open market, as I have said, I think the authority ought to be put somewhere. The suggestion in the House bill, that a board of five gover-

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nors be required to give an opinion before the board exercises that power, I think probably could work out very satisfactorily. But the power must be vested somewhere, and, as I have said, I earnestly hope that it will be vested in the Federal Reserve Board, with the duty of calling for a formal opinion from all the governors, or from five of the governors. It Congress sees fit to impose some limitation on that, that before the Board departs from the official opinion of the governors it must have, we will say, an affirmative vote of five, that would be reasonable. I think that is the law now, where we force one bank to rediscount for another.

Next, as to the proviso as to the initiation of rates. A great many opponents of this bill seem to think that for the first time this bill gives the Board power to initiate rates. The fact is that this bill somewhat restricts the power. It says that before the Board can use that power of initiation it must get the opinion from five of the governors. The power to initiate rates is not an original power for the first time given to the Board in this bill. The power to initiate rates, as the Attorney General has advised us, is in the original Federal Reserve Act.

Senator GLASS. What Attorney General?

Mr. HAMLIN. The Acting Attorney General, but he was acting as Attorney General. It was the Attorney General's Department.

Senator GLASS. I am glad he found something in the bill that I never discovered, and the Board never discovered it either. It attempted it once.

Mr. HAMLIN. It did it twice, Senator. In 1920 the Federal Reserve Board initiated a rate of 6 percent at the Federal Reserve Bank in New York, raising the rate, I think, from 4½ to 6 percent on commercial paper, and the New York directors declined to put in that 6-percent rate. The Board all agreed that there should be an advance in rates, but many of the Board felt that a jump from 4½ to 6 was rather sudden and extreme. The matter finally came up before the Board, and was lost on a tie vote, whereupon the chairman was asked to vote, and the chairman voted aye, and that initiated the rate of 6 percent in the Federal Reserve Bank of New York. The directors pointed out that if we wished that rate we could only get it by initiating it, and initiate it we did.

Senator BULKLEY. What was the date of that?

Mr. HAMLIN. That was 1920. I think it was March. I can get that exact date for you.

Senator BULKLEY. That is sufficient.

Mr. HAMLIN. Then in 1927, a lower rate was initiated in the Federal Reserve Bank of Chicago. To my mind the power to initiate rates is absolutely vital to the Federal Reserve System, never to be exercised except in some extraordinary condition, and I think I can speak without any prejudice, because in both the cases where rates were initiated I voted against initiating, not on the ground of lack of power, but on the ground that there was no good reason shown for lowering the rate in Chicago, and I believed that it was rather extreme to raise the rate in New York. But I think that is a vital power which should be given to the Board, or which should be retained in the Board, assuming that the opinion of the Attorney General's Department is correct.

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Senator GLASS. You look at your wonderful diary and see if you did not vote against it because you did not think you had the power.

Mr. HAMLIN. No; I have gone through that diary very carefully, and I took the opinion of the Attorney General of the United States, or his office, as binding on the Board, and I voted for the reason that I thought it was too excessive an increase.

Senator GLASS. An opinion of the Attorney General is not binding on the Board.

Mr. HAMLIN. It is binding on the Secretary of the Treasury.

Senator GLASS. It is not binding on any department of the Government. It is merely advisory.

Mr. HAMLIN. I may be wrong. I accept your criticism, but I have always supposed that the opinion of the Attorney General was binding on every executive department, and when the Secretary of the Treasury asks an opinion of the Attorney General, I assume that he is bound by that opinion. I may be wrong. It is merely the assumption that I carry in my mind. I feel that it might be well to have the same limitation—an affirmative vote of five—before you initiate a rate, for example. There would be no objection that I could see to that at all.

There is one other question, the question of Federal Reserve notes, which the proposed bill would authorize without collateral. I regard that as not very vital at the present time, because today the Federal Reserve notes can be issued, and just as many notes can be issued with the collateral of Government bonds as could be issued under the Eccles bill without any collateral at all.

Senator BYRNES. Who was Secretary of the Treasury at the time that opinion was asked of the Attorney General? Was it Secretary McAdoo?

Mr. HAMLIN. Who was Secretary of the Treasury at the time of the Attorney General's opinion?

Senator BYRNES. Yes.

Mr. HAMLIN. I think the Honorable Carter Glass was Secretary of the Treasury.

Senator GLASS. When what?

Mr. HAMLIN. When the Attorney General's Department rendered that opinion.

Senator GLASS. What opinion?

Mr. HAMLIN. As to the power to initiate discount rates. That is what I thought the question was.

Senator GLASS. I always opposed the proposition, whether the Attorney General rendered an opinion or not. I do not recall ever having asked the Attorney General for any such opinion. I do recall that I was very definitely told that the Board was so ashamed of its attempt to usurp that power with the Chicago bank that it eliminated the fact from its record.

Mr. HAMLIN. I heard that the other day, and I had the most careful examination of the records made, and I can say that not one paragraph has been eliminated of that whole discussion.

Senator GLASS. I will not enter into that further than to say that a member of the Board, and one of the original members of the Board, certainly told me that. I did not dream it.

Mr. HAMLIN. I heard it the other day, and asked to have it checked up, and the report was that there was nothing eliminated.

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On the subject of Federal Reserve notes, of course, this proposed bill would make those notes practically an asset currency. I can remember very well the old Baltimore plan for an asset currency, and that was considered as sound currency, with the proper reserve, and, of course, a first lien on the assets. But the point I wish to make is that this bill, so far as that is concerned, is no radical departure, because for 2 years, at least, we can issue as many Federal Reserve notes with Government bonds as collateral, as could be issued without any collateral at all, because there is the upper limit of two and a half times the free gold. So that no one could fairly claim that the purpose of that is to increase the issue of Federal Reserve notes. They are always bound by the reserve requirement, two and a half times the free gold, which could be used as a reserve against the notes.

Senator BULKLEY. And the reserve requirement may be freely changed at any time.

Mr. HAMLIN. The reserve requirement under the original Federal Reserve Act——

Senator BULKLEY. I mean under this proposed bill.

Mr. HAMLIN. No; I do not understand that there is any change in the existing law. You can reduce the reserve requirement under existing law for Federal Reserve notes, but that was the law under the original Federal Reserve Act. There is no more danger of that now than there would be under the original law. But for 2 years——

Senator GLASS. You can only reduce the reserve requirement under penalty.

Mr. HAMLIN. Certainly, under penalty. But for 2 years, with the privilege of having Government bonds as collateral, just as many notes can be issued as under the House bill, without any collateral whatsoever. I think it is hardly likely that at the end of 2 years, even, we will do away with the privilege——

Senator BULKLEY. I am interested in that, because it does not seem to me that there was any limit at all to the amount of notes that could be issued under the bill as it passed the House.

Mr. HAMLIN. The limit is 40 percent. There must be 40 percent gold reserve.

Senator BULKLEY. Unless the Board sees fit to change it.

Mr. HAMLIN. The Board, under existing law, could lower those reserve requirements for periods of 15 days, imposing a heavy tax on the Federal Reserve notes.

Senator BULKLEY. Under the bill as it passed the House, what can they do?

Mr. HAMLIN. Just the same, I do not understand that that reserve clause is changed in any way.

Senator BULKLEY. They have changed it so that the Board can do anything it pleases at any time, without any penalty.

Mr. HAMLIN. If that is so, that ought to be covered. The Board can now make a change in the reserve requirements.

Senator BULKLEY. For a limited time, and under penalty.

Mr. HAMLIN. Yes.

Senator GLASS. That has been the law from the first.

Mr. HAMLIN. That has been the law from the first.

Senator BULKLEY. You do not think it would be material to remove those limits?

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Mr. HAMLIN. No; I think that limit should be kept just as it is—a fixed reserve. Of course, as I have said, that would make the Federal Reserve note an asset currency. I believe that is ultimately a wise step, but, of course, that is not any grave emergency. I remember perfectly well, under the Aldrich monetary bill, for forming a central bank, the notes could be issued on the collateral of Government bonds, which, of course, now, for 2 years, is the law. Ultimately I should hope to see that removed, and to see those notes a pure asset currency, with the proper gold reserve, and make them a first lien on all the assets of the bank.

Senator BULKLEY. So that the only change you would suggest in the House bill is that you do not believe in removing all restrictions on the maintenance of a reserve against the notes.

Mr. HAMLIN. Oh, yes. I do not remember the exact wording of the House bill, but I should say the present law ought to remain, as to lowering the reserve requirement. There is no change in the proposed law on the reserve requirements, I am informed. I did not know of any change until you spoke.

Senator BULKLEY. I would like to put in the record what it says, if I can find it.

Senator GLASS. Is there any other provision you want to discuss, Mr. Hamlin?

Mr. HAMLIN. There was just one point I wanted to refer to briefly. The Board has been very severely criticised because, as I have said, it has shown a lack of independence, and the principal fact cited to prove that lack of independence was its attitude in objecting to the increased rate in 1929, which the Federal Reserve Bank of New York advocated, and which the Board 10 times refused to approve. The Board is criticised for lack of independence. As a matter of fact, I think that is an instance of independence rarely equalled in the history of any board in the United States. A majority of the Federal Reserve Board put through that policy against the votes of the Secretary of the Treasury, the Governor of the Board, and the vice-governor of the Board, and, whether the policy was correct or incorrect, I think it was certainly a sign of virile independence. The real gist of the criticism apparently is that the Board refused to be dominated by the administration, and had the courage to stand up for what it believed to be correct. That question was a very simple one. The public thought the controversy was between the Board and New York; that New York wanted to increase the rate from 5 to 6 percent, and the Board 10 times refused. That is partially the truth, but not the whole truth. What the Federal Reserve banks of New York desired was to have the Board accept a policy of affimative increase of rates, beginning at 6 percent, and going up to 7, 8, 9, or 10, until the situation was corrected. I remember 3 years ago you asked me what that meant, and I said I supposed it meant until the speculation on the New York Stock Exchange was at an end. The Board took this position: "It is not our duty to go in and regulate the New York Stock Exchange. Our duty is complied with when we take Federal Reserve credit that has seeped into the exchange out, and that duty we propose to perform." We said the existing rate of 5 percent on agricultural and comercial paper was certainly not too low a rate. Many thought it should be lower, that it should be 4½ percent, but we

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were asked, because of speculation in New York, to enter on a campaign of higher rates for agriculture and business, men whose lives depended on short-term credit, beginning at 6 percent and going up to 7, 8, 9, or 10. To my mind it was like asking a father to cut the ears off his child because a drunken man was carousing in the street.

Senator GLASS. Is not that exactly what we are asked to do now, order to prevent a repetition of that?

Mr. HAMLIN. No; I do not so understand at all. We are asked to put up the reserve requirements, but we are given power now to take an individual bank under the Banking Act of 1933. We can fix the percentage, but I feel that it would be a great help to us——

Senator GLASS. But the proposition is to repeal all that.

Mr. HAMLIN. Not to repeal the Banking Act of 1933. I hope not.

Senator GLASS. Those two sections.

Mr. HAMLIN. I hope not. I think they are most valuable features.

In that connection, a great many men have said that it is not now expedient to make these changes. That reminds me of the gentleman whose roof was leaking, and he did not want to repair it while it was raining, but when the rain was over there was no necessity of repairing the roof.

I have read Mr. Owen Young's testimony. I have the very highest esteem for him in every way. I have known him many years before this act was formed, but I think he is a little nervous and scared about what may happen from bringing about these changes. Three years ago, Senator, you will remember that Mr. Young and Governor Harrison signed a memorandum to you, giving—to them—conclusive reasons why there should be no legislation at all in the year 1933. Those same reasons would almost apply today. I think bankers necessarily are easily moved and scared. They do not want any change.

Senator GLASS. On the contrary, Mr. Harrison came down here, and over and over and over again, urged our subcommittee to legislate.

Mr. HAMLIN. You mean this subcommittee?

Senator GLASS. Yes. This subcommittee has existed, except for the three members who were recently added, under the administration of Senator Norbeck as chairman, as well as under Senator Fletcher. We were urged to take legislation, and did take legislation, and have practically turned the country back to a bond-security country.

Mr. HAMLIN. Was this with relation to the act of 1933?

Senator COUZENS. Yes.

Mr. HAMLIN. There is a memorandum filed with this committee, signed by Governor Harrison and Mr. Young. I think it was before the act of 1933, and in relation to that act.

Senator GLASS. Perhaps that related to certain powers that the Federal Reserve banks generally did not want vested in the Federal Reserve Board.

Mr. HAMLIN. It covered the whole bill. It said that there were some good things in it.

Senator GLASS. What whole bill?

Mr. HAMLIN. The bill which subsequently became the Banking Act of 1933. It covered that whole bill, in the shape in which it then was.

Senator GLASS. For that matter, the Governor of the Federal Reserve Board appeared before our committee and opposed the whole bill.

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Mr. HAMLIN. Opposed the whole bill?

Senator GLASS. Yes.

Mr. HAMLIN. My recollection is that the Governor of the Federal Reserve Board appeared before this committee and spoke for a unanimous opinion of that Board in favor of the bill as it then was.

Senator GLASS. I do not recall that at all.

Mr. HAMLIN. I think that is a fact, Senator. The Board had a long discussion——

Senator GLASS. You have a diary, and unfortunately I have not. You may be correct, but my recollection is that Mr. Meyer appeared before the subcommittee and opposed many provisions of the bill, and filed with us, as I recall, a very elaborate opinion of your counsel, Mr. Wyatt, who is here now, pointing out just exactly how we might have a unified banking system in this country, putting under the Federal Reserve Board control of all banks of deposit.

Mr. HAMLIN. I think that was another occasion. My memory is absolutely clear that the Governor of the Federal Reserve Board and the members went to a session of this committee, and the Governor read a unanimous report. We made some minor criticism of the bill. Of course, that is a matter of record, and I will endeavor to make that perfectly clear. Then, you will remember, Senator, that all the governors of the Federal Reserve banks were on record as opposing the bill in 1933, even taking the amendments the Board had suggested, many of which were accepted by the committee. I am not criticizing them. I am simply saying that it is the natural state of mind to hesitate to have any new change.

As I have said, I am confident that this Board is a virile, independent board, in fact. I assume, from what Secretary Morgenthau and Dr. Miller said, that the question will be before you of making it an absolutely independent board in law. On that assumption, after a thorough examination of this bill, with many minor reservations, of course, that are not very material. I am prepared to say that I support this bill, and I believe it would be for the greatest good of the people of the United States to have these questions settled now, and, incidentally, that it will be of great help to the bankers themselves.

That is all that I think of.

Senator GLASS. We are very much obliged to you, Governor.

Senator BULKLEY. Senator Glass, permit me to say that after having reread the House bill I want to confess my error concerning proposed changes in reserve requirements. The authority given the Federal Reserve Board to change reserve requirements relates only to reserves of member banks, and the requirement of 40 percent reserve over gold certificates behind circulating notes is absolutely fixed.

Senator GLASS. Very well, Senator Bulkley.

The committee will recess until 2 o'clock, when it will convene in the Appropriations Committee room of the Senate. At that time other members of the Federal Reserve Board will be heard.

(Whereupon, at 12:15 p. m., a recess was taken until 2 p. m.)

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AFTERNOON SESSION

The subcommittee resumed its session, at the expiration of the recess, at 2 p. m., in the hearing room of the Senate Committee on Appropriations, in the United States Capitol.

Senator GLASS. I understand that there is a banker here from Texas who wants to be heard for a few moments.

Mr. WOODS. Yes, Mr. Chairman.

STATEMENT OF J. E. WOODS, PRESIDENT THE TEAGUE NATIONAL BANK, TEAGUE, TEX.

Senator GLASS. Please give your name and address for the record.

Mr. WOODS. My name is J. E. Woods; I am president of the Teague National Bank, Teague, Tex.

I am a small-town banker operating a national bank with $100,000 capital and surplus and average deposits of $600,000. While I have been delegated by the officers of the Texas Bankers Association to speak with authority for the member banks of the association, it shall be my endeavor to convey to you particularly the thoughts of the so-called "country bankers" and "small-town bankers" of our State concerning certain phases of the pending banking bill.

My remarks concerning the bill will be confined to subdivision 8 of section 101 of the House bill providing for a mandatory annual assessment of one-eighth of 1 percent of the deposit liabilities of member banks as a premium on the limited insurance of deposits by the Federal Deposit Insurance Corporation and to some observations concerning Postal Savings competition.

Regardless of the wide difference in opinion as to the feasibility and the wisdom of the undertaking prior to the enactment of the act providing for insurance of deposits, it is now a part of the law of the land and it is the earnest desire of all of us to lend our best efforts and give our full cooperation toward making the plan the success that it proponents cherished. Imbued with that spirit, our views are offered not in a spirit of criticism but to try to acquaint you with the views of the average banker who is in close contact with the people and who is fighting the economic battle in the front-line trenches. The matter is of vital importance to his welfare and, indirectly, to the welfare of the community served by his institution. It is sincerely hoped that with the expression of these views you may be assisted in a small way in your deliberations on this important proposition.

The wisdom of the plan providing for the payment of an annual premium for the purpose of creating and maintaining a fund to take care of current losses and to provide a reserve for future losses (such rate of premium to be arrived at on a proper actuarial basis) cannot be questioned; and the conservative thought that prompted the committee to fix the premium at an adequate rate is commendable, although we feel that in view of the present condition of the banking structure the rate of one-eighth of 1 percent fixed by the House bill is too high. The difficulty in arriving at a just and adequate rate on an actuarial basis is fully appreciated. That a rate based on losses on the insured deposits during the 16 months that the temporary insurance plan has been in operation, when the losses amounted to only a small part of the annual income from investments of the

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capital funds of the corporation, would be inadequate, is elementary. On the other hand, a rate based on losses during the 4 years ending June 30, 1934, during which 4 years' period two-thirds of the losses occurred during the 70 years' period ending on that date, would not be fair.

Indeed, we are in an experimental stage with insurance on bank deposits; no statistics are available that are accurate enough to be relied upon as a criteria for future performances. The amount of premium necessary to collect must of necessity result from study and experience. With the banks as a whole, thanks to the wise policies of the administration, beginning with the bank holiday in 1933, probably in the soundest condition that they have been in during our banking history, can we not safely assume that during the next biennium, at least, fatalities will not increase appreciably? According to figures released by the Federal Deposit Insurance Corporation, only 17 insured banks had failed as of May 15, 1935, resulting in an estimated loss to the Federal Deposit Insurance Corporatin of 2½ million dollars. For the next few years, at least it seems that losses could conservativly be expected to be less. It is admitted that by reason of the emergency, unsound banks were admitted to membership in the Insurance Corporation. In an address delivered recently, an officer of the Federal Deposit Insurance Corporation said [reading]:

> The urgent necessity of reopening the banks made it imperative that all banks which had a reasonable chance of continuing their business should be licensed. The examinations preliminary to such licensing were necessarily made with tremendous speed and under unusual conditions. It was natural that some banks were licensed which did not have adequate support really to warrant their continuance as banking institutions.

With the fine job that the Reconstruction Finance Corporation, the Federal Deposit Insurance Corporation, the Comptroller's Department, and the various State banking departments cooperating are doing and with the wise provisions of the pending bill that will force member banks to get their houses in order where necessary and exclude from membership unsound banks, does it not seem that fatalities in the next few years should not increase materially over the past year and one-half? Income to May 15, 1935, from investment of capital funds exceeded losses and expenses by approximately 2½ million dollars.

The Federal Deposit Insurance budget for the year 1935 provides for current expenses of 2½ million dollars against a present income of 8½ million dollars from investment of capital funds, leaving $6,000,000 net income that may be used for the payment of losses on insured deposits. For the past 2 years, and there is nothing at this time to indicate a favorable change in the near future, banks, particularly the country banks where the volume is small, are having difficulty in meeting operating expenses and taking care of losses that inevitably occur. In Texas, where it appears that the banks have withstood the depression better than the average, only a small percentage of the total number were able to pay dividends during the past year. Out of 469 State banks only 121 paid a dividend in 1934. We have not been able to get similar information as to national banks. It was very generally the case where the smaller or average-size banks were able to earn enough to permit paying a dividend such profits resulted

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from profits from the sale of securities the market value of which had appreciated and such earnings were nonrecurring.

At first glance, the proposed assessment, at even one-eighth of 1 percent, does not appear great as to the country banks, but with very limited income the additional load placed on the expense side of their operations in most cases will be more keenly felt by the small banks than by the large banks with greater incomes. In considering the shrinkage in income which the banks have suffered, I call attention to the loss of profit on circulation, which is in the process of retirement. The discontinuance of approximately $800,000,000 circulation will result in a loss of profit to the national banks of not less than $12,000,000 annually. To the little bank of which I am president, the loss will amount to $900 annually, or 1½ percent of the capital stock. This loss in income will be reflected by bank operations for the period beginning July 1, 1935.

In order to exist and perform their important functions in the community life, banks must earn enough to pay the stockholder a reasonable return on his investment. While protection of depositors' funds is always of prime importance in the operation of a bank, the interest of the stockholder who provides the capital structure of the bank must have next consideration. For the past several years ownership of bank stock has been a liability, and the stockholder has, indeed, played the role of the forgotten man in the banking industry. He deserves and, eventually, must receive consideration.

An assessment of one-eighth of 1 percent premium, as provided by the House bill, would yield annually on the basis of present deposits of insured banks approximately 47½ million dollars, while, as pointed out, losses from January 1, 1934, to May 15, 1935, in insured banks that have failed have amounted to only 2½ million dollars, and the net income from investment of capital funds on the present basis is estimated to yield $6,000,000 per year. I respectfully submit that the addition of this vast sum to the already heavy operating expenses of the banks would be a distinct shock to a great majority of the institutions, especially the so-called "country banks." It would be revolutionary in its nature. If as we go along it is found that such a charge will ultimately be required, it seems that it would be a more desirable plan to gradually increase the rate to the required figure than to apply the maximum assessment at a time when the banks are not in position to withstand the shock. It is earnestly urged that there would be no departure from conservatism in fixing a rate of one-sixteenth of 1 percent for the present.

Concerning the operation of the Postal Savings System, I wish that I might impress upon the members of your committee the serious inroad that postal savings competition is making upon the operation of the smaller city banks. The effect of this competition has been most damaging to banks in towns ranging in population from 2,000 to 5,000. It is not because these banks have compacently accepted this condition that relief from this menace has not been persistently urged upon the Congress, but it is because of the fact that during the past 2 years each session of Congress had had under consideration major banking bills, which the legislative committees of our associations have felt were of such vital importance to the banking industry or profession as a whole that they should concentrate their efforts on these major bills; and as the small-town banks are the ones that are

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bearing the brunt of this competition the matter of urging relief has been deferred pending settlement of the major measures.

It is my opinion, arrived at after careful study of the postal savings question, that the operation of the Postal Savings System has served to dry up credit in our erstwhile prosperous communities more than any other cause that possibly could be reached by legislation. The ideal functions of a bank are to provide facilities for impounding the earnings, savings, and the liquid wealth of the community and use it as the basis for legitimate credit which is used in the channels of trade and the building up of worthy enterprises in the community. Any enterprise or operation that drains this liquid wealth from the community that produced it will retard the development of and, if continued long enough, will wreck the community economically.

Senator BYRNES. It is your information that the postal savings deposits have increased during the last few years?

Mr. WOODS. Is it; yes, since the deposit insurance it has increased.

Senator BYRNES. The figures I saw within the last few weeks show no increase, or a very slight increase.

Mr. WOODS. Possibly the current figures; but over 1934 I understand they increased $10,000,000. I believe that is shown in the Postmaster General's report.

Senator COUZENS. What interest do they pay?

Mr. WOODS. Two percent.

Senator COUZENS. What are you paying?

Mr. WOODS. We pay 2 percent on savings accounts. The average country banker, before the postal savings competition became so great, had very few interest-bearing accounts.

Senator TOWNSEND. The competition of the postal savings bank forced the country bank to pay that interest?

Mr. WOODS. Yes. The country banks cannot benefit by this deposit insurance like the city banks can because we have to compete with the postal savings. The city banks can take our money that we used to get as interest on daily balances, and they do not have to pay it. They kind of break even and, in a way, offset their expenses.

This is just what is happening in the operation of the Postal Savings system. In many towns having good banks, deposits in postal savings almost equal the deposits in the banks and where this condition exists contraction of local credits and the resulting stagnation in business are apparent.

It was confidently hoped that when the insurance of deposits became a reality that the Congress would, at least, eliminate from the Postal Savings System all competitive features, if not repeal the act in its entirety. This hope was strengthened by statements made by our efficient Comptroller of the Currency, Hon. J. E. T. O'Connor, in an address delivered at the annual convention of the American Banker Association in Chicago in 1933 and on several occasions. In his Chicago address, Mr. O'Connor, in commenting upon the growth of the postal savings, said:

> When the insurance fund becomes operative most of this money will be returned to the banks and Congress will be justified in repealing the Postal Savings Act.

Contrary to Mr. O'Connor's prediction, postal savings deposits have increased rather than decreased; the total deposits at the close of 1934 being $1,207,200,000. While all but a negligible percentage of

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this total is in postal savings offices in towns where one or more insured banks are located, it might be argued that the existence of the System is necessary to provide a safe depository for funds where no insured banks are located. Granting that in a few cases that is true, can it be argued that it is necessary to penalize the whole banking industry of the Nation to accommodate the convenience of just a few? To the argument that might be advanced by some that we have not gone far enough with our experiment with insurance of deposits to insure its permanency and warrant the repeal of the Postal Savings Act, we of the smaller banking cities who are suffering from what we honestly feel is an unjust and unwarranted Government competition, suggest that for the present instead of repealing the Postal Savings Act the law be so amended that the payment of interest on deposits be discontinued. In the alternative, if it is deemed the best policy to check and gradually eliminate the operation of the System, reduce the interest paid on postal savings deposits one-half and that to be paid on strictly time deposits. It is suggested that provision be made for reduction of interest from 2 percent to not over 1 percent on time deposits and prohibit the payment of certificates of deposit before maturity as the law now applies to time deposits in banks. The present rate of 2 percent was fixed when the act was passed in 1910 at a time when banks paid 4 percent and more on open deposits and although changed conditions have reduced interest rates until member banks of the Federal Reserve System are now prohibited by law from paying any interest on demand deposits, the interest on postal savings deposits has not been changed.

As an excuse for continuing the Postal Savings System, the argument has been advanced that the System is used largely by our citizens of foreign extraction who could not be trained to use our banking system. A close observation and study of the operation of the System in Texas reveals that the postal savings is patronized less in centers thickly populated by citizens of foreign extraction than in places where the foreign population is negligible. The argument also is sometimes advanced that the total is made up of very small savings accounts, too small for the banks to handle and which remain on deposit from year to year. While the average deposit in postal savings per depositor is about $500, an investigation will reveal that a big percentage of the total amount is composed of deposits of from $1,000 to $2,500 per person; and as evidence of the activity of the accounts, it is noted that deposits during the fiscal year ending June 30, 1934, amounted to $966,000,000 and withdrawals amounted to $955,000,000. It has also been suggested by some who seem to favor the continuance of postal savings that postal savings depositors are only small depositors that commercial banks do not want and on which accounts the banks make a service charge. That argument is not correct as banks generally accept savings accounts no matter how small and charge only on the small active accounts that are expensive to handle.

In appealing to you gentlemen, who have given the matter of banking and its relation to the welfare of our people so much of your time and consideration, to give us relief from this unwarranted competition, I am sure that I express the sentiment of every banker in the country who has felt the damaging effects of its operation.

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In conclusion, I desire to present and file with you a copy of a resolution unanimously passed by the Texas Bankers Association at its annual State convention in Galveston on May 23, 1935, memorializing Congress to fix the premuim to be paid by banks at one-sixteenth of 1 percent and setting out the reasons therefor.

(The resolution referred to and submitted by the witness is here printed in full as follows:)

RESOLUTION

Whereas there is now pending in Congress House bill no. 7617, better known as the "Banking Act of 1935", which under title 1, Federal Deposit Insurance, provides for the fixing of a permanent assessment rate of one-eighth of 1 percent per annum, to be levied annually upon the average total amount of deposit liabilities of banks for the purpose of creating a reserve with the Federal Deposit Insurance Corporation in the insurance of deposits as provided for in the bill; and

Whereas we are not unmindful of the necessity of putting the Federal Deposit Insurance Corporation on a functioning basis by fixing a rate that would yield a sufficient amount to give ample protection under the insured liability, we can see no reason for taxing the banks for the purpose of creating unnecessary excess funds in the Treasury of the Federal Deposit Insurance Corporation, especially since the corporation at the present time has assets of approximately $350,000,000, and has the power to issue debentures in a substantial amount in time of emergency; and

Whereas the House Banking and Currency Committee in fixing the rate seems to be unaware of the fact that the banks of the country as a whole during the past few years have had practically no earnings, and that over a long period of years the average earnings of banks as a whole have been less than 1 percent on total deposit liabilities; and

Whereas in considering this matter, it is evident that after the serious crisis through which the banks have passed involving heavy losses which have not yet been completely written off, with increasing taxes and with the present tendency toward declining earning power, there is a great need for net earnings in the banks with which to write off losses currently and build up depleted capital structures; and

Whereas it is obvious that every dollar that is transferred to the Federal Deposit Insurance Corporation to lie idle in its reserve is a dollar taken out of the lifeblood of the banking system, where it could be put to work for the strengthening of the individual banks and the banking structure as a whole; and

Whereas the administration recommended to Congress an assessment of a twelfth of 1 percent per annum on total deposits, and the House of Representatives saw fit to raise this assessment to an eighth of 1 percent per annum without permitting the corporation to assess a lesser amount; and

Whereas the bill affects large and small banks alike, and the raising of the assessment to one-eighth of 1 percent per annum and making same mandatory works a particular hardship on the small banks of the country by imposing this additional burden upon them at a time when they are least able to meet it: Now, therefore, be it

Resolved, That this association in convention assembled go on record as opposing in strongest terms the action of the House of Representatives in making mandatory the assessment of one-eighth of 1 percent per annum od total deposit liabilities of banks; and be it further

Resolved, That the Secretary of this association be instructed to wire our Senators and Congressmen of its action, and that the representatives of the individual member banks of the association be urged and requested to wire or write their Senators and Congressmen, setting forth the injustice of this assessment; also urging their influence, support, and vote in fixing the rate at one-sixteenth of 1 percent per annum which, in our judgment, would yield sufficient revenue to meet the requirements of the corporation.

(The witness withdrew from the committee table.)

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STATEMENT OF J. J. THOMAS, VICE GOVERNOR FEDERAL RESERVE BOARD, WASHINGTON, D. C.

Senator GLASS. You are familiar with the pending banking legislation, and if you care to express any view on the problem, the committee would be very glad to hear from you.

Mr. THOMAS. I am somewhat familiar with it. I do not think I should take up the time of the committee to go into detail, and I do not know of anything that I can offer that would add to what has been said. It would seem to be presumptuous to try to add to anything that Dr. Miller and Governor Hamlin have said. I would say that I am in harmony with the objectives of the bill.

Senator COUZENS. Do you think title II ought to be enacted now?

Mr. THOMAS. I am inclined to feel as Mr. Hamlin does, that we should patch the roof before it rains. I think there are things in that title that will be needed if the time comes. No one can tell when that will be.

Senator GLASS. What is there in the bill that cannot be as well done under the existing act?

Mr. THOMAS. I think, open-market operations, principally, that we do not have power over now. I think that authority should be centralized in the Board. I think it is not a regional bank operation. I think it is a system operation that affects the entire country as a whole, and is not a regional matter. Therefore I think authority ought to be in some central body representing the public's point of view rather than the bankers'.

Senator GLASS. You differ, then, with the unanimous verdict of the Board in March 1932?

Mr. THOMAS. I was not a member of the Board at that time.

Senator GLASS. I say, you differ with the unanimous action of the Board in 1932?

Mr. THOMAS. If that does not agree with what I have said now, then I differ: yes.

Senator GLASS. I wanted the record to indicate that.

Mr. THOMAS. I am in harmony with what Mr. Hamlin said.

If that is all the committee cares to ask, there is another matter that has not been brought out. It is in title III. I should like to call it to your attention. It has reference to interlocking directors between banks and also between institutions that are engaged in the sale, purchase, and handling of securities. We are sending a recommendation which differs from what is contained in the printed bill.

The original Clayton Act prohibited interlocking directors between banks having resources aggregating more than $5,000,000; also in cities of more than 200,000 inhabitants. The act excepted certain banks, but as to others, was absolute in its prohibition.

Later Congress enacted the so-called "Kent amendment" which vested the Federal Reserve Board with discretionary powers to permit interlocking directors in certain cases provided such banks were not "in substantial competition."

In 1928 the act was again amended so as to authorize the Board to grant permits for interlocking directors if, in the Board's judgment, it would not be "incompatible with public interest."

We found a great deal of difficulty in understanding what that means or in agreeing upon a policy or arriving at some standard by which

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we could measure what was "incompatible with public interest" in a given case.

Under the interpretation of our Legal Division we gradually took in everything, and there are some twenty or thirty different factors which have been considered under various circumstances in trying to ascertain what was "incompatible with public interest." Furthermore, it has been very difficult and unsatisfactory to administer from Washington.

We have recommended that the law be amended so as to prevent interlocking directors between two or more banks in all cases whether or not they are located in the same town, and regardless of the size of the bank or the town.

If the Senate does not feel it should go that far, then we would like to have the law amended so that we can decentralize its administration and have the applications acted upon in the first instance by the Federal Reserve banks.

I am in favor of more autonomy, so far as administration of the Banking Act is concerned. If we are going to pass on applications individually I think they should be originally passed on by the Federal Reserve banks under rules and regulations adopted by the Board, to insure uniformity, and permitting appeal or review.

Senator GLASS. So you are in favor of giving regional banks some authority?

Mr. THOMAS. Yes. I want to give them some work.

Senator GLASS. Do you think it is incompatible with the public interest for a regional bank to determine how to use the reserves of member banks, which involves also the deposits of the member banks?

Mr. THOMAS. I think this, Senator. The money of the banks belongs to the public, and it is recognized. Otherwise we would not regulate the banks.

Senator GLASS. What public?

Mr. THOMAS. The depositing public.

Senator GLASS. It belongs to the depositors, does it not?

Mr. THOMAS. The depositing public; and the directors are handling other people's money, just as we are, and I think the same principle applies to the Interstate Commerce Commission. The Commission does not own the railroads, and the Government does not. They are privately owned, but they are charged with the public interest; and I think the money and credit system is just as much charged with public interest as are the railroad systems.

Senator GLASS. The Interstate Commerce Commission cannot change a rate without due notice and public hearing, can it?

Mr. THOMAS. Perhaps not.

Senator GLASS. Is not that a fact?

Mr. THOMAS. It is a fact. But they can change it. They regulate even more than that; they regulate the character of service, and things of that kind; they tell a road whether it can discontinue a branch, and so on.

Senator GLASS. Railroads are not regional, are they?

Mr. THOMAS. No. I do not think a national banking system ought to be regional, either, excepting so far as the ordinary banking functions are concerned. I think the proper function of banking should be regional, and for that reason I recommend that in passing upon interlocking directors' applications they could handle it better than

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we can from Washington; but I think when it comes to policies that are national in scope, they should be under the ultimate control of some body which represents the public. You may call it a political body if you want to, but that is the way I feel about it.

Senator GLASS. Let me ask you one other question. You say you are in sympathy with the objectives of the bill. Did you have any part in its preparation?

Mr. THOMAS. None.

Senator GLASS. Did you see it until it was sent up here and printed?

Mr. THOMAS. No; I think not. We were meeting the same day on which it was printed and introduced, and we were to have a meeting to consider it, but I think that inadvertently it was introduced without that. But we have discussed it considerably since then.

Senator GLASS. Since then?

Mr. THOMAS. Yes.

(The witness withdrew from the committee table.)

STATEMENT OF M. S. SZYMCZAK, MEMBER OF THE FEDERAL RESERVE BOARD, WASHINGTON, D. C.

Mr. SZYMCZAK. Mr. Chairman and gentlemen of the committee, it seems essential to preserve our regional Federal Reserve System, which consists of 12 Federal Reserve banks with 9 directors in each bank, together with a Federal Reserve Board in Washington. In this particular respect, our System is different from that of most countries because of our extensive area, and because of our political and economic structure of States and districts, based upon industrial, agricultural, commercial, and financial conditions and needs which are widely different in the various parts of the United States. The System is composed of essential parts. These parts, however, must be cohesives for the best functioning of the System.

To make for an efficient administration of the act by the System and to arrive at the purposes for which the act was passed by Congress, it appears necessary for the Federal Reserve Board to have a more direct contact with the various sections of our extensive area.

To be effective, the whole Federal Reserve System must be one. This end is not difficult to attain; personal contact of the members of the Board with the directors of the 12 Federal Reserve banks seems one of the best direct avenues.

Bank powers of the boards of directors of the 12 Federal Reserve banks should be retained, and in some respects increased and extended, at least by regulation of the Federal Reserve Board.

While of course it is sound to have the Federal Reserve Board and its principal offices in Washington, and while it is sound for the board to hold its meetings in the capital because of the national scope of its considerations, yet it would be desirable from a practical standpoint for the Federal Reserve Board to meet at least four times a year in at least four parts of the country—the East, West, North, and South—to meet with and understand better the directors of the Federal Reserve banks and their officers; as well as the conditions and needs of commerce, industry, agriculture, and finance in the respective districts. It would also seem wise to provide by law that each member of the board should be assigned by the Federal Reserve Board to the task of keeping himself especially familiar with conditions in at least

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two of the Federal Reserve districts each year, in order that he might act as a liaison officer between the Federal Reserve banks, their directors and officers, the representatives of commerce, industry, agriculture, and finance on the one hand, and the Federal Reserve Board in Washington on the other hand. Provision could be made to have members of the board rotate in their district assignments, so that eventually each member of the board would have covered by direct contact all of the sections of the country and would know their needs thoroughly. Without this it is next to impossible for the board members to appreciate fully the needs and requirements of the Federal Reserve banks and of the country as a whole; without this the Federal Reserve Board inclines too much to theory and bureaucracy; without this there is bound to be misunderstanding between the Federal Reserve banks and the Federal Reserve Board leading to differences of opinion on authority; and without this a cry is heard on the one hand that the private interests wish to control the system and direct its operations for their own selfish purposes; and that on the other hand political interests wish to control the system and direct its operation in accordance with their own political ambitions.

Members of the Board, when assigned by the Board to several districts, would keep personally in touch with the boards of directors and the officers of the Federal Reserve banks in those districts. They would thus become familiar with the management of such Federal Reserve banks, with their viewpoints, and with the problems of their districts. They would also know men in the industrial, commercial, agricultural and financial fields of the districts. They would not be compelled to depend entirely on the Board's staff for information having to do with the internal management of the banks, as well as with the general agricultural, commercial, industrial, and financial banking conditions of the districts; thus there would be a better opportunity for sound and practical rulings of the Board on all questions when they are presented by the banks to the Federal Reserve Board under the law. It is specifically stated in the act that the Federal Reserve Board has general supervisory responsibilities, but in order to supervise, one must be in direct contact with those supervised. Otherwise, one is compelled to act upon information obtained from other sources.

Of course in all cases the Board, as a whole, would act officially on all these matters, but the Board would have the benefit of the information obtained by the individual member assigned to the specific district.

It would also seem desirable to have the boards of directors of the Federal Reserve banks meet once every year with the Federal Reserve Board in Washington, or, if this could not be accomplished, with the directors who are farther removed from Washington, the Federal Reserve Board could arrange to meet them at a point more accessible at least once every 2 years to discuss frankly and completely matters pertaining to the operation of their banks and the conditions in their districts, as well as problems of a national character.

The execution of many of the powers vested in the Federal Reserve Board could, under the provisions of the Banking Act of 1935, be decentralized under regulations of the Federal Reserve Board so that they could be carried into effect by the Federal Reserve banks without the reference of many individual matters to Washington, and thus

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obtain desirable and effective administration. This will be facilitated by the provision in the bill authorizing the Board to delegate its powers to individual members or other representatives.

To make for a constancy and a permanency of the work of the Board by its individual Board members, I recommend that there be a specific requirement in the law that the Board assign its work to individual Board members, each Board member to have a specific task assigned on which he is to specialize and through which he is to keep in touch with the Federal Reserve banks and the country, and on which he is to report to the Federal Reserve Board with recommendations. This seems to me to be very important, from the standpoint of good administration.

It has been my experience that the Federal Reserve Board does not wish to, nor should it, assume any more powers than it can properly use for the effective administration of the System, and whenever powers are granted to the Federal Reserve Board having to do with matters that could be handled better by the directors and officers of the Federal Reserve banks, the Federal Reserve Board should be able to give the 12 Federal Reserve banks the power of determination of many important matters.

It is good organization for the Federal Reserve Board to recognize this fact and to avail itself of the commercial, agricultural, industrial, and financial experience of the directors of the 12 Federal Reserve banks, as well as the technical and banking experience of their officers, who are the vehicles through which the policies of the System are executed.

There are many powers now in the Federal Reserve Board, however, which in my opinion should be placed in the regional Federal Reserve banks. This would expand the authority and responsibility of the directors of each Federal Reserve bank and make for more prompt and efficient administration of the Federal Reserve System. The general supervision should be retained, but the direct and ultimate action in these matters should be taken by the directors and officers of the Federal Reserve banks.

The detailed matters which might be delegated to the Federal Reserve banks (or the Federal Reserve agents, if their offices are not abolished) include the following:

1. Admission of State banks to membership in the Federal Reserve System.

2. Expulsion of such banks from membership for violations of the law or the Board's regulations.

3. Waiver of 6 months' notice of voluntary withdrawal of State banks from membership.

4. The granting of voting permits to holding-company affiliates of member banks.

5. The revocation of voting permits for violations of the law or the regulations.

6. The issuance and revocation of permits authorizing officers, directors, and employees of member banks to serve not more than two other banks (if the provision for individual permits is not repealed as proposed in the bill).

7. The issuance and revocation of permits for officers, directors, and managers of security companies to serve as officers and directors

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of member banks (if the provision for individual permits is not repealed as proposed in the bill).

8. The granting of trust powers to national banks.

9. The cancelation of such powers at the request of national banks.

10. Approval of reduction of capital stock by national banks (if the requirement of the Board's approval is not repealed as proposed in the bill).

11. The granting of permission for member banks to invest amounts exceeding their capital stock in bank premises or in the stock of corporations holding their bank premises.

12. The approval of the establishment of branches by State member banks (if this power is transferred from the Comptroller of the Currency as proposed in the bill).

13. Authorizing national banks to establish foreign branches.

14. Authorizing national banks to invest in the stock of banks or corporations principally engaged in international or foreign banking.

15. Permitting interlocking directorates between member banks and foreign banking corporations in which they own stock.

16. Approval of compensation of officers and employees of Federal Reserve banks.

In addition to the above, where action by the Board is required under the law, numerous matters are presented to the Board for consideration in connection with banking supervision and requiring action on individual cases; for example, reductions of capital stock of State member banks, consolidations of State member banks with other banks, and whether or not individual banks should increase the amount of their capital and surplus in relation to their deposit liabilities. In some cases of this character the Board has already authorized the Federal Reserve agents to act on its behalf in the individual cases within certain prescribed limitations.

Some, or perhaps all, of the powers enumerated above, and perhaps others too, it seems to me, should be vested directly and ultimately in the Federal Reserve banks. This would make for efficiency and good relation between the Federal Reserve Board and the Federal Reserve banks. It is quite natural that the Federal Reserve banks know more about that subject matter because they are directly and constantly in contact with it. It is also natural, however, that the Federal Reserve Board should supervise and coordinate and bring to the attention of the Federal Reserve banks any incorrect or improper administration of these powers. This would make for unity.

Therefore, in view of what I have already stated, it seems that the chairman and Federal Reserve agent of the Federal Reserve banks should be retained, because this is consistent with the purposes of the framers of the Federal Reserve Act, namely, that the Board should have an official representative at each Federal Reserve bank to directly supervise the operations of the bank. It seems that in the minds of the framers of the act the chairman was apparently to be the supervisor of the bank as a representative of the Federal Reserve Board. Actually the governor appointed by the board of directors of the bank has been the chief executive. By consolidating the offices of chairman and governor, the governor would be mentioned for the first time in the act, and would be designated as the chief executive of the bank, and since he will also be chairman of the Board,

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he will report to himself. At the same time, however, the representative of the Federal Reserve Board at the Federal Reserve banks is eliminated.

Some say that under the pending act the combination of the two positions takes away powers from the directors of the Federal Reserve banks because the Federal Reserve Board would have a veto power over the appointment of the governor and chairman. The fact of the matter is that the chairman and Federal Reserve agent, appointed under the Federal Reserve Act by the Federal Reserve Board, would be eliminated and the directors of the Federal Reserve bank would appoint the governor, and when the governor is approved by the Federal Reserve Board, he would become a class C director. The vice governor, who would also be appointed by the directors of the bank subject to the approval of the Board, might also be appointed a class C director by the Board. This would leave the Federal Reserve Board only one additional class C director for appointment as compared with six class A and B directors elected by the member banks, and two class C directors selected by the board of directors and approved by the Federal Reserve Board.

Here it seems to me we are getting away from what was originally intended by the framers of the Federal Reserve Act, namely, that the chairman of the board, the head of the board of directors of the Federal Reserve bank, be likewise a representative of the Federal Reserve Board, and that the Federal Reserve Board, of itself, and not upon recommendation of the class A and B directors, appoint three directors of the nine at each Federal Reserve bank.

Also by having the Governor feel that his appointment rests with both the directors of the bank and the Federal Reserve Board, we divide responsibility, and, therefore, we divide authority over the chief executive officer. This places the Governor in a dual position. This is another reason why I should prefer to have the chairman and Federal Reserve agent retained.

An effective relationship between the directors of the regional banks and the Federal Reserve Board in Washington can be accomplished if individual members of the Board are each assigned several Federal Reserve districts with which they must keep constantly in touch, especially on matters affecting the relation between the Board and the banks.

Proper assignments of districts among the Board members should be directed by law. This might be done by some modification of the proposed amendment authorizing the Board to assign specific duties and functions to designated members of the Board or its representatives.

I agree with the recommendations made by Dr. Miller, with some modifications, with reference to making the Board further independent, except that I feel that the chairman and vice chairman of the Board should be designated by the President.

At the present time the President designates the Governor of the Board without the advice and consent of the Senate.

His term as a board member should not expire with the expiration of his term as chairman. The Secretary of the Treasury should continue as ex officio member, but not as chairman of the Board. The Comptroller of the Currency should be continued on the Board as an ex officio member. Both the Secretary of the Treasury and the

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Comptroller of the Currency should have no vote on the Open Market Committee.

Under the bill, authority for open market policy is taken away from the Federal Reserve Board and the directors of the Federal Reserve banks, and the governors, and is placed in a committee of five, a majority of whom are members of the Federal Reserve Board.

It would seem that a better method would be to have the governors make recommendations on open market policies. However, actual determination of what these open market policies should be seems to be a national and not a local question. Therefore authority should be vested in the Federal Reserve Board. The Board should receive information from the Federal Reserve banks and should not act until after it has received proper advice and guidance from the Federal Reserve Bank directors through their governors. Power should be granted to these directors, if they object to open market policies, to make objections to the Federal Reserve Board in writing, and opportunity should be provided for hearings before the Federal Reserve Board, but final determination of policies in any case should be with the Federal Reserve Board.

I understand that Governor Eccles has made a recommendation to this effect. I should, however, like to suggest that all 12 of the governors constitute the committee to advise the Board on open market policies. They should be allowed to choose any method of procedure they think best.

It is generally assumed that the Federal Reserve Board is responsible for open-market policies. Few people, even today, are aware of the fact that the present open-market committee consists of 12 men who represent the 12 Federal Reserve banks, and that the Federal Reserve Board merely approves or disapproves, but does not initiate open-market policies. Few people also realize that each Federal Reserve Board has the right to refuse to participate in an open-market operation after it has been adopted by the 12 Governors and approved by the Federal Reserve Board. It may be contended that the Federal Reserve Board should not have this power because it is in Washington, the Government's capital, and because its members are appointed by the President with the advice and consent of the Senate. It may be said that political pressure might be used against the Board and that the Board might be influenced by such pressure in its monetary control. On the other hand, it is argued that the Governors are appointed by the directors of the Federal Reserve banks, six of whom are elected by member banks—private interests—and that such Governors may be guided in determining open-market policies by the private interests of the member banks, and not by national needs and requirements of the country. Both views are most extreme.

Authority must be vested where responsibility rests. That is logical. With 3 of the members of the open-market committee consisting of Federal Reserve Board members and 2 of Federal Reserve bank governors, the open-market committee would be construed to be the Federal Reserve Board without the Board actually having any authority over open-market operations. But since open-market policy is a national question, authority as well as responsibility for this policy should be located in one place, and in the Federal Reserve Board, which is a national body.

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Senator GLASS. Whence are the funds used in open-market operations derived?

Mr. SZYMCZAK. From the member banks. I come to that point later, Senator.

Senator GLASS. Proceed.

Mr. SZYMCZAK. This seems to be in the essence of the purposes of a Federal Reserve Board. This seems to be the surest way of establishing the fact whether the System or the Board is, or is not, functioning in accordance with the purposes for which it was created. It removes the opportunity for excuses.

Of course, the Board would feel that its own research organization should be extended and strengthened and given more active functions to perform and the membership of the Board would feel the need of keeping more closely in touch with current developments which might affect open-market policy and the interpretation thereof, but the Board would be in far better position to determine when and in what circumstances to initiate an open-market policy on the basis of a coordinated view of all the factors entering into the monetary situation—reserve requirements, discount rates, lendings of member banks, the Government's fiscal policies, etc.,—and could take action promptly on its own responsibility in whatever direction seemed best to meet the needs of the situation at the time. However, to make the parts of the System more cohesive a provision might be made for a sufficient representation of the regional banks on this committee for the sake of unity in the System so long as the tendency is in the direction of making the System one and not two.

In the interest of unity, the Open Market Committee might consist of the 6 appointive members of the Board and 5 Governors—the 5 Governors to be designated by the 12 Governors of the 12 Federal Reserve banks and to be chosen from five sections of the country, namely, the North, South, East, Middle West, and the Far West. While the Secretary of the Treasury and the Comptroller of the Currency might continue as members of the Board they should have no vote on Open Market Committee policies. Their membership on the Federal Reserve Board is valuable in many respects, but the Act might provide that they have no power of a vote on open market operations, but might be called by the Open Market Committee for information that the committee might wish to have in the consideration of adopting open market policies.

I also recommend the striking out of the following words from the suggested amendment on the objective of the System:

> As to promote conditions conducive to business stability.

I agree with Dr. Miller also with slight amendment, that the offered amendment on eligibility of discounts be amended to read as follows:

> "Notwithstanding any other provision of law, when it deems it in the public interest, a Federal Reserve bank may recommend, and by an affirmative vote of not less than five of its appointive members, the Federal Reserve Board may authorize any Federal Reserve bank, for limited periods to be recommended by the Federal Reserve bank and prescribed by the Board, but which may be extended by the Board from time to time upon application of the Federal Reserve bank, to make advances to member banks which have no further eligible and acceptable assets available to enable them to obtain adequate credit accommodations through rediscounting at the Federal Reserve bank or by any other method provided by this act. Such advances may be made on the promissory notes of

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such member banks secured to the satisfaction of the Federal Reserve bank, and shall be subject to such regulations and shall bear such rates of interest as may be prescribed from time to time by the Federal Reserve Board upon recommendation of the Federal Reserve bank."

My recommendation places in the Federal Reserve banks the power of making the request.

Of course, I can understand that this Banking Act offers much opportunity for extreme interpretation. However, with the amendments offered, it seems to me to meet existing conditions and to serve a definite purpose without being extreme in either direction. It deserves at least having each section considered on its merits. It seems to serve the definite purpose of a better administration of the Federal Reserve Act.

Senator GLASS. Did you have any part in the preparation of this bill?

Mr. SZYMCZAK. No, sir.

Senator GLASS. Did you see it until it was printed?

Mr. SZYMCZAK. No. I saw certain parts of it from time to time, but I did not see it as a whole until it was printed.

Senator GLASS. I note that in March 1932 Governor Eugene Meyer suggested, with respect to membership on the Board of the Secretary of the Treasury and the Comptroller of the Currency, that it might be well to permit them to be continued as ex-officio members without vote.

Mr. SZYMCZAK. I did not know that he made that recommendation.

Senator GLASS. I note that you have, in a modified form, made the same recommendation.

Mr. SZYMCZAK. Yes, sir.

Senator GLASS. What is your reaction to the suggestion of Dr. Miller that the Federal Reserve Board be constituted a board of governors of the Federal Reserve System?

Mr. SZYMCZAK. I think that is very sound. I think the suggestion is a very good one.

Senator GLASS. We are very much obliged to you, sir.

(The witness withdrew from the committee table.)

Senator GLASS. Is there any other banker here from Texas who desires to be heard? (No response.)

Senator COUZENS. I move that the hearings be closed.

Senator GLASS (after conferring with members of the subcommittee). The committee has determined to close the hearings, there being nobody representing groups of people who seem to desire to be heard. So that we will close the hearings for the present, and I think finally.

Mr. CZERWONKY. Senator Glass, would you like to hear from an engineer? I have some information here that is vital on this bill, and I want to have an opportunity to put it into the record or present it before the committee.

Senator GLASS. You may present it for the record, and if the committee deems it of the same importance you think it is, it will agree to put it in the record.

Mr. CZERWONKY. I would surely appreciate it. It would take about half an hour. I think it would change the opinion of some of the members of the committee. This is an engineering and scientific approach to the problem.

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Senator GLASS. It would have to be very scientific and very superior engineering to change the minds of any of the members.

Senator COUZENS. I move, Mr. Chairman, that his brief be placed in the record.

Senator GLASS. Without objection, if, after examining the brief, we determine it ought to go in the record, we will place it there.

The committee will go into executive session at this time.

(Whereupon, at 3:05 p. m., the hearings were concluded and the subcommittee went into executive session.)

STATEMENT SUBMITTED BY HUGO E. CZERWONKY,[1] 705 EIGHTEENTH STREET NW., WASHINGTON, D. C.

Answer to the questions: (3) Does the banking bill of 1935, with amendments that have been proposed, remedy the defects in our present money rules, and (4) How can this banking bill be strengthened and made more effective.

The object in the first stage of this treatise was to explain why changes in our money rules were necessary. The last part, answer to questions 3 and 4, was to center the attack on the best methods (technique) which might be utilized.

There was no thought in the presentation of the preceding or subsequent material to publicly express opinions, but to give those who are interested in economics and economic liberty a factual analysis of why our economic system breaks down, and why it will continue to break down until certain changes are made in our money rules. There was no intention to attack the "new deal." The President has all along indicated his receptiveness to constructive criticism.

My special purpose in appearing before your committee is to offer an amendment to the banking bill which I believe will materially strengthen it, add something constructive to it. Before stating the amendment, copies of which I will later give each of you, I would like to refresh your minds on the mechanics of the bill as it appears at present.

There is provision therein which permits the Board to alter the reserve requirements or reserve ratio. The authority to increase the reserve requirements is intended to prevent an expansion of bank credit which would be injurious to those members of society who receive fixed return on investments (owners of bonds, mortgages, etc.) or fixed incomes. As Governor Eccles has mentioned before this committee, the member banks, with the reserves that they now have, could expand credit by approximately 20 billions of dollars if there existed a demand by industry or individuals for loans, and provided the bankers were willing to make the loans. The discretionary power, therefore, to increase reserve requirements is well taken under present conditions.

There exists power in the Banking Act should it later become necessary, for the Board to likewise decrease the reserve requirements below what they are today should this be justified. There always exists then within the power of the Board to permit an expansion of bank credit, providing a combination of necessity of loans (necessity of expansion) within the Nation and a demand by entrepreneurs or individuals for loans exists. These conditions provide for a solution of one-half of the problem.

Should, however, there exist a need for expansion of the flow of dollars within the Nation, a need to ease the market as economists might say, but no demand for increased loans, then the Reserve Board is empowered to resort to open-market operations, buying United States bonds from member banks and exchanging therewith dollars in currency or credits subject to check. The member bank would then have its reserves increased, enabling it to make new loans to others. The resorting of the Reserve Board to the purchase of United States Government bonds does not, however, provide any positive assurance that the new dollars or bank credits will be put to work (loaned to others), that they will be spent for goods or services on wants which otherwise would go unsatisfied. If banks cannot

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[1] The writer is a member of the engineering profession with more than 10 years of practical experience in engineering, sales, and advertising, 6½ years acting as technical advisor (sales engineer) on the processing of products through labor-saving equipment. For 2 years he was on the faculty of the University of Wisconsin, college of engineering, extension division, as instructor in statics and dynamics. For approximately the past 2 years he has been engaged full time in scientific research in the field of economics. Part of this research was at Government expense, and part at his own expense. The approach to the economic problem was dynamic and not static, viewed from the physical concept of flows and changes of flows.

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find a place where they personally believe they can profitably and safely invest them, even at lower interest rates, cannot find entrepreneurs who desire to use them or individuals to borrow for current consumption of goods, then business instability will set in. The net result of open-market operations is to influence an increase in demand for goods, not assure increased demand.

As you gentlemen well realize, there is a distinct difference between trying to influence the attainment of an increased flow of dollars for goods, and taking conscious measures to see that increased flow takes place; the latter can be accomplished without price inflation.

With the new powers, controls available in this legislative act, it is impossible to maintain business stability. This bill within itself lacks the definite, drastic double-edged means of action to control the situation. The method of performance is weak. The apologetic statement "so far as such purposes may be accomplished by monetary and credit policy" is well taken. The controls authorized herein must be supplemented by another instrument, outside this measure, governmental works projects financed by bank credit expansion. Budget deficits balanced by governmental borrowings; the Government undergoing an interest-bearing obligation to the commercial banking system of the Nation. The latter is the direct means for reinforcing the flow of dollars.

A direct method of expansion, or direct method of inducement to create expansion of credit, should be incorporated in this banking bill; a method which is not made inoperative by failure of Congress to approve governmental Budget deficits; a method which would for one thing result in a positive impetus by entrepreneurs for credit when the expansion is necessary to maintain business stability; a direct method which would work hardship on no groups or individuals in society, which would result in cooperation by all parties concerned—generated through the motive of gain. With this added feature in the banking bill there need not ever be another general business depression.

The maintenance of the flow of dollars and adjusting it when necessary is the vitalizing factor which keeps the wheels of industry turning—the water which motivates the turbine wheels—and the method of accomplishing this must be positive. Failure to adjust and maintain the flow accounts for our economic system getting the way it has, out of order.

Section 2 of the banking bill as now drawn has some constructive proposals, such as powers to raise or lower the reserve ratio; power to raise or lower the discount rates; and wider eligibility of paper for discount, bu t the main device, open-market operations, is not an effective instrument of monetary and credit control. Those who are advocating open-market operations as the instrument for maintaining industrial stability have overlooked the importance of the indirect method of "capital" formation which in the main characterizes our economy.

A recovery which shall be accompanied by continued business stability cannot come through makeshift tactics or devices. The tools must comply with sound scientific principles.

The statement of Mr. Aldrich before this committee, challenging the theory that under conditions which have existed in this country the volume of bank credit can be stimulated by open-market operations, substantiates my scientific contentions of the inadequacy of these working tools. He (Mr. Aldrich) recalled that between March 1932 and November 1933 the Reserve banks bought $1,600,000,000 of Government obligations in open-market operations, and that the effect in the beginning was to relieve strain on the member banks, but there was no proportionate stimulation of the growth of bank credit, one of the purposes of the operations.

Let me cite you another instance as recorded in Credit Policies of the Federal Reserve System, page 221, by Dr. Hardy. "The purchase of securities by the Reserve banks has somewhat more effect on the volume of credit than have changes in the rediscount rate, but its primary incidence is on the rates charged in the open market. It does not produce corresponding changes in the amount of credit taken by businessmen. Reference has been made to situation in 1924. In the 12 months from October 31, 1923, to October 31, 1924, the Reserve banks increased their open-market holdings from $296,000,000 to $784,000,000, yet during that time the total of Reserve bank credit outstanding decreased by $130,000,000."

Governor Eccles in his appearance before this committee flatly said he did not believe the stock of the 12 Federal Reserve banks should be held by the Government. He pointed out that the powers of management are "the important matter rather than who owns the bank." I concur with the Governor in his

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statement, providing the powers (instruments) granted to management under either set-up are identical. A management without power (the proper tools) is impotent, no matter how good their intentions or capabilities. This bill as it is written, with amendments suggested or requested by Governor Eccles has not the instruments within it that are as effective as if ownership resided in the Government, but by properly drawn amendments it can be made as equally effective as the latter, and without doing injury to private bankers or stockholders. My personal belief is it could even be made superior in performance to a bill as it is now drawn, pending in the committee, with Government ownership of the 12 Reserve banks as its objective. This amendment I now offer in the interests of the public and of the banks to assure effective and workable banking legislation.

AMENDMENT TO TITLE 2 OF THE BANKING BILL OF 1935 (THE FLETCHER-STEAGALL BILL)

An account known as the "business stability account" shall be caused to be set up in the Federal Reserve System [2] by the Federal Reserve Board, and be subject to control by this Board. (It is the purpose of the business-stability account to supplant open-market operations as the instrument for maintaining business stability within the Nation.)

To the business-stability account of the Federal Reserve System shall be caused to be debited:

(1) Such total number of dollars as are credited by member banks to entrepreneurs as a result of negative interest rates on loans when these rates are authorized by the Board;

(2) Such total number of dollars as are credited to member banks for services rendered on loans involving negative interest rates when these rates are authorized by the Board; and

(3) Such total number of dollars as are authorized by the Reserve Board as grants to be credited to the account of the Federal Government.

The total number of dollars credited to the Federal Government as grants shall be expended with minimum delay by the Treasury, in accordance with previously drawn recommendations by Congress. In general these dollars are to be used for promoting education, scientific research, the arts, and for such other public projects as Congress may hereafter specify.

It shall be the duty of the Federal Reserve Board to exercise such powers as it possesses in such manner as to maintain business stability and promote full employment.

EXPLANATION OF OPEN-MARKET OPERATIONS FROM CREDIT POLICIES OF THE FEDERAL RESERVE SYSTEM, BY DR. HARDY, PAGE 229

"When it is desired to ease (increase the flow of dollars) [3] the market, securities are bought and the discount rate is lowered. The lowering of rediscount rates by itself would give some incentive to banks to make added use of their rediscount facilities. But the fresh money which comes into the reserves of member banks on account of the open-market purchases makes it their immediate problem to find uses for new money rather than to increase their balances by rediscounting. Under such circumstances the practical alternatives are either to buy securities, to increase open-market loans, or to pay off rediscounts * * *. In the converse case, when sales of United States securities are made in large volume the banks lose reserves. They cannot sell securities except to one another, nor can they quickly collect any substantial amount of their outstanding loans. Consequently they borrow, at least temporarily, to replenish their reserves, and the higher rates which are exacted at such times have no apparent restrictive effect."

[2] This means the 12 Federal Reserve banks.

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Illustration of the principle of negative interest rates as suggested by Hugo E. Czerwonky; purpose, an instrument to promote business stability

Amount of loan	$1,000
Length of term years	12
Rate of interest percent	−3
Annual payments tendered	$70

Annual periods	Tendered annual payments	Interest, −3 percent	Total paid on principal	Amount of principal still unpaid
1	$70.00	−$30.00	$100.00	$900.00
2	70.00	−27.00	97.00	803.00
3	70.00	−24.10	94.10	708.90
4	70.00	−21.25	91.25	617.65
5	70.00	−18.50	88.50	529.15
6	70.00	−15.80	85.80	443.35
7	70.00	−13.30	83.30	360.05
8	70.00	−10.80	80.80	279.25
9	70.00	−8.40	78.40	200.85
10	70.00	−6.05	76.05	124.80
11	70.00	−3.75	73.75	51.05
12	49.52	−1.53	51.05	
Total	819.52	−180.48	1,000.00	

NOTE.—All calculations were made by slide rule.

BOOKKEEPING ENTRIES (JOURNAL ENTRIES) FOR LOANS INVOLVING NEGATIVE INTEREST RATES,[4] AND SERVICE CHARGES ON SUCH LOANS

EXAMPLE: An illustration of a $1,000 loan involving an annual tendered payment by entrepreneur of $70; a negative interest rate of 3 percent; a service charge of member bank established by the Board of $100:[5]

Books of member bank

Debit:
- Notes receivable (note given by entrepreneur) $819.52
- Notes receivably (note given by Federal Reserve System) 280.48

Credit:
- Entrepreneur $1,000.00
- Service account of member bank 100.00

Books of Federal Reserve System

Debit: Business-stability account $280.48
Credit: Member bank $280.48

BOOKKEEPING ENTRIES (JOURNAL ENTRIES) FOR GRANTS, AUTHORIZED BY THE BOARD, TO BE CREDITED TO THE ACCOUNT OF THE FEDERAL GOVERNMENT

Example: A $10,000 grant to be spent in accordance with previously drawn recommendations by Congress:

Books of Federal Reserve System

Debit: Business-stability account $10,000
Credit: Member bank $10,000

Books of Member bank

Debit: Notes receivable (note given by Federal Reserve System) $10,000
Credit: Federal Government $10,000

[4] Rate to be established by the Federal Reserve Board.
[5] Service-charge rate to be determined by the Federal Reserve Board, sliding scale of rates. The $100 charge was decided on arbitrarily in order to illustrate the principle.

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DEFINITION OF "SOUND" MONEY

A "sound" money is one that obeys or conforms to scientific money rules. Scientific money rules depend on the nature of the economy. We have in the United States a profits economy with "capital" formation in the main indirect. Scientific money rules for such an economy are not identical to scientific money rules in a profits economy wherein everyone is a producer, owner of "capital", and marketer of goods.

The above definition declares by implication that a money which by combination of statute and rule of thumb is caused or permitted to expand or contract only with respect to the total of any specie or combination of specie is unsound money for a profits economy wherein "capital" formation in the main is indirect.

DEFINITION OF INFLATION AND DEFLATION

Deflation and inflation arise out of a failure of a nation to adhere to scientific money rules. Deflation (in a profits economy wherein the formation of "capital" in the main is indirect) is the phenomenon resulting from the failure to maintain, or adjust to, the proper minimum flow of dollars.

Inflation (in a profits economy wherein the formation of "capital" in the main is indirect) is the phenomenon resulting because of making adjustments or maintaining a flow of dollars that are excessive.

NOTE.—To understand these definitions a person has to have a physical concept of flows when thinking of an economy.

The prime idea of negative interest rates on loans made to industry is to induce both a current expansion of flow of dollars, and an absorption of idle man-power where employment will be sustained in the community, not have to be supported through taxation. If dollars are spent on public-works projects the workers directly engaged therein lose employment when the projects are completed. This is not true when workers are absorbed by industry.

The Board should be given authority to establish the interest rates, varying them so as to induce action by entrepreneurs, be able to cope with economic conditions.

Compensation to the member bank for their services could be established at a definite interest rate (detailed schedules could be worked out, or a definite percentage of the face of the loan could be allowed for service, these charges or the lump sum being likewise debited to the business-stablility account, and credited to the account of the member bank originating the loan to industry. The entire matter could be handled in a very businesslike manner. Observe that the community as a whole, not the entrepreneur, would bear the service charge as well as the dollars accruing to entrepreneurs because of negative interest rates. This would not, however, represent a sacrifice on the part of the members of the community, maximum goods flow otherwise not generated.

The loans at negative interest rates would not be granted for refunding present indebtedness by industry, but to bring into existence an increased flow of goods, or the maintenance or expansion of industrial facilities. These loans would not be permitted excepting for purposes of "capital" formation as previously defined, and for fixed investment in goods in process. This eliminates such loans to individuals for purchasing either durable consumers' goods—homes, automobiles, radios, apartment buildings, etc.—or such loans for more perishable consumers' goods as food, clothing, etc. The board, under these conditions, should be permitted to establish such rules as would assure the loans being properly employed.

It is very likely that if the Board were addressing the problem with complete current data on the flow of finished consumers' goods and of dollars from week to week, or month to month, that the total of grants to industry during a period of a year would be a ridiculously small amount after our economic system was again functioning near capacity. Regurdless of the amount, society would be the gainer because we would be running at capacity instead of having idle workers and idle plants.

Under present conditions this method would be a very much more effective tool to get the unemployed back in their normal pursuits in industry than public works projects. If this method were introduced now, the negative interest rate could be set very high, possibly −6 percent, and then gradually reduced as business got into full swing.

Here, gentlemen, is a positive practical stimulant to employers (entrepreneurs) to provide steady work, and not an appeal to patriotism. Here is a measure providing real social security, scientifically sound.

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The granting of negative interest rates in loans to industry in order to induce entrepreneurs to increase the flow of goods, compensating for the difference between the total dollars loaned and those eventually to be repaid by debiting the business-stability account, or making grants to the Government to spend as Congress shall decree, likewise debiting the aforementioned account, are not utopian panaceas. They are practical measures to positively deal with a situation in a pecuniary system wherein profits are the motivating factor, and where "capital" formation in the main is indirect. Failure to make adjustments as suggested herein will otherwise necessitate periodic writing-off of losses by industry, with consequent confiscation of property of savers (investors, endowments of our educational and charitable institutions; untold suffering to individuals through unemployment, etc.) in order to balance the bookkeeping system of the Nation.

The question will undoubtedly be asked, "For what purposes are the member bank service charges?" It should be made clear that the establishing by the Reserve Board of negative interest rates on loans in no way changes the procedure which would be followed by entrepreneurs in making loans. The individual banker in the community would continue to pass judgment on whether a loan should or should not be made. They would be held responsible to see to it that the entrepreneur repays his obligations to the banking system. For this responsibility, and the bookkeeping and check handling expenses which would be incurred, the service charge is intended.

It is not the intention that the Federal Reserve banks shall make loans directly to industry to engage in banking functions. The functions of Reserve banks and the Board are only that of monetary policy, maintaining business stability and using their offices to gain full employment of the people within the Nation.

The physical purposes for which the loans would be utilized, outside of the fact that they must be for "capital" purposes and goods in process, are of no concern to the Board. From this it is apparent that industry would have nothing to fear, that entrepreneurs would be dealing with their local banker, and not with any one person or group who had visions of a planned economy. Elimination of political domination would also be maintained.

Observe the difference to the member banks in using the business-stability account to ease the market instead of open-market operations. First, the member banks would not be forced to part with some of the their income-earning property (assets), their revenue would be sustained. Better still, they would be assured increased earnings. There is no class economics in this proposal or amendment. It is consistent with the American method of doing things, the ideal of fairness. A society as a whole working through science and the scientific professions is enabled to enjoy an increased consumption of goods (increased flow of consumers' goods has been generated and is ready for consumption) then the private bankers and their stockholders also benefit and share in the prosperity. They are not singled out as a group through open-market operations and punished by having their income or goods consuming ability curtailed. Second, the new loans would be made under more favorable conditions for the bank, the risk would be less because the entrepreneur would be obligated to repay less to the banker than he had borrowed. Third, if entrepreneurs could not be induced under any conditions to make additional loans, or provided the Board believed the funds could be more sensibly utilized by the community in making grants to the Government for encouraging science, the arts (general unemployment had been overcome), then the adjustments could still be made and business stability positively assured. This would protect the investment portfolio of the banks. Fourth, we could positively fulfill our responsibility as a creditor Nation, and some of the assets which are now owned by banks, which are practically worthless, foreign government bonds and private foreign issues, would regain their income-earning capacity, rewarding the community and the officers and stockholders of banks.

An additional advantage in the establishment and the utilization of the business-stability account rather than open-market operations in order to maintain business stability is that this would disarm all those critics of the control of the flow of money whose objections are that this bill (1) opens the way to the political seizure of the assets of the Nation, what is meant is the seizure of the income-earning assets of the member banks (Uuited States bonds), and (2) those from whom emanate the fear talks of governmental insolvency made possible by "turning debt into money through the means of a political bank.[4]

[4] Rate to be established by the Federal Reserve Board.

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It would seem to me to be in the best interests of society both from a practical point of view, and public honesty to protect the private member banks in the event that a positive interest rate less than what was adequate [4] to meet expenses and allow a "fair" profit to the owners and managers of private banks were necessary in order to induce entrepreneurs to make loans at a given period of time.

Example: Let us assume that it was necessary that the member banks realize at least 2½ percent interest on new loans which were extended in order to meet running expenses, and be protected against the risk they were taking, but that a 2 percent positive interest rate was necessary to induce entrepreneurs to make loans at the given time, and decreed by the Reserve Board.

It is herein suggested then that in fairness to the member banks that the difference of one-half percent in interest be made up by the Reserve banks upon authorization of the Reserve Board, debiting the business-stability account, and crediting the member bank. (The member bank would thereupon receive a note from the Reserve bank. The face of the note would be the amount of the interest charge in dollars, and this would be gradually liquidated by the Reserve bank by extending credit for the amount of interest as it became due from year to year. These credits, what ever the amount in dollars, would extend over the period of the loan made to the entrepreneur.)

It must be remembered that timing of the additions in the flow of dollars is of foremost importance, and nothing must be permitted to stand in the way of performance, nothing which might preclude the adjustment in the flow of dollars from either the viewpoint of the private banker or the entrepreneur. The interest rate is of secondary importance to the economy as a whole. The major thing is the adjustment in the flow of dollars at the time and in the amount needed to maintain business stability.

With a profits economy functioning under scientific money rules the risk of the private banker would be minimized, but a certain margin for protection against bad judgment is necessary as well as for covering bookkeeping, check handling, and return on investment. If these charges are not met in one manner they must be met in another, or else result in an ill-managed business enterprise. The latter cannot be tolerated in so vital an institution in our economic life.

I cannot concur with the statement made by Owen D. Young in his testimony before this committee when he said, "everything which can be done by the Federal Reserve System to relieve the depression either has been done or is now being done." If he had said that everything within the limited imagination and understanding of the leaders of industry and finance, and within the powers of the officers of the Reserve System then I would agree with him.

The powers now sought by Governor Eccles should not, and I believe are not only intended to prevent another credit runaway, but for purposes of rapidly regaining prosperity. Unfortunately the instruments for effecting recovery in the banking bill are weak and inadequate; especially so now.

The Reserve Board if equipped with the proper tools (suggested in the amendment) can make it so attractive to business men (entrepreneurs) by the use of the business-stability account (negative interest rates) that they will borrow. Tactics can be employed which will remove any hesitancy, or apprehension on the part of entrepreneurs to go into debt to put the unemployed back to work, and take up some of the vast reserves which the banks are anxious to lend. The motive would be gain.

A great emergency exists today and title 2 with revisions as I have suggested should be passed without fail in this session of Congress. It will not retard, but to the contrary, speed recovery. It is a constructive plan for progress and stimulation of borrowing from our commercial banking institutions, by a group of borrowers with whom the member banks are accustomed to do business (no entrance into real estate or mortgage loans wherein officers of banks lack business experience).

If the suggestions proposed in my amendment to the banking bill are understood then open-market operations would be completely abandoned as an instrument of monetary control. The authority over reserve requirements would be used only to permit a scientific adjustment and a curb in the flow of dollars; it is very likely that member banks would maintain their minimum legal reserve. The broadening of the eligibility of paper for rediscount would be intended only to protect against runs on the banking institutions, purely for emergency purposes to protect against the accumulation of dollars by individuals through fright, etc., at any rate not as the instrument to encourgae member bank borrowing. The rediscount rate would be high to discourage rediscounting excepting

[4] Rate to be established by the Federal Reserve Board.

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for emergencies. The lowering of reserve requirements would permit the adjustment in dollars as mentioned previously. The business-stability account coordinated with interest rate charged by member banks on loans would be the real tool for securing adjustment of the flow of dollars to maintain business stability; compensate for the action of indirect "capital" formation by saving within the community; for accumulations of dollars by individuals through habit or fright; for the increased flow of goods or services necessary to perform our function as a creditor Nation, a double-edged instrument. As long as general unemployment was with us the attack would be through inducement of loans to industry (negative interest rates) and not through grants to the Government.

Failure to adopt scientific money rules will undermine the political and economic structure of the Nation. We do not have to call upon social justice and morality to solve our economic problem but simply obey physical laws and combining this with common sense. These are days of grave doubts and confusion because those who are controlling our economic policies do not understand fundamentals, fundamentals in economics as applied to our present pecuniary arrangements within the Nation. Instead of business men "fighting" as Gen. Hugh Johnson recently implored them to, they should first think cleanly in terms of fundamentals and then act. Then a sound prosperity, in keeping with our democratic principles, will be attained.

Now the question will be asked, maybe it has not yet risen in your mind, How will the credit on the books of the member banks, which is the counterpart and which has been originated by debiting the business-stability account of the Federal Reserve System, be repaid (retired or cleared from the books of the member banks)?

Here again it is necessary to remember the physical concept of flows. The new dollars were originated in order to adjust for the increased flow of finished consumers' good brought about through indirect "capital" formation. As long as this flow is maintained there is no physical need for retiring the credit (the dollars) nor can the specific credit be retired excepting if it is immediately recreated in a loan to someone else within the community. To violate this principle would result in injury to entrepreneurs in general.

Now there are sound reasons why expansion of dollars justified within a nation, and effected by crediting dollars to the account of individuals, corporations, cities, or States should be repaid to the economic system as a whole, or remain as a debt to the banking system, but inasmuch as the whole community, bankers, bondholders, stockholders, wage earners, salary workers originally benefited through the expansion (or new credit emission) there is no social justification for taxing the entire community for the dollars debited to the business-stability account so that they may be reloaned to a private individual for use.

The answer to the question then is, That as long as the flow of goods is maintained the credit will rmain open (this will not interfere with the individual member banks balancing their books), as will the debit in the business-stability account of the Federal Reserve System.

The matter of maintaining an unbalanced budget, when it is necessary to maintain business stability, and meeting the deficit by borrowings from the commercial banking system which it is as mechanically correct as grants made from a business-stability account to entrepreneurs through negative interest rates or to the Government, is psychologically wrong. It is negative to the entrepreneur. He hesitates to use savings offered him for use, because he envisions Government borrowing as requiring future taxation, which in turn might seriously jeopardize his employing the savings profitably.

It should be clearly understood that in making the adjustments in the flow of dollars the Federal Reserve Board is not engaged in fixing the prices of commodities. The selection of, and the price of goods would still be a matter of individual bargaining between the entrepreneur and the individual. The Board would just be making adjustments which were necessary because of the changes in our economic structure, such adjustments which were necessary to maintain the proper relationship between the parts (between the flow of goods and the flow of dollars) to assure security of property and individual opportunity. In this everyone would be the gainer. The development of financial institutions as investment banks, life-insurance companies, investment trusts, etc., have modified our economic system over that of our earlier or more primitive period.

It will be observed that in the adoption of the amendment we have within the hands of the Board a positive double-edged instrument for maintaining business stability. If entrepreneurs do not desire loans our system can still be kept in balance.

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There are some who would possibly oppose the method of making grants to the Federal Government, claiming that it would be so easy to pay debts. We would not be using the central bank credit to finance the Public Treasury. I would remind the Senators that this action is only intended to compensate the action of thrift. The latter being a process of individual self-denial, the additions would be limited.

In making the grants from the business-stability account for education, science, arts, etc., we are not fostering the theory that the people should look to the Government for support. The grants have to be made for a purpose which benefits the whole Nation, not a class, and where they will do the most good, give vitality, and stimulate progress in a democratic nation. I believe that governmental support and encouragement of scientific labors, free from political control, would repay the Nation many times over.

In conclusion, in regard to the grants to the Federal Government, let me say that it would be false to state that in the neutralizing introductions of money which are made to maintain business stability that because they are devoted to socially desirable ends we are gliding into acceptance of the theory that when the Government wants money it is not necessary to go out and borrow it, or raise it by taxation, but that it is only necessary to telephone the Bureau of Printing and Engraving to send up another truck load of money.

What we are embracing is the recognition of the fact that most of the economics we have been taught and which has been guiding our industrial leaders and legislators has been static in concept; that the theorizing did not embrace the pecuniary profit-seeking economy existing today, wherein in the main indirect "capital" formation predominates; that the classical economics while it provided entertainment; mental exercise, was but a diversion into a land of make-believe, not realistic; further that it is urgent that we protect ourselves and not subject ourselves to pummeling just to prove we can take it; further that if we continue artificial production control we are frustrating science and the possibility of attaining the higher standard of living which science can provide, yet if we eliminate production control with our present unscientific monetary rules we will again be fighting between ourselves in the dark, which will lead inevitably to despair; finally, that our trouble does not arise fundamentally through error or misjudgment on the part of managers of the banking system, but a failure to know the money rules, have the instruments to carry them out, and use them, all of which cannot be righted by firing the present managers.

The business-stability account is a recognition of the fact that we are in an economic system wherein "capital" formation in the main is indirect, a recognition that investors will only be rewarded provided the entrepreneurs can dispose of the goods in general offered for sale and recover money costs; a recognition of the fact "capital" formation is induced by the entrepreneur only if he believes he can use the dollars profitably which are offered to him.

Gentlemen, in effecting the change in the banking system which is recommended in this amendment we are not destroying or modifying democracy. Rather, we are just adjusting the functioning of our money system to the complex industrial organization (indirect "capital" formation), which did not exist in the simple life of an earlier day. There is no need to alter the fundamental form of our society. There is a great difference between putting in 8 hours at work and doing 8 hours of work as anyone versed in industrial activity can attest to from personal observation and experience. It seems a personal incentive of gain is needed to bring out initiative and ambition in individuals. It is then "gain" which is the mainspring. And even then, only comparatively few are capable of planning their own work to good effect. This requires an expert knowledge in production methods, organization ability, and marketing for which entrepreneurs are paid. It is this mainspring (gain), which this amendment protects.

By effecting the adjustment recommended herein the paralyzed state of the market for new bond and stock issues will be remedied because those receiving income in excess of what they need for their own gratification will be induced to invest their dollars (the profit motive will be the inducement), and entrepreneurs will be induced to use these dollars for "capital" formation. By these methods the heavy industries will receive the needed impetus for revival.

As long as we have an unsound money system (one which does not obey scientific money rules) all the benefits arising out of regulation of securities will be for nought (at least lessened) because under those conditions the most honestly financed industries cannot be assured to give a reasonable return to the investing public. Further, even should we succeed in restoring prosperity it cannot be maintained, made permanent.

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The proposed amendment represents the simplest and easiest method of meeting the new conditions and of eliminating the check (leash) on production. If industry were to have but this one objective in its platform, striving for it unrelentlessly with all the energy it is dissipating on trying to counteract consequences arising from this abuse it would quickly enjoy the prosperity, freedom of action, which have been realized but in rare intervals. If these leaders of industry will but think this problem through, instead of engaging in but wishful thinking or the establishing of production rules which science and human inventiveness will quickly wreck, they will put an end to our economic paralysis.

This is not an "easy" money doctrine, but a positive instrument to guarantee against a repetition of the disaster which took place in 1929. I believe that the amendment is conservative in the sense that it is practical, and that it is liberal in the sense that we are no longer living in an era (economy) wherein everyone owns his own "capital", produces, and markets his product, and we are meeting todays problems on theorizing and methods adjusted to the practical facts of today.

Our economic and social security is dependent on sustaining (freeing) our productive machine and these measures provide the simple instruments for accomplishing that end. This amendment prevents the exploitation of legitimate business, the savers, and the workers in industry. This it is the right and duty of Government to adopt. These measures remove the artificial brakes upon individual initiative and enterprise through which alone private employment can be expanded. It would then be possible to discontinue those temporary measures as the National Recovery Administration and Agriculture Adjustment Administration, and grant the fullest practicable freedom for the individual to conduct his business without interference by the Federal Government.

I maintain that by reason of failure of Congress to exercise its constitutional right, which is mainly due to the ignorance of its members in dynamic economics—the physical implications of indirect "capital" formation in a profits economy—the constitutional right of citizens as guaranteed by the amendment to the Constitution, article 7th, is being and has been constantly violated. This article literally interpreted means that no person shall be deprived of life, liberty, or property without due process of law. When a Congress fails to see to it that its money system obeys scientific money rules then it is collaborating, not willfully, but none the less, in confiscating the property of individuals without due process of law, depriving individuals of incomes from investments which property through the inactions of Congress is made worthless, and is depriving individuals of the opportunity to earn a livelihood or their economic liberty.

We have had a depression not because of the selfishness of man, the cussedness of industrial leaders, or the dishonesty of bankers. The way to recovery is not through moral regeneration. We must not look at this problem from a sentimental viewpoint because that will hamper our vision. Nor have labor-saving devices, or the World War, or tariffs been the fundamental cause of this depression as some people would like to have us believe. We are undergoing this depression not because we are bankrupt as far as resources are concerned—manpower, plant, technical training, and raw materials—but because we have money rules which are scientifically unsound. They will pull us down again unless they are made scientifically sound. There is no need for privations. Our master, whether we be business men, workers in industry, widows who clip coupons, or farmers in the field, is ignorance. Rout this and we tread forward steadily with the advance of science.

Gentlemen, I repeat that it is my contention that provided the Reserve Board is granted full power and responsibility to initiate, adopt, and enforce open-market operations it is still impotent to cope with the problem in the most efficient or effective manner, and with the least possible disturbance to our economic system. The instrument is as crude in the performance of its function as attempting to hit a baseball with a broom handle.

I am in accord and in sympathy with centralizing the responsibility for the exercise of the powers which control the establishment of business trends, but deplore the ineffectiveness of the controls, and favor the substitution of more effective methods. To fix or "nail down" the responsibility is excellent, but the body (the Board) should be equipped with the proper tools to perform the task.

I offer my amendment to provide these double-edged tools. I believe that it is in keeping with the principle and spirit of the Constitution as stated in the preamble, as an effective means to assure justice, domestic tranquility, promote the general welfare, and secure the blessings of liberty to ourselves and our posterity.

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GENERAL REMARKS

There are some bankers who are protesting a greater measure of control. To those who would suggest amendments to the banking bill which would retain most of the existing autonomy of the Reserve banks with proportionate lessening of powers for the Federal Reserve Board the expression "some men learn and live, others only live" can be fittingly addressed.

If you would write a prescription directing that a research moratorium be declared; of stopping progress, then you need only sit by and permit things to take their course. That is resignation to defeatism at its worst, and not statesmanship. Those of us in the engineering profession who understand the problem do not intend to follow such a procedure, but will subject intimate beliefs and practices which are employed to scientific scrutiny, helping in whatever manner we can to effect practical remedies.

It is short-sighted for the officers of banks, or their stockholders to consider their business as a purely individualistic enterprise. The functioning of money is a matter which concerns every individual, and every corporation and every business, large and small. These new measures safeguard the banker against the evils which have repeatedly been his undoing, and will continue to do so, overcoming his best judgment. What bankers should do is to concentrate on the design of instruments of control which will be most effective to maintain business stability. Unless they cooperate and agree to reasonable measures the Government will have no other alternative but to purchase the stock of the Reserve Banks.

It is true that the Government owns not one dollar of stock in the Federal Reserve banks, but it has a vital interest in their proper functioning. With these measures the member banks are not being forced to lend their money to an entrepreneur or to the Government, nor are they being dispossessed of their property.

If giving the power and the instruments to a body within a nation which will enable our industrial machine to operate and enable it to continue to operate at full speed, free from governmental meddling, free from regimentation and snooping; and which will grant ample work opportunity to our people and enable them to regain their self-respect (economic liberty); which will permit the full expression of human initiative and curiosity; which will enable free selection of goods by individuals; which will assure steady profits to entrepreneurs and protect the investments of individuals against confiscation; which will provide a firm basis for security in old age; if giving powers to a body which will assure this is a grant of despotic power it surely is a benevolent form of despotism. Control we now have, though unintelligent. We are just substituting more scientific methods.

The establishing of negative interest rates by the Reserve Board would be in the public interest in order to—

(1) Restore and maintain the economic liberty of the individual citizen within the Nation, open up work opportunity sufficient to enable him to gain a wide selection of work, and under remunerative conditions;

(2) Maintain domestic peace and tranquillity, minimize industrial disputes and their accompanying disorders;

(a) Cutthroat competition eliminated;

(3) Prevent the taking of the property of investors (savers) without due process of law;

(4) Remove the obstructions to the free flow of interstate and foreign commerce, permit foreign citizens and nations to repay their obligations to our citizens, and gain the widest selection of goods; and

(5) Permit science and the scientific professions to fulfill their function as a benefactor of society.

It is a step which is necessary because of the nature of our economy, a profits system wherein, in the main, "capital" formation is indirect. It maintains the Reserve system as an agency intended to accommodate industry, commerce, and agriculture not in a passive, but in an active roll. There is nothing "planned" about it excepting that the system is made to conform to scientifically sound principles.

If the method of negative interest rate on loans were undertaken now and acted as a tax, increased the price of consumers' goods over what they would otherwise be, it would be constitutional in that it did not discriminate against anyone, but was borne by the public in general. The recuperative efforts would be in a manner consistent with the authority granted by the Constitution, acting as a stimulus in starting the forces making for expanding commercial activity.

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It would be an inexpensive method of relieving the burden of relief, much more inexpensive and effective than public works projects.

Our present money rules in this Nation became obsolete from the inception of the industrial revolution in the late eighteenth century, but the evil effects were not so pronounced then as they have recently become because we were primarily an agricultural Nation. We were a Nation wherein individuals in the main performed the triple role of (*a*) producer of goods, (*b*) capital owner, and (*c*) marketer of goods.

Mechanization and indirect "capital" formation developed slowly. It was only beginning about the middle of the nineteenth century that decided progress began to be made in the practical application of scientific discoveries. But upon the beginning of the engineering professions in the last quarter of the nineteenth century and the accompanying research which followed, the importance of scientific money rules were destined to play an increasing role, and failure to adhere to them to cause depressions of increasing severity.

Scientific money rules grew in importance with the industrial development of this Nation because industrial efficiency demanded specialization and large expenditures for equipment and goods in process; this required the pooling of large quantities of dollars from savers scattered all over the Nation.

The rapid development of investment banks, life-insurance companies, investment trusts, and the further developments in science and the scientific professions and the increased specialization in industry since the establishment of the Federal Reserve System have intensified the need for obeying scientific money rules. The repercussions which follow their violation now intimately effect everybodys welfare. We no longer can run away and hide ourselves in an environment where we can barter goods and services; nor is there a need for following such an unintelligent procedure.

We cannot hold on to the present money rules without suffering periodic business convulsions, confiscation of property of individuals and widespread unemployment. The banking bill of 1935 is intended to cope with this problem, prevent the undermining of our economic system. Unfortunately, the instruments of control are weak.

Please understand, gentlemen, that I am not expounding or endorsing the theories of Major Douglas—the A+B theory. I maintain that under our present monetary system (the present money rules) the flow of dollars may be sufficient; may be in excess; or may be deficient to enable the disposal of the flow of finished consumers' goods in general offered for sale at prices covering the total of money costs (plus a fair profit) incurred in their production.

It must always be borne in mind that the primary object of making the expansion of dollars is not to create employment, but to adjust the stream of dollars so that the flow of goods is not impeded, so that finished consumers' goods in general offered for sale by industry can be disposed of remuneratively. The purposes for which the expansion of dollars are utilized (used) is of secondary importance.

The adjustment of the flow of dollars is vital to prosperity, outside the control of industry, but not of the community or Nation. Good and bad trade in general are but conditions resulting from ignorance of the community in knowing how to control or adjust the flow of dollars. We can, of course, permit supply and demand to work themselves out, but not without periodic convulsions within the Nation. By exercising a positive control over the flow of dollars the simplest and most effective instrument is being utilized over economic environment.

It cannot be overemphasized that in order to understand the functioning of our economic system we must have the proper physical concept, not only in terms of flows (flows of goods and flows of dollars) but also in terms of changes of flows. Then we must bear in mind how these changes in flows of goods are effected. We are in an economic order which is based on the private ownership and operation of industry, conducted for profit. The formation of "capital" is, in the main, indirect (the savings of individuals are utilized for "capital" formation only providing an entrepreneur is assured that he can make a profit through the use of the savings—can make a profit off of new plants, machinery, etc.). Then we must bear in mind that in the production of all goods that minister directly to the satisfaction of human wants (consumers' goods) the attainment and maintenance of an increased flow involves a fixed investment in "capital" as well as a fixed investment in consumers' goods in the various stages of fabrication. Finally, if we would understand our present predicament we must understand the institutional arrangement and present money rules which govern expansion and contraction of dollars (must understand the functioning of our commercial banking system).

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It should not be so difficult to see what physical actions are necessary to counteract the instability caused by the indirect method of "capital" formation. The latter results in an adjustment in the flow of goods (an increased flow of consumers' goods) in which—the increase in flow—definite money costs are borne by entrepreneurs, and which costs must be recovered in goods in general offered for sale. No one questions that stones are sure to fly if he kicks them, or that he is certain to be injured if he fails to leap out of the way of an auto which is bearing down on him. Then why stand by idly and be punished for violating the physical factor of indirect "capital" formation instead of positively correcting (adjusting) the flow of dollars so that the increased goods flow can be disposed of remuneratively.

(The following statement is from Robert B. Warren, economist of Case, Pomeroy & Co., New York City, who was invited to appear before the committee to speak for a large number of political economists in protest against title 11 of the pending banking bill. Hearings having ended before Mr. Warren was called, the chairman of the subcommittee is presenting his statement for the record:)

STATEMENT OF ROBERT B. WARREN, NEW YORK CITY, N. Y.

In one sense, the Banking Act of 1935 is a routine measure. In its two central themes, namely those relating to the activities of the Reserve system in what are called "open-market" operations and those defining the nature of the currency, it does no more than clarify and perpetuate de facto actualities. These de facto actualities represent gradual and evolutionary developments over the 20 years since the establishment of the Reserve System. Even those which have the appearance of innovation (specifically, for example, those defining the relation of the currency to gold) prove, upon even superficial examination, to trace their origins considerably earlier. They have developed gradually and cumulatively; and it is only by retrospection that we can recognize that the entire nature of the Federal Reserve System has been revolutionized. By a succession of small turns, each dictated by the exigencies of an immediate situation, we have reoriented our course so completely that we are now proceeding in a direction exactly opposite to that which the Congress, under the leadership of President Wilson, laid out 20 years ago.

The original Federal Reserve Act was devised to give the United States an effective gold standard. The proposed Banking Act of 1935 is devised to give the United States a managed currency, almost completely divorced from gold. But in the twenty-odd years between December 28, 1913, when President Wilson signed the Reserve Act, and the present time, the original act had been so amended, its basic principles so obliterated, the actual relation of the currency to gold so obscured, that when the people of the United States and the Congress of the United States are presented with a bill definitely and finally renouncing (I might almost say, denouncing) the basis of the original act, it is presented by the drafters and accepted by the Congress, the financial community, and the people, as a routine administrative measure. Such objections or suggestions, or even questions, as have been offered at these hearings have mostly related to matters of detail—whether a given board should consist of X members or Y members, whether a given type of credit should be X percent or Y percent of a given sum.

It may be that I exaggerate the importance of monetary problems in the function of government and functioning of economic society. But I cannot regard a fundamental change in our monetary policy as a routine matter. Nor has Congress previously so considered it.

The passage of the original Federal Reserve Act was far from a routine matter; although it involved no fundamental change from the familiar and long-established monetary system. The Congress of that period considered the matter of sufficient importance to provide first for an elaborate study of prevailing systems, practices and theories, and second, a deliberate debate upon every major item of the bill. The record of the study was published in the encyclopedic report of the National Monetary Commission, which I venture to say a century hence will still be studied and quoted as a compendium of the monetary wisdom of the race.

Cynics often quote the philosopher Hegel: "What experience and history teach is this: That peoples and governments have never learned anything from history, nor acted on principles derived from it." But for once at least Hegel was wrong; for the Congresses of that period, when they undertook that major legislation, drew upon history, and were guided by it. As I said before, the original

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Federal Reserve Act involved no basic change in our money system, yet Congress deliberated over it for a good part of a decade.

The definitive abandonment of metallic money and the adoption of what is called a managed currency is a major decision, in comparison with which the passage of the original Reserve Act was simple. That involved no more than the perfection of a familiar and well-tried standard. The formal adoption of managed currency carries the United States into the unfamiliar and the experimental.

Mere abandonment of the gold standard does not create a managed currency. It might create instead monetary anarchy. The concept of managed currency, from Aristotle to the present, has run through a long history. There is a long and controversial literature on the subject. The fact that irredeemable paper has tried many times in many countries, and invariably with consequences ranging from the unfortunate to the disastrous, has never deterred adventurous minds from speculating on the possibilities of an ideal money, free from the vagaries of the prospector's pick.

Since 1929, several of the theories of the managed currency school have been put into effect, notably, artificially low discount rates and large open-market operations, both prior and subsequent to our abandonment of gold. In no case, was the economic consequence comparable to the indicated hopes of the proponents. This would suggest that something was lacking either in the theory or the technique. But neither the debates in the Capitol nor the hearings on the bill have adverted to that obvious, if disagreeable, fact, nor raised the question as to why it should be expected that certain monetary devices which had produced such mediocre results in the past should be expected to produce superior results in the immediate future.

Furthermore, certain economic results which in the past have been claimed for managed currencies, such as the control of the price level, were expressly disclaimed in the testimony before the House committee. Since the claim to the control of the price level is perhaps the commonest and most persuasive argument of advocates of managed currency, this disclaimer must disappoint the hopes of many persons who had believed in this act, Congress was creating a money of such constant value as would permanently establish equilibrium between the status of debtor and creditor. Since the argument that a managed currency can control the price level has usually been rated as the chief reason for adopting it in preference to the gold standard, it seems appropriate to question whether this hope is to now be regarded as vain, or whether the disclaimer is to be understood as remarking a defect in the bill under consideration. If the former be the case, the presumed advantage of adopting managed currency is brought into doubt; if the latter be the case, the bill should be perfected. I do not advance these comments so much in criticism of the proposed measure, as to emphasize my contention that the whole question of establishing a managed currency is one of considerable intricacy; that exponents of managed currency are by no means in agreement either as to its possibilities or its mechanics; and that the bill under consideration far from being a routine measure, subject to debate only in its details, is a piece of major legislation which deserves the investigation and deliberation accorded previously to major acts of legislation.

If my first point is simple—namely, that Congress should thoroughly explore basic question of whether or not a managed currency should be adopted in preference to some other standard, my second is even simpler. The adoption of a managed currency involves the delegation to the managing authority one of the fundamental attributes of sovereignty. It would seem needless to emphasize the fact that it endows this authority, whether termed a board or a committee, with the power to create and to annihilate money. It endows this board or committee with the full power to issue "money and regulate the value thereof." Our Constitution, as recently interpreted by the Supreme Court, expressly gives this power to Congress. It is not to be supposed that this should be interpreted to require of Congress attention to the details of administrative routine; nor to prohibit Congress from delegating details of administrative routine to its qualified administrative servants. For example, Congress has never directly conducted the operations of the mint; it has delegated the actual minting of coins to appropriate administrative officials, acting strictly under authority delegated to them by Congress.

But the power granted under this act far exceeds any power previously delegated by Congress. Under the provisions relating to open-market operations, it absolutely delegates to this group of administrative officials, full power to issue money and to regulate the value thereof, not according to terms and principles strictly defined by Congress, but at their personal discretion. It is true that the original Reserve Act authorized open-market operations; but it authorized them

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only under strict limitations imposed and defined by Congress—namely, that all currency, whether notes or deposits, issued under such discretionary power, must at all times be kept interchangeable with the standard of value prescribed by the Congress itself. It has been decided that Congress has authority under the Constitution to alter the standard of value. It is for constitutional lawyers to question the authority of Congress to delegate to a group of administrative officials the powers to issue money and regulate the value thereof at their discretion. I will question the economic expediency of endowing any committee of administrative or quasi-administrative officials with such a delegation of sovereignty, except in the limited capacity and with the limited authority of agents of Congress.

To me, the much-disputed composition of the open-market committee, whether it should be composed of X members from this group and Y members from that group, or of Y members from this group and X members from that group, is a mere quibble over a routine detail. The essential fact is that if this committee is the agent of Congress, its qualification requires no more than that it should scrupulously, diligently, and with technical efficiency execute the will of Congress. If, on the other hand, this committee is not the agent of Congress, then we must concede that Congress has abdicated its prescribed function and has delegated to this committee the soverign power to issue money and regulate the value thereof; and in that event, the composition of the committee still seems to me a secondary matter. I should be equally dubious of the economic merit of intrusting 5 individuals or 7 individuals or 10 individuals with the sovereign power to issue money and regulate the value thereof, at their discretion, whether the individuals appointed were bankers, college professors, farmers, or any mathematical combination thereof. Nothing in my reading of monetary history, or in my experience in financial affairs, has led me to the conclusion that any committee of economically omniscient supervisors exists, to whom could be delegated discretionary power to issue money and regulate the value thereof in such a way as to insure a system equal to, or superior to, the gold standard.

Yet if Congress delegates this sovereign power to a committee as its agent, it seems to me imperative that Congress define the terms and powers of the agency—that it should prescribe guides and standards of action for its agents—in order that their administrative discretion may not conflict with the intent of Congress in issuing money and regulating the value thereof.

Thus I return to my first point. It required long study and arduous debate on the part of Congress to devise the original Federal Reserve Act, which delegated to the administrative officials of the Reserve System relatively simple and limited powers available within the canons of the gold standard. It is an infinitely more difficult thing to frame an act governing the operations of a managed currency. Whether one considers it a merit or a defect, the gold standard, as defined under the original Reserve Act, imposed strict boundaries and limits to discretionary action. Under the system contemplated by the proposed act, all the old boundaries and landmarks are swept away and the area of discretionary action infinitely widened. Assuming the intent to abandon the gold standard to be final, the task before Congress is to set up new norms, standards, and criteria for the guidance of a committee of administrative agents, to guide them in their delegated functions, to the end that their administrative action may conform to the will of Congress in the matter of issuing money and regulating the value thereof.

But I find in the bill under consideration no such concept. In the bill, as presented, Congress is called upon to delegate to a committee its full sovereign power to issue money at their discretion and to regulate the value thereof at their will, except for such reservations of power as are left, not in the hands of Congress but in the hands of the Executive.

My objection to the bill, therefore, does not lie against its details but against its essentials. It is, perhaps, superfluous for me to affirm my personal belief in intrinsic money as contrasted with currency which represents a mere monetization of debt; and to reaffirm my opinion that the original Federal Reserve act, the fruit of years of congressional study and debate, was infinitely superior to the novel forms that in the past 20 years have been superimposed upon it, including the present bill. In this, I do not believe I am stating an individual idiosyncrasy; I believe I am supported by a considerable body of opinion, both academic and practical, impressed, as I am, by the records of monetary history. But I take it that these views are the views of a minority, and that by the majority they are regarded as out of keeping with the age. Evidently it is the intent of Congress and of the people of the United States to complete the break with the monetary past and to establish a new system in the hope that the new system will be better than the old. If this be the case, I can only offer my opinion that the success of

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the new, difficult, and untried system will be proportionate to the study, deliberation, and debate expended by Congress in determining its principles and establishing norms, standards, and criteria for the guidance of those administrative officers to whom, under Congress, will be delegated the power of issuing money and regulating the value thereof.

(The following statement is from Prof. Walter A. Spahr, economist of New York State University, who was invited to appear before the committee to speak for a large number of political economists in protest against title II of the pending banking bill. Hearings having ended before Dr. Spahr was called, the chairman of the subcommittee is presenting his statement for the record:)

Statement of Walter E. Spahr

1. There are no circumstances calling for legislation dealing with the fundamentals of the Federal Reserve System at this time. It appears to be assumed by the advocates of title II of the bill that the proposed changes will enable the Federal Reserve banks in some better manner to aid business recovery. In reply to this apparent assumption, it may be pointed out that there are no powers which a central banking system can employ in aiding a sound business recovery that are not now possessed by the Federal Reserve banks. The arguments for the passage of this title II must, therefore, rest upon other grounds.

The proposals in title II deal with far-reaching fundamentals and should not be undertaken until after a commission of competent experts has made a thorough study of the money and banking problems of this country and, on the basis of adequate evidence and after careful deliberations, has drafted a plan which offers real promise of providing this country with appropriate and workable money and banking systems. Both systems have suffered sad mutiliation in recent years; and what is needed now is careful and deliberate overhauling and reconstruction, rather than further mutilation and distortion such as will result if title II of this bill is passed, particularly since efforts are being made to force its passage in an atmosphere characterized more by a tense emotionalism than by careful and searching examination of the fundamental principles underlying our money and banking problems.

The monetary legislation of 1933 and 1934 was enacted without giving opportunity for careful or comprehensive consideration by the appropriate committees. Some parts of the legislation received no committee consideration. The Emergency Banking Act, for example, was rushed through all legislative stages in a single day. Few members of Congress had an opportunity to read it. Some of the other measures received, at best, only perfunctory consideration. Sometimes parts of bills were scattered among 3 committees in the House—those on Banking and Currency; Coinage, Weights, and Measures; and Ways and Means—and 2 committees in the Senate—Banking and Currency, and Agriculture. These methods of rushing through legislation, which the Administration at the time insisted was pressing in nature, have made it impossible for Congress to give careful consideration to fundamentals and to various implications of much of this legislation. We thus have on our statute books money and banking laws of such a hodge podge nature that it is imperative that a careful study be made in order to give this country a rational money and banking system. To add the provision of title II to the existing chaotic collection of money and banking statutes, many of which either have an emergency character or are fundamentally unsound, would be quite unwise, especially since there are no pressing circumstances which call for such a radical change in the fundamental nature of our Federal Reserve System.

The 3-year limitations in the Gold Reserve Act expire on January 30, 1937. The act provides that authority shall continue for 2 years with power to the President to extend it for a third year. Undoubtedly the Administration will come forward with legislation to be effective at the expiration of the 3-year period. January 1937, is a logical time in which to consider legislation of a permanent character, which will preserve good features of the new laws but eliminate unsound provisions. If a commission were appointed by the end of the present session of Congress, it would have a year and a half in which to make its investigations. There would not be sufficient time before the session of Congress of

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1936. It would be unsatisfactory also to attempt to enact new legislation in the year of the Presidential campaign. Conditions for a proper consideration of the subject would be more favorable in January 1937, after the Presidential election has taken place.

There should be no legislation at this time beyond that necessary to correct technical difficulties, or to remove crude inconsistencies, in existing laws. And even this type of legislation should be undertaken only upon the recommendation of the Federal Reserve Board and in strict accord with specific proposals drafted by the Board.

2. There are other reasons why legislation dealing with the fundamental nature and functions of the Federal Reserve System should not be passed at this time. These are found in the nature of the principal notions which obviously surround the proposals embodied in title II and which provide the excuses for attempting to enact them into law at the present time.

Running throughout the arguments of practically all advocates of title II is the fundamental notion that our money and banking systems were primarily responsible for the depression and also that recovery can be aided, if not actively generated, if only our money and banking systems are changed.

Both notions are fallacious. The depression was caused by the World War and the attendant maladjustments which it created. Abnormalities of almost every kind crept into our economic system after the war as a result of the efforts made to avoid the painful readjustments which the economics of the situation demanded. One of these abnormalities assumed the form of credit inflation. It resulted from the prevailing notion that through installment buying and cheap credit the prevailing apparent prosperity could be maintained indefinitely. Those were the days of the "new era" economics. The stability of the price level, maintained in the face of what we now know were unsound underlying conditions, mislead most people. Only because the commercial banks and Federal Reserve System went long with the notions of the day were they partially responsible for the depression. But the prevailing notions of the day were Nation-wide; they were part of the "new era" economics; they were all part of, or in harmony with, the devices employed to maintain production at an artificially high level on the assumption that a painful readjustment could be avoided. The Government, as well as business men, banks, retailers, and consumers, was responsible for the prevalence of those notions. The whole Nation was involved. Therefore, to single out the money and banking systems, and especially the banks and the bankers, as being responsible, is hardly rational.

In addition to the fact that the World War and the attendant maladjustments were fundamentally responsible for the ultimate collapse, two other lessons should stand out as warnings to the advocates of title II. One is that the price level was maintained at a very steady level from 1923 to 1929, and the other is that underlying it and bolstering it up was a huge credit inflation which finally collapsed. Despite these facts, the chief advocates of title II propose to restore these same conditions, and they wish to employ the same general methods. They wish to inflate the currency to obtain the price level which they think desirable—and this usually means that of 1926—and then they expect to keep average prices at that level by currency manipulation. To do this they hold that the Federal Reserve Board and banks should be brought under the control of the party in power so that these notions as to inflation, price-level stabilization, and currency control can be made effective.

Stated briefly, the lessons as to the causes of the depression do not appear to be clearly understood by the advocates of title II (and of similar proposals) and their notions as to how to generate a sound business recovery involve the reemployment of some of the very devices which contributed to inflation and the collapse and which would lead to a repetition of the same things.

These advocates, who hold our money and banking systems primarily responsible for the crash and who believe prosperity can be aided or generated by changing these systems, also seem to forget that the depression, like the war, was almost world wide. They forget that regardless of the type of money and banking systems in vogue, the depression came and currency systems collapsed. They also appear to ingnore the fact that the losses and sufferings were most severe in those countries in which the central banks were brought under the control of the Government and paper money issued. These lessons seem to have no meaning to the advocates of title II who would bring our Federal Reserve System under the control of the party in power and provide the means by which inflation can take place through the conversion of illiquid assets into deposit currency or legal-tender Federal Reserve notes.

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These advocates also fail to understand how a sound business recovery starts itself, and just what part a Government and central banking system may play in aiding a sound recovery. They do not understand that a rise in the price level which accompanies a sound recovery is radically different from the rise in prices which is caused by currency inflation. They do not seem to appreciate the fact that the former is a sound rise in prices and the latter is an unsound one. In short, it is quite clear that they do not understand that there are two types of rising prices, that the causal factors in each case are different, that the reactions of people to each type of rising prices are different, and that the economic consequences flowing from each type of rising prices are very different. To them all rising prices are alike. That idea has been underlying all the monetary legislation of this Administration. Professor Warren expressed the common notion when he said "The effect of rising prices is the same regardless of cause." (See his Prices, 3d reprint, revised, p. 371.) This same confusion of thought, but in a different form was revealed by Governor Eccles, to use but one illustration, in his testimony before the House Committee on Banking and Currency (Mar. 13, 1933). Asked regarding the nature of inflation, Governor Eccles replied: "The difficulty is that so many people, when you say inflation, think it is something unsound; they think of worthless money. What I mean is that a rise in the general price level, in employment, and improvement in the business situation, from whatever it is, would be inflation, no matter how small the extent."

It should be emphasized that the causal factor in a sound rise in prices, which accompanies a sound recovery, is the increased activities of producers, particularly those in the heavy goods industries, whose inventories and costs are reduced sufficiently to enable them to resume operations at a profit. This condition comes about as a consequence of the persistent though declining purchasing which takes place during the business recession and depression. On the average 3½ years will tend to bring about such a condition; and, as a matter of fact, the middle of 1932 seemed to show that recovery was ready to start and might have maintained itself had not other strong and overwhelming factors intervened. It also should be emphasized that as the activities of these producers increase, their loans at banks increase, and deposit and other currency are drawn into circulation. It is for these reasons that the amount and velocity of currency in circulation increase under conditions of a sound recovery and are a result rather than a cause of increased business activity.

The unsound rise in prices, on the other hand, is caused by currency inflation. Indeed, inflating the currency is the only certain way known by which a currency can be made a positive causal factor in raising prices. Since devaluation of a currency is not inflation, but is the adoption of a new standard unit of less weight, there is no known predictable relationship between a given amount of devaluation and the effect on the price level. The effects of devaluation are on foreign exchange parities. Inflation takes place on the basis of the prevailing currency unit and does not affect foreign exchange parities, but it does have an effect upon the price level.

Under conditions of a sound rise in prices a feeling of widespread confidence is generated because it is based upon increased productive activity, increased employment, increased wages, and increased prices. Prices are pulled up as a result of the increased demand and because the demand runs ahead of the supply of goods in stock.

Under conditions of an unsound rise in prices, caused by inflation or the threat of inflation, a feeling of widespread fear is generated. People rush to purchase not because there has been increased production, or increased employment, or wages, or increased income, but to save what they can of their savings from the devasting effects of a depreciating currency. They draw out their savings and borrow and buy if they have property on which to borrow. It is startling to notice that the Governor of the Federal Reserve Board, in his testimony before the House Committee on Banking and Currency (Mar. 14) said it was a fear of the currency which is desired. To be more exact he said: "Inflation can only be brought about by the willingness of the people and corporations to borrow money and that is one thing we are trying to do. We are trying to induce the borrowing and lending of money upon which recovery is based. We are talking about the fear of inflation or reflation when as a matter of fact that is what we want."

This illustrates once more the fact that the Governor is confused in his thinking on these fundamental points. He does not recognize the difference between a sound and an unsound rise in prices and he fails to distinguish the causal factors

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in each case. It is for this most fundamental reason that the Governor's advocacy of the proposals incorporated in title II are fraught with such great dangers for this country.

Under conditions of a sound rise in prices the ultimate economic consequences tend to be a state of economic equilibrium and a condition of widespread prosperity. It is the best condition of economic affairs known to human beings. It is the condition for which we should strive. A sound rise in prices is the only kind known which need not, of necessity, culminate in an aftermath of liquidation.

Under conditions of an unsound rise in prices, caused by currency inflation, a state of economic equilibrium can never be attained; only heavy losses in some form can be the ultimate result. This disaster can take any one of three forms: (1) There will be a business collpase if inflation is halted; (2) repudiation may follow upon the extreme inflation of the currency; (3) devaluation may be the ultimate device used to peg an inflated currency in order to avoid the collapse or repudiation and to obtain a new starting point for working toward a new equilibrium. In every case severe losses are suffered; and it is for this reason that there is no sound argument which can be offered in behalf of currency inflation.

Yet the advocates of title II, in the main, overlook these fundamental facts and propose to aid recovery, which they confuse with an unsound rise in prices, by providing the means for pumping additional supplies of currency into circulation.

Another aspect of the unsound inflationist theories lying behind title II is seen in the notion presented to the House Committee on Banking and Currency by the Governor of the Federal Reserve Board to the effect that there is presumed to be a causal connection between national income and the amount of currency in circulation. The obvious flaw in this most unsound theory is that the national income of the German people must have been phenomenal as the amount and velocity of their currency reached their peak. Nevertheless, this riduculous notion, to the effect that the national income is determined in this manner, is being used by some of the chief advocates of title II as a basis for urging that it is necessary to put more currency in circulation and to increase its velocity in order to enlarge the national income.

It should be understood that in a normal expansion and recession in business both national income and currency supply and its velocity are the resultant factors; that an increased monetary income, resulting from currency inflation, as in Germany, is something radically different from an increase in real national income; and that the velocity of a currency which accompanies a currency inflation is a type of velocity differing from that associated with a sound rise in prices. An inflation velocity may be a fear velocity and is likely to be much sharper in its ups and downs than is the velocity associated with a noninflated currency. This attempt to relate the supply and velocity of currency to national income has been advanced by Governor Eccles and by Mr. Robert Hemphill, an inflationist, who recently wrote some articles for the Magazine of Wall Street (Oct. 27 and Nov. 10, 1934, issues) and for the New York American. Dr. Currie, Assistant Director of Research at the Federal Reserve Board, in his book, The Supply and Control of Money in the United States (p. 6), relates the currency supply to the country's aggregate money income and employs the concept of income velocity. This concept obviously is not the same as that of the velocity of currency, but it has confused some of those who have attempted to relate the currency supply and its velocity to national income. Real national income is not the same as national income in terms of money; and the concept of income velocity has no value in reality. Indeed, the notion has had the unfortunate effect of misleading the inflationists.

These points are mentioned so that the nature of some of the philosophy lying behind this title II may be more clearly understood. This section of the banking bill is supported in whole or in part by the ardent economic planners, by the inflationists, by the managed currency advocates, and by those who believe a government can spend a nation into a state of recovery and that the Federal Reserve System should be so adapted as to make it easy for the Government to use the Federal Reserve System to finance the former in its borrowing and spending program. The fundamental purpose, in title II, in its final analysis, is to convert the system into a politically controlled agency of the party in power so that these purposes can be accomplished.

In title II are also found misconceptions as to (*a*) the proper functions of central banking systems, especially with respect to the appropriate relation between a nation's central banking system and Government financing; (*b*) the appropriate functions and powers of the central banks with respect to the control

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