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C O P Y

DEPARTMENT OF JUSTICE

Washington, D.C.

October 6, 1933.

Honorable Walter Wyatt,
Chief Counsel,
Federal Reserve Board,
Treasury Building,
Washington, D. C.

Dear Mr. Wyatt:

There is attached a copy of the memorandum for which you asked, and also a summary of the memorandum. I should like to have both of them returned to me. I will appreciate it if you will have your secretary telephone me in the morning as to the time for our discussion.

Sincerely yours,

(signed) William G. Davis,

WILLIAM G. DAVIS,
Special Assistant to the Attorney General.

W. G. Davis #1
FOR FILES
M.E. Pilger

C O P Y

WGD/HEM

October 5, 1933.

Summary of the Memorandum with respect
to the Proposed Taking of Gold Profit
from the Federal Reserve Banks in the
event of Devaluation under the Thomas
Amendment.

The memorandum is addressed to three principal questions: (1) Whether, in the event of a reduction by the President of the weight of the gold dollar, Congress has power to deprive the Federal Reserve Banks of the profit on their gold stocks; (2) Whether, if such power exists, the profit could be taken under any existing statute, and (3), In the alternative, whether the Federal Reserve Banks could voluntarily surrender such profit. The memorandum first summarizes the gold position of the Reserve Banks as of September 27, 1933. (pp. 1-2.)

It is pointed out (pp. 2-3) that, in general, four legal difficulties arise in connection with each of the three questions outlined above: (a) That unless the Thomas Amendment is valid the Federal Reserve Banks in fact would obtain no profit on their gold stocks, since, if held invalid, the President's action would be a nullity; (b) That, if devaluation were proclaimed and the gold profit taken from the Reserve Banks (or surrendered by them), any action taken thereafter by Congress or the President increasing the weight of the gold dollar might impair the capital of the Banks; (c) That any action taken with respect to the gold profit of the Banks must be considered in the light of the statute requiring the Banks to maintain a fixed gold reserve, and (d) That any such action must be considered in the light of the possibility that it will be challenged by suits brought by the member banks, the stockholders of the Federal Reserve Banks.

(1) The power of Congress to take the profit from the Reserve Banks. (pp.3-8.). The Constitution (Art. I, Sec. 8, clause 5) provides that Congress shall have power to coin money and "regulate the value thereof." It was held in the Legal Tender cases

(12 Wall. 457; 110 U.S. 421) that this clause authorized Congress to legislate with respect to the weight of the gold dollar and that the power was a continuing one. As an illustration of this power it was pointed out that the weight of gold contained in the dollar had been reduced 6% in 1834. (Act of June 24, 1834, c. 95.) The question arises whether the power to confiscate the profit on gold stocks, resulting from devaluation, is impliedly given to Congress by this provision of the Constitution. In other words, may Congress not only change the gold content of the dollar, but also deal with the results flowing from such action, such as the matter of gold profits. We think that the source of Congressional power to deal with the subject of gold profits of the Federal Reserve Banks may reside not only in the grant of power "to regulate the value" of money but also in its power to regulate an agency created by it. Because of the note-issue and other functions given to the Reserve Banks, gold which otherwise could have been brought into the Government Treasury has been diverted to the Reserve Banks. Such legislation might be justified, therefore, on the ground of the peculiar relationship of the Banks to the Government.

We think, moreover, that legislation depriving the Reserve Banks of their gold profit upon devaluation would not violate the Fifth Amendment, provided, at least, that the Banks were secured against loss resulting from any subsequent statutory increase in the gold content of the dollar. While it is true that the Banks are privately owned, they are not primarily profit-making institutions. Devaluation would result in a decrease in their deposit and currency obligations, in terms of gold, and depriving them of their gold profit, upon devaluation, would not, therefore, weaken their cash position.

(2) Whether the gold profit could be taken under any existing statute. (pp.8-12.)

The Thomas Amendment, which authorizes the President to fix the weight of the gold dollar, does not in terms confer any authority upon the President to deprive the Federal Reserve Banks of any gold profit, resulting from devaluation. In our opinion, the Thomas Amendment vests no authority in anyone, even by implication, to deal with the subject. The debates in the Senate upon the bill (H. R. 3835) show that the question whether gold profits should be taken was discussed; that the Chairman of the Committee on Banking and Currency expressed the view that the bill was not intended to cover that subject, and that it could be dealt with later. (Vol. 27, Cong. R_{ec.}, 2555-2556.)

Nor do we think that the President could require the Federal Reserve Banks to surrender their gold, by virtue of Section 5(b) of the Trading with the Enemy Act, as amended by the Act of March 9, 1933. The retention of gold by the Banks is not "hoarding".

Section 3 of the Act of March 9, 1933, authorizes the Secretary of the Treasury to require "any or all individuals, partnerships, associations or corporations" to surrender gold, upon payment therefor of an equivalent amount of any other form of coin or currency. While it could be asserted that the language is broad enough to include the Federal Reserve Banks, it is our view that they could not be required, under this section, to surrender their gold, since the section provides that this authority of the Secretary can be exercised when "necessary to protect the currency system of the United States."

Congress, in legislating on the subject of gold profits after devaluation had been proclaimed, could ratify the President's action, and perhaps thus meet any contention that the action of the President was a nullity, because the Thomas Amendment delegates legislative power to the President. It may be urged with great force that the Amendment is invalid for this reason. The question is important in this connection, since the Federal Reserve Banks would in fact have no profit unless the President's action were valid.

(3) Voluntary surrender of the gold profit by the Reserve Banks. (pp. 12-15.)

The memorandum outlines the details of a plan proposed whereby the Banks voluntarily might surrender their gold profit. (pp. 11-12.) This plan contemplates the purchase of \$3,000,000,000 Government obligations by the Federal Reserve Banks, under subsection (a) of the Thomas Amendment, the purchase price to be paid in gold. The President would thereafter devalue the dollar 50%, and the obligations would be redeemed with one-half the gold paid over by the Banks.

While we conclude that the provision in question does not contemplate nor authorize such a transaction, we think that whether some plan for voluntary surrender of the gold should be

worked out is a matter for the Federal Reserve Board and the Reserve Banks to determine. We observe, however, that the Bank directors might be held personally liable for unauthorized action resulting in a waste of assets. The chief danger in voluntary surrender of the profit is that the Banks could probably not be safeguarded against a subsequent increase in the gold content of the dollar. Also, an impairment of the capital of the Banks probably would result, if the Thomas Amendment were held unconstitutional.

Respectfully submitted,

HAROLD M. STEPHENS,
Assistant Attorney General.

WILLIAM G. DAVIS,
Special Assistant to the
Attorney General.

C O P Y

WGD-jh

October 5, 1933.

MEMORANDUM FOR THE ATTORNEY GENERAL

Re: The Proposed Taking Of the Gold Profit
from the Federal Reserve Banks in the event
of Devaluation under the Thomas Amendment.

The question has been presented whether, if the President exercises the power granted him by the Thomas Amendment to reduce the gold content of the dollar, the profit which would accrue to the Federal Reserve Banks by reason of the increase in the dollar value of their gold stocks could be taken from them by the Government. The purpose of this memorandum is to discuss the questions: (1) Whether Congress has the constitutional power to take such profit from the Reserve Banks; (2) Whether, assuming such power to exist, there is any statute authorizing the taking of such profit, or whether new legislation would be required, and (3) Whether the Federal Reserve Banks voluntarily might give up the profit.

Preliminary to the discussion of these questions, it may be noted that the Federal Reserve Banks have gold stocks, which, at the existing parity (\$20.67 per ounce), are valued at approximately three billion, six hundred million dollars. If the gold dollar were devaluated 50%, the limit under the Thomas Amendment, the book value of such gold stocks would be

increased to approximately \$7,200,000,000. Or, stated otherwise, the obligations of the Banks, consisting chiefly of member bank deposits and Federal Reserve notes, would be reduced 50%, as measured in terms of gold. As of September 27, 1933, the outstanding circulation of Federal Reserve notes was \$2,972,072,000. Section 16 of the Federal Reserve Act requires every Federal Reserve Bank to maintain a 40% reserve against Federal Reserve notes in actual circulation. The gold reserve required against circulating notes, as of September 27th, would be \$1,188,829,000. Section 16 requires also that reserves of 35% "in gold or lawful money" shall be maintained by Federal Reserve Banks against member bank deposits. The deposits of the Reserve Banks on September 27, 1933, amounted to \$2,807,779,000, and their cash to \$231,762,000. Accordingly, in order to meet the reserve requirements against deposits, \$750,960,650 additional gold was required as of that date, making the total of gold required for reserve purposes \$1,939,789,650. The gold reserves on that date were \$3,591,799,000.

In considering the questions presented in connection with the taking by the Government of the gold profit which would accrue to the banks in case of devaluation, there will be certain recurring difficulties which may be here outlined in advance. In the first place, no profit will accrue to the Reserve Banks, upon devaluation, unless it be assumed that the Thomas Amendment is constitutional. If the statute is unconstitutional, any action by the President would be a nullity and the existing parity between the dollar and gold would not be affected by a proclamation reducing the value

of the dollar. Secondly, if the gold content of the dollar were reduced 50% resulting in a book profit to the Reserve Banks upon its gold stocks, such profit would be lost if the present parity between the dollar and gold were subsequently reinstated. Consequently, if the entire profit of the Reserve Banks on its gold stocks were taken by the Government upon a 50% devaluation of the dollar, the subsequent restoration of the \$20.67 ratio would probably result in wiping out the surplus and impairing the capital of the Banks. Third, any action which is taken with respect to the gold profit of the Reserve Banks must be considered in the light of the statutory requirement regarding the maintenance by them of gold reserves. And, fourth, it cannot be assumed that any of the various legal objections to the taking of the profit from the Banks will not be raised merely because the directors of the Reserve Banks assent thereto, since stockholders' suits might be filed by the member banks or proceedings brought by them to hold the directors personally liable.

I. The Power of Congress to Deprive the Reserve Banks of the Profit

The power of Congress, in general, to take gold profits obtained by private individuals as a result of devaluation, would have to be implied from Article I, Section 8, Clause 5 of the Constitution, which provides that it shall have power "to coin money, regulate the value thereof, and of foreign coin . . .", and rested upon Clause 18, empowering it to "make all laws necessary or proper for carrying into execution the foregoing powers"

It seems clear that, under this provision of the Constitution, Congress has power to reduce or to increase the existing gold content of the dollar, and also that the power is a continuing one. In the Legal Tender Cases, 12 Wall. 457 (1870), the Court based its conclusion that greenbacks could be made legal tender for private debts, upon the premise that the Constitution empowered Congress to reduce the weight of gold contained in the dollar (p. 552). It was pointed out that such power had been exercised by the Act of June 28, 1834 (Ch. 95), reducing the weight of the gold contained in the gold dollar by almost 6%. (p. 548, 551-2.) The Court also stated in that case, that the power to regulate the value of the currency was a continuing power, not exhausted by its first exercise. (p. 547.) In the Legal Tender Case of 1883 (Guillard v. Greenmar), 110 U. S. 421, the Court again predicated its conclusion that greenbacks could be made legal tender upon the ground that coins of the same denominations as those already current by law, but containing a lesser weight of precious metals, could be issued by Congress and made lawful tender for pre-existing debts. The Court referred to the 1834 statute and to the Act of February 28, 1878 (Ch. 20), reducing the silver content of the silver dollar. In the former decision (12 Wall. 457, 545), it was suggested that the power given to Congress over the currency might be regarded to be as extensive as the power vested, as an attribute of sovereignty, in the governments of foreign countries. Of course, if this were true there would be little question as to the power of Congress to take the gold profit from the Reserve Banks, but obviously the Con-

stitution imposed restrictions to which most foreign governments are not subject.

Assuming that Congress may reduce the weight of the gold dollar, two constitutional objections could be urged against an involuntary taking from the Reserve Banks of the gold profit resulting from devaluation. In the first place, Congress is given no express power by the Constitution to claim the profit accruing to a holder of gold from a reduction in the gold content of the dollar. In the second place, it might be urged that such action would be a taking of private property in violation of the Fifth Amendment. There are, of course, no precedents which would aid in resolving either question. It would seem, however, that the Federal Reserve Banks are in a less favorable position successfully to maintain either position than a private individual, provided that Congress in taking the profit should safeguard them against any subsequent increase in the value of the dollar. Legislation intended to deprive them of the profit could be rested not only upon the power of Congress to regulate the value of the currency but also upon its power to regulate the Reserve Banks created by it.

Were it not for the Act of March 9, 1933, and the regulations issued thereunder, it would seem very doubtful, as above pointed out, whether Congress, in view of the Fifth Amendment, could deprive private individuals, upon devaluation, of the increased value of their gold in terms of dollars, any more than it could deprive them of the enhanced exchange value of their commodities because of such dollar depreciation. However, the Act of March 9, 1933 (amend-

ing Section 5 (b) of the Trading with the Enemy Act) as effectuated by the Executive Order of August 28, 1933, makes it unlawful, with certain exceptions, for any person to retain title or to hold gold. While it may appear strange to suggest that one act of Congress could impart constitutional basis for another, it is believed that the March 9, 1933 Act may afford a sounder basis than otherwise would have existed for a statute depriving private individuals of any gold profit resulting to them from devaluation of the dollar. At the time of the passage of the Act of March 9, 1933, the currency and credit system of the country was threatened or might have been endangered by large withdrawals of gold into hoarding. This fact affords a persuasive argument in favor of the constitutionality of Section 2 of the Emergency Banking Act. Assuming it to be constitutional, the possibility that a private individual could successfully assert that the Fifth Amendment would be violated if he were deprived of the dollar profit upon his gold (due to dollar devaluation), is considerably diminished. He would be in the position of asserting that he could improve his financial position by having failed to comply with the regulations in effect before devaluation occurred. Of course, the Federal Reserve Banks are not in this position because they are authorized by law to have gold. However, it would seem clear that they could be deprived of the gold coming into their reserves under the Executive Orders, since they should not be entitled, against the Government, to the profit on the gold which private individuals were not allowed to keep. We understand, however, that the amount of gold in the reserves which can be traced to

this source amounts to only about \$350,000,000.

The question whether Congress validly could deprive the Banks of the profit on the remainder of their gold is a serious one. It may be said in favor of such legislation that the Reserve Bank system is comparable to a central governmental bank; that they have been assigned certain functions, including that of issuing notes, in the performance of which this country's supply of gold has come into their hands; that the ownership of the gold has now become important for the first time; and that, under these circumstances, the Government and not the Reserve Banks should receive the gold profit upon devaluation. Against the constitutionality of such legislation, it may be urged that the banks are privately owned; that the gold constitutes a part of their assets, of which the private stockholders may not be deprived; and further, that the Banks would be wrecked if the profit were taken and the present gold content of the dollar again restored. While it is true that the banks are privately owned they are not primarily profit-making institutions, and no other private persons are now entitled to keep their gold. It is only because of the Banks' relationship to the Government that the private member banks have been able to retain an interest in such gold. Moreover, so far as the Reserve Banks are concerned, a reduction in the value of the dollar would effect, in terms of gold, a corresponding reduction in their obligations in deposits and currency.

Although it is not free from doubt, it is our view that Congress might appropriate at least a portion of the gold profit of the Banks

provided that they are guaranteed against loss in case of a future increase in the gold value of the dollar, and are assured of an ample supply of gold above the minimum reserve requirements to take care of possible changes in their reserve position. It would seem desirable that such legislation should be directed to the creation of a deposit credit in favor of the Government, rather than to effect a change in title to gold now held in the reserves.

(2. Whether the Gold Profit Can be Taken
Under any Existing Statute)

We think it may be fairly said that if there is any present statutory authority for taking the gold profit from the Reserve Banks it must be found in the Thomas Amendment, for it is that statute alone which authorizes a reduction in the weight of the gold dollar. If the authority is not found in that statute it does not exist, for Congress certainly did not intend to cover by any other existing statute, a subject arising collaterally in connection with dollar devaluation.

It seems clear that the Thomas Amendment does not authorize the Government to take gold profits resulting from devaluation. Sub-section (a) (of Section 43) authorizes the Secretary of the Treasury to enter into agreements with the Federal Reserve Banks, whereby the latter may undertake to conduct open-market operations in Government obligations, or to purchase directly Treasury bills or other Government obligations, Sub-section (b) (1) authorizes the President to direct the Secretary to

issue greenbacks, not to exceed \$3,000,000,000, to meet maturing Federal obligations or to purchase United States bonds. Sub-section (b) (2) authorizes the President, by proclamation, to fix the weight of the gold dollar in grains .9 fine, (but not to reduce its present weight more than 50%), and to fix the weight of the silver dollar at a definite fixed ratio in relation thereto "at such amounts as he finds necessary from his investigation to stabilize domestic prices or to protect the foreign commerce against the adverse effect of depreciated foreign currencies, and to provide for the unlimited coinage of such gold and silver at the ratio so fixed. . . ." It provides also that he may fix the weight of the gold dollar at the ratio established under any agreement with any foreign government. It concludes by stating that the gold dollar, at the weight so fixed by the President, shall be the standard unit of value and that all currency or forms of money shall be maintained at a parity with this standard. The remaining substantive provision (Section 45 (a)) permits the acceptance of silver, not to exceed \$200,000,000, in the payment of debts owed the United States by foreign governments.

There is nothing in the entire Amendment which remotely suggests that the President, or the Secretary, may deprive the Reserve Banks of the profit on their gold stocks resulting from an exercise of the President's power to fix the weight of the gold dollar. The debates in Congress also show that the Amendment was not intended to cover at all this subject of gold profits resulting from devaluation. (Vol. 27, Cong. Rec., pp. 2555-2556.) Senator Fletcher, Chairman of the Committee on Banking and Currency, was

asked whether the Amendment provided any method by which any profit made by those holding gold, at the date of devaluation, could be taxed. (p. 2555.) He replied that there was not, and further, that he did not favor incorporating such a provision in the pending bill, although he was in sympathy with the proposal and believed that it should be considered later. (pp. 2555-6.)

In view of the fact that the Thomas Amendment does not authorize the taking of the gold profit from any holder of gold, at the time of devaluation, we think that the question should be left to Congress, unless the Federal Reserve Banks should determine voluntarily to surrender the profit under an agreement between themselves and the Government. The problems involved (supra, pp. 5-7) are sufficiently serious without being aggravated by Government action taken under some mere shadow of statutory authority. As an example of the latter, it might be suggested that the President issue a new Executive Order requiring the Reserve Banks, as well as individuals now affected, to surrender their gold. Such an order could be rested only upon Section 5 (b) of the Trading with the Enemy Act, as amended by Section 2 of the Act of March 9, 1933, and, in our opinion, would be valid only if the retention of gold by the Reserve Banks constitutes "hoarding." We think it clear that it does not, and the action thus far taken by the President, which exempts the Reserve Banks from the requirement that gold be surrendered and, in effect, makes them his agents in collecting gold, is plainly inconsistent with such a position. Moreover, the Federal Reserve Act requires that the Banks maintain gold reserves, and the President

could not relieve them of that duty, even if it were wise as a matter of policy to do so. Removal of all the gold from the reserves would undoubtedly shake public confidence in the Federal Reserve notes, even though they are not presently redeemable in gold.

Nor do we think that Section 3 of the Act of March 9, 1933, would provide authority for taking the gold profit. It provides that "whenever in the judgment of the Secretary of the Treasury such action is necessary to protect the currency system of the United States," he may "require any or all individuals, partnerships, associations and corporations to pay and deliver to the Treasurer of the United States any or all gold coin, gold bullion, and gold certificates" owned by them. Upon receipt thereof, the Secretary is required to pay "an equivalent amount of any other form of coin or currency coined or issued under the laws of the United States." It might be suggested that since this language is broad enough to include the Reserve Banks, they could be required to deliver their gold for currency, the value of which could thereafter be reduced by proclamation of the President. We think it sufficient answer to this suggestion to point out that the Secretary could not find such a transaction to be "necessary to protect the currency system of the United States."

One additional advantage would be derived by action of Congress on this subject. There is a serious question whether the Thomas Amendment is not unconstitutional in delegating legislative power to the President. This question has already been considered at length in a

memorandum prepared in the Department, dated April 27, 1933. The conclusion was then reached that the bill (H. R. 3835) (which is less objectionable in this respect than the statute) delegated legislative power to the President and could not be regarded as within the scope of the decisions in Field v. Clark, 143 U. S. 649, and Hampton & Company v. United States, 276 U. S. 394. If devaluation of the dollar should be proclaimed by the President and the gold profit question should thereafter be dealt with by Congress, the action of the President could be ratified in the same statute. This question of the validity of the Thomas Amendment is a vital one in this connection, because unless the President's action is valid the Reserve Banks have in fact obtained no profit on their gold stocks.

3. Voluntary Surrender of the Gold Profit by the Reserve Banks

The questions involved if the gold profit were surrendered voluntarily best may be considered in connection with a specific plan. Subsection (a) of the Thomas Amendment provides that the Secretary of the Treasury may be directed by the President to enter into agreements with the Federal Reserve Banks and the Federal Reserve Board, providing, inter alia, that the Banks shall "purchase directly and hold in portfolio for an agreed period of time . . . Treasury bills or other obligations of the United States Government in an aggregate sum of \$3,000,000,000, in addition to those they may then hold . . . unless prior to the termination of such period . . . the Secretary shall consent to their sale." It

also provides that no suspension of reserve requirements made under Section 11 (c) of the Federal Reserve Act, necessitated by operations under this provision, shall require the imposition of the graduated tax usually imposed upon a deficiency in reserves.

The proposal is made to take action under this provision as follows:

(a) An agreement would be entered into between the Reserve Banks and the Secretary of the Treasury, providing that the former would purchase three billion dollars of Treasury bills or other obligations and pay therefor \$3,000,000,000 in gold, which would be earmarked for the account of the United States Government; (b) Prior to such sale the Reserve Board would suspend for several days the reserve requirements; (c) On the day following the transfer of title to the gold the President would reduce the gold content of the dollar 50% (under the conditions supposed); (d) Immediately thereafter the Treasury notes would be redeemed by the Government by payment to the Banks of one-half the amount of gold earmarked for the Government; (e) The remaining one-half of the gold, constituting the profit, would be turned over to the Reserve Banks, in consideration for the establishment on their books of a credit of three billion dollars in favor of the Government.

We think that the question whether, as a matter of policy, a voluntary transfer of the gold profit should be made by such an agreement is a matter to be resolved by the Federal Reserve Board and the Federal Reserve Banks. However, we may point out the legal questions which might arise. It cannot be assumed that even if all the Reserve Banks consent to such a

a plan, litigation will be avoided, since member banks may seek to make the Reserve Bank directors personally liable for waste of assets. The directors presumably could answer that Congress would have deprived them of the profit in any event and that it had the power to do so; that their action was taken pursuant to statutory authority, and that the cash position of the Banks was no different after consummation of the plan than before.

The chief danger in a voluntary surrender of the profit would seem to be that appropriate safeguards could not be erected to protect the Reserve Banks against any subsequent increase in the gold content of the dollar. If the dollar were devaluated 50% and then revaluated at the present parity level, the surrender plan would result in the Banks losing \$1,500,000,000 of their gold reserve. Moreover, it is not beyond possibility either that the President might have to exercise the power given under the Amendment more than once. Furthermore, the question of the directors' liability may depend on the constitutional validity of the Thomas Amendment, whereas we have pointed out that Congressional action on the subject might cure that objection (supra, p. 11.) We think also that Subsection (a) (2) of the Thomas Amendment clearly does not authorize such an agreement; it was intended to provide for credit expansion and not for dealing with the question of the gold profit of the Reserve Banks.

We are of the opinion, however, that the question whether the plan proposed should be carried out is one primarily for the determination of the Federal Reserve Board, the Federal Reserve Banks and the

Secretary. There are, of course, large questions of policy involved, and the administration would undoubtedly want to give consideration to the question whether the present public emergency warrants the use, under guise of statutory authority, of the device above described.

Respectfully submitted,

HAROLD M. STEPHENS,
Assistant Attorney General.

WILLIAM G. DAVIS
Special Assistant to the Attorney General