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THE AMENDMENTS TO THE FEDERAL RESERVE ACT IN THE MCFADDEN BILL REFERRING TO
BRANCH BANKING.

The McFadden Bill (H. R. 6855) has been announced as a bill drawn for the purpose of liberalizing the National Banking Act, so that National banks may no longer be prevented by law from performing banking functions regarded as useful and sound in principle which State banks have long been performing. The Comptroller of the Currency has noted the fact that State banks have steadily gained in numbers and in resources while National banks have failed to maintain the same rate of growth. Since January 1, 1913, he tells us 173 National banks, each with capital of over \$100,000 have given up their National charters and taken out State charters.

These facts are indisputable and in so far as the bill confines itself to its announced purpose I have no criticism to make of it, further than to state that some of the departures from commercial banking need very careful consideration. One of the liberalizing provisions of the bill has to do with branch banking within city limits, and with this provision the Federal Reserve Board is unanimously in agreement. I think I may fairly add that the members of the Board regret that this liberalizing feature of the bill does not go to the full limit of permitting the establishment of branches in all cities large enough to have need for outlying banking facilities, as a matter of right and without regard to the limitations of State laws. It would seem that the National banks might sometimes be permitted to take the lead in a matter of sound banking which every competent banker and every economist approves.

So much for the liberalizing, or modernizing features of the bill, designed to permit banks to transact legitimate business along sound lines by modern methods. We can all get behind and support these features, these amendments to the National Banking Act. But the bill doesn't stop there. It seeks to amend the Federal Res-

serve Act, and here it becomes repressive and reactionary. Because many bankers are opposed to any further liberalizing of the National Banking Act the bill seeks to deprive state bank members of the Federal Reserve System of some of their charter rights guaranteed them under the Act of June 21, 1917, particularly with reference to branch banking. Certain states permit and even encourage banks of sufficient capital to establish branches beyond city limits, on the theory that the farmer is as much entitled to the best and safest banking service as the city dweller is. Instead of advocating the same privileges for National banks that these states give their State banks the Comptroller of the Currency has entered into an elaborate argument against branch banking in general, an argument which would, if sound, utterly destroy his city branch banking recommendation if it were not for the development of a very ingenious theory of home rule. The states may, according to this theory, decide for themselves whether banks shall or shall not have branches within city limits, but they must not be allowed to decide whether any branch banks shall exist outside of the large cities - if their banks are to remain in the Federal Reserve System.

There isn't an economist in the country who would agree with the arguments of the Comptroller. Some 322 independent banks have failed in this country since the 1st of January this year(to April 11th), more than two-thirds of them banks with a capital less than \$50,000, and more than seven-eighths of them banks with a capital less than \$100,000. With failures still running at the rate of nearly 100 a month an unprejudiced outsider might be pardoned for thinking that unit banking rather than branch banking is at present in most need of defense.

The Comptroller bases his arguments on two assumptions, both demonstrably erroneous. He assumes, first, that branch banking in this country is wholly a big

city proposition - that the banks in the big cities will establish branches throughout each state if allowed to do so - and, second, that country branch banking, that is branch banking outside of the big cities, is "fostered and protected" by the Federal Reserve System.

The first of these assumptions the Comptroller partly discredits himself in his statement that he has never yet discovered a big banker who wished to extend his institution beyond city limits. I think that is true of the big bankers in Chicago and in most of the great cities of the East. They already do a national business, receiving deposits from and making loans to large commercial and manufacturing institutions throughout the country, without branches. Furthermore they receive deposits from, make loans to, and exercise a certain amount of control over, thousands of small banks all over the country. It is doubtful if they would gain enough more to compensate them for the added responsibility if they were to establish branches outside city limits. But the error of the Comptroller's assumption is fully demonstrated not by conjectures or by the statements of big bankers but by the facts of the development of branch banking in the states which have permitted it. Although the laws of California have provided distinctly for state-wide branch banking since 1909 only one institution has really spread its branches throughout the State, one other has branches covering about one-third of the State and two others cover territory that is hardly more than suburban or contiguous. The overwhelming majority of the institutions engaging in branch banking in California are country banks not located in any of the large cities. Throughout the Southern states branch banking is a country bank proposition, with head offices generally not even in towns large enough to be called cities. The bank having the largest number of branches in Alabama (about 15 branches) is not a

Birmingham bank, but a bank at Decatur. The largest branch banking system in Mississippi, with about 14 branches, has its headquarters at Grenada, and the largest branch banking system in Maryland has its head office not in Baltimore or in Annapolis, or in any town large enough to be called a city, but in Cambridge. In Alabama, Georgia, Louisiana, Maryland, Virginia, North Carolina and South Carolina there are 134 banks operating 319 branches, less than three branches to a bank, and less than a dozen of these banks are domiciled in the larger cities.

Further positive proof of the error of the assumption that branch banking is a city monster which must be chained up lest it spread its tentacles over the whole country is found in connection with the facts which disprove the Comptroller's second assumption, viz: that branch banking is "fostered and protected" by the Federal Reserve System. Of the 134 banks which operate branches in the Southern states mentioned only 20 are member banks, leaving 114 non-members, and these 114 non-members are operating 233 branches, or about 2 branches to each bank. In Virginia there are 2 members operating 3 branches and 22 non-members with 29 branches. The "head offices" are located in such towns as Clintwood, Columbia, Gloucester, Keller, Keysville, Louisa, Staunton, Tappahannock, Urbanna, Wakefield and Williamsburg. Six banks in Richmond maintain branches, but not one of them has more than 2 branches and only one of them, the Richmond Trust Company, of which Mr. John Skelton Williams is president, has a branch outside of the city. One bank in Norfolk has 2 branches both outside the city and one bank in Lynchburg has a branch at Bedford.

Exactly the same conditions prevail in North Carolina and in Georgia, with the single exception of the Citizens and Southern of Savannah, which has branches in Atlanta and Macon. In the section of Tennessee within the Atlanta Federal Reserve

District there are 12 non-member banks operating 33 branches, and no member banks with branches. In the other end of the district one member bank in Memphis has branches, but they are inside the city.

Certainly this Southern development of branch banking is not "fostered and protected" by the Federal Reserve System, since it is nearly all outside the System. But even in California, the great branch banking state, the same thing is true. There are 88 state banks in that state maintaining branches, but only 19 of them are members of the System, leaving 69 outside, and the outsiders are almost all country banks. It is true of course that the member banks maintain the most branches, but when it comes to the question of being "fostered and protected" it should be said that the large branch banking systems, the Bank of Italy, the Pacific Southwest Trust and Savings, and the Security Trust and Savings, have none of them ever been large borrowers from the Federal Reserve System. One of them never has borrowed and the other two only to carry Liberty bonds. During the strenuous months of 1920 and 1921 it may fairly be said that these large branch banking institutions furnished a large share of the reserve funds which were loaned by the Federal Reserve Bank of San Francisco to the independent unit banks.

The restrictive amendments to the Federal Reserve Act are, it seems to me, unfair, as they overthrow the guarantees under which the larger California State banks, and many State banks elsewhere were persuaded to join the Reserve System. We were willing enough to invite them in and offer them the guarantee of their charter rights when their funds were sorely needed, but now that the seas are smooth we propose to repeal the guarantees so far as branch banking is concerned.

It not only seems to me unfair but from every point of view unwise. Every economist favors branch banking as affording the best and safest means of extending

banking accommodations to agricultural sections and small communities. Professor O. M. W. Sprague begins an article on branch banking in the Quarterly Journal of Economics with these words: "Upon few subjects has the consensus of opinion of both economists and financial writers been more general than upon the advantages of branch banking over a system of separate local banks. Its superiority in respect to safety, economy, the equalization of rates for loans, and the diffusion of banking facilities cannot be questioned."

The economists generally agree that branch banking is a matter of most concern not to the big cities or their big banks, but to thinly settled agricultural communities. They believe that our present scheme of extending banking facilities to such communities by means of small weak independent banks, banks with a capital of \$5,000, \$10,000, or even \$25,000, is unsafe for depositors and uneconomical, making interest rates to the farmers higher than necessary. Professor J. Laurence Laughlin of Chicago University, one of the men who had a prominent part in the preliminary work leading to the establishment of the Federal Reserve Act, declared in 1912 that "the maintenance of such conditions necessarily involves some rather serious suffering." Hasn't this prediction been rather strikingly and painfully verified by the great number of bank failures in the Northwest?

Most of the Comptrollers of the Currency have recommended branch banking in some form, and nearly all of them have recognized its superiority either as a general proposition or under certain conditions to unit banking. The first Comptroller, Hugh McCullough, was himself the President of one of the most notable branch banking systems in the country, the Bank of Indiana. Mr. Hepburn refers to this bank as "an exemplary illustration of the efficiency of branch banking as a system." Comptroller Eckles, whose administration felt the full force of the

Panic of 1893 advocated the establishment by national banks of branches in places not having national banks already established. Comptroller Charles G. Dawes who succeeded him recommended branch banking in places with a population less than 2000. Mr. Dawes in an address to Pennsylvania bankers in 1903 spoke against "general domestic branch banking," but in the course of the address frankly admitted that one of the advantages of branch banking would be lower interest rates to the farmers who grow crops having a cash value. Recent Comptrollers have recommended branch banking within city limits as something absolutely necessary in most of our great cities in order to save the National banks of the cities from destruction by state bank competition. Branch banking by counties was recommended by some of them, and was recommended also by the Federal Reserve Board in 1918. In its report for 1922 the Board urged that National banks be given the same privileges with regard to branches that state banks have been given in the branch banking states.

The last recommendation is the only one that will fully meet the situation, so far as the competition of state banks is concerned. If this cannot be carried the Committee might authorize branch banking by national banks in cities where the states limit branch banking to cities, and in counties where states permit country banks to establish branches. Such an amendment would greatly strengthen the country banks in agricultural sections, and would enable the Federal reserve banks to deal with well managed institutions, instead of small banks which often have no fair chance to survive in times of stress.

The argument that branch banking is monopolistic is unsupported by any actual evidence - the evidence on the other hand is clearly to the effect that branch banking increases competition. It is true that the number of chartered banks in

Canada, and the number of joint stock banks in England and Scotland, have greatly decreased, but except in the largest cities there are more banks competing with each other than before. A recent Parliamentary investigation (1923) into the question of banking in its relation to agriculture in England contains this statement:

"Finally, from the point of view of the agricultural community, it is important to realize that, notwithstanding the absorption of the small country Banks, there is, in fact, far keener competition for rural business than ever before; while, in the matter of security to depositors, the amalgamation of the Banks has also been of very great advantage. The old private Banks were always heavily involved in the fortunes of a restricted area and this was a source of weakness at times of local crisis. The Joint Stock Banks spread their risks over a wider area and a greater range of industries, and can better carry periods of depression." (Report of the Committee on Agricultural Credit, p. 22).

Similar findings were made by a Canadian committee, which investigated credit conditions in the Canadian northwest a year or so ago. Furthermore Mr. Frank W. Murphy and Mr. Castleman, a committee representing our own northwestern farmers, testified a few weeks ago that one of the advantages Canadian wheat growers had over the wheat growers on our side of the line was better treatment from their banks and lower interest rates.

Why ignore this direct testimony? And why ignore the direct testimony of the Californians? Can any one maintain that there is less competition among banks in California today than there was before the development of the branch banking systems in that state? Can any one deny that agricultural situations as serious as that now existing in the wheat growing states of the Ninth Federal Reserve District have been handled in California practically without bank failures?

Isn't it rather un-American to express fear of monopoly in a field where the units are so overwhelmingly numerous? "In union there is strength" is an American

shibboleth. Every week brings increased evidence of the lack of strength of the small unit banks in agricultural sections of our country. The states chiefly concerned have tried guaranteeing deposits and every other remedy, except the one remedy of uniting resources, a remedy which has been successful wherever tried.

In conclusion I wish to say that the Federal Reserve Board has directed its division of analysis and research to make a complete study and survey of branch banking in this country, and with some reference also to conditions in other countries. The Board has also recently adopted regulations dealing with branch banking, copy of which I present for the record. I submit that these regulations will take care of the matter adequately and make unnecessary the amendments to the Federal Reserve Act contained in the bill.

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Edmund Platt.