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SUPPLEMENT

GOVERNMENT GUARANTEE OF BANK DEPOSITS DEBATED AT BEDFORD

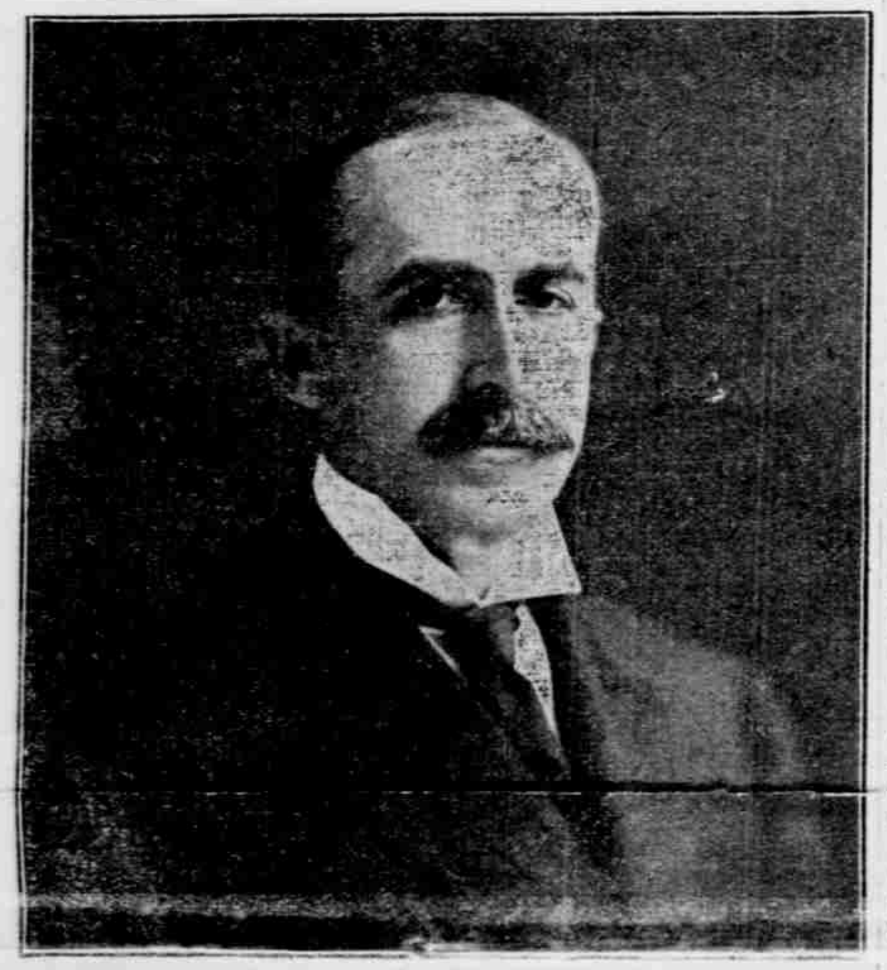
THE CRUCIAL FEATURE OF THE FINANCIAL PROBLEM DISCUSSED BY HON. JOHN G. M'HENRY AT BEDFORD SPRINGS.

Bedford Springs, Pa., Sept. 9.—The feature of the second days' session of the Pennsylvania Bankers' Association in annual session here, was the address of Hon. John G. McHenry, of Columbia county, in support of the proposition that the Federal government ought to guarantee deposits in banks. The opposite side of the proposition was supported by Mr. James J. Buchanan, President of the Pittsburg Trust Company.

Mr. McHenry said:

Mr. Chairman and Gentlemen of the Convention:

Your accomplished Chairman has invited me to present the argument of the people in the case of the Banks vs. the people now up for trial before this splendid body of jurymen.



JOHN G. McHENRY.

The question under debate is: Shall Congress enact a law levying a reasonable tax on National Banks, permitting all banks to avail themselves of the privilege, as an insurance fund for the protection of the depositor?"

In speaking for the people on the affirmative side of this great question, I realize to the fullest extent that I am addressing a jury of men the majority of whose minds are already adversely fixed. But I respectfully ask that you at least let your minds open to conviction and in a receptive mood to receive my argument. The final solution of this important question tion will be largely a question of human judgment. You may be right, and I may be wrong or I may be right and you may be wrong. We are dealing with a fundamental principle and because I may favor it, it does not necessarily follow that I am right nor because the big bankers of the country oppose the measure, it does not necessarily follow that they are right, but when the great mass of American people finally make up their minds upon any great public question, past history records them always in the right; so it will be with this question, the final decision, for it is a fundamental question and cannot be decided by mere argument. The American people as a whole embrace the Christian religion, yet there are many unbelievers who can marshal an astounding array of facts and eloquence with what they consider conclusive proof that the Christian Religion is all wrong—So it will be with my brilliant opponnet who is to follow me taking the negative side of this question, whom I have no doubt honestly belives he is right but you must remember the "fake" profit idea back of his argument and the infidelity of his teaching as applied to the banking religion.

You have a condition confronting you—not a theory. You must accept either a form of guarantee of Deposit or a Postal Savings Bank. Because the people demand that their earnings shall be protected. To argue that they are already protected is not sufficient. This is a people's Government and after the public mind is fully made up the people always get what they want. The predatory interests and the politicians may thwart the people's wishes for a time but in the end the people will rule. If you choose you may have a voice in moulding their final opinion upon these great financial questions and help frame the law but if you continue to show the same indifference which characterized you during our recent currnecy legislation you must accept the law as given to you and abide by the result.

Is It Right and Will It Pay?

When the honest legislator is called upon to consider a public question, he has but one predominant thought for his guidance, is it right? When the banker or business man approaches any question relating to his business he has but one predominant thought—Will it pay?

I hope to prove to the satisfaction of both the unbiased Law Maker and the Banker that a form of Federal Guarantee of bank deposits is not only right and sound as a fundamental principle of Banking economics but that it will pay—and I also shall prove that a Postal Savings Bank law would be a menace to the banking interests of the country and to the welfare of our people.

For the intelligent consideration of this question, I beg your indulgence that it may be taken up in a systematic way. Let us consider briefly:

First, is the Banking business a public or a private business?

Second, what is the real mission of a Bank?

Third, would a form of Federal Guarantee help, or retard the true mission of a Bank?

Fourth, Will it pay?

Is the Banking Business a public or a private Business? That depends altogether on how you run your Bank. In the early history of Banking, the business was confined exclusively to men of great wealth who carried on the business of loaning their own money to the borrowing public. Later on in the natural evolution of the business, Banks began to receive moneys in trust from the people. So rapidly did the business develop that it was deemed necessary for the public welfare that same form of Governmental supervision should be devised until finally we have the National Bank act authorizing the issuing of Federal charters for the operation of National Banks and our several States issuing State charters for the operation of State Banks. So if you are running a private Band, and some of the best banks I know are private banks, simply using your own money and not receiving money on deposit from the general public then the Government, National or State, has no constitutional right to interfere with you nor would they interfere with you under this proposed Guarantee.

If you are running a private Bank with your own money and not with public money, then your failures or losses are of no concern to the general public nor to the Government. But if, upon the other hand, you have asked either the State or the Federal Government to give you a special charter and are receiving money on deposit from the general public, then your Bank immediately becomes a public institution and the Government issuing your charter owes a moral obligation to the public to surround the business with such safeguards as will insure the public against loss.

In this connection and under this head I want to answer in advance one of the arguments which my opponent will produce, and that is,

Why Not Guarantee All Lines of Buisness?

He will argue that if the Government is to guarantee the Banking Business why not guarantee the business of the merchant, the manufacturer, and the farmer. The absurdity of this form of argument carries with it its own rebuttal as being unworthy of earnest consideration. Under a form of Federal Guarantee the government does not guarantee the Banking Business—it does not release the stockholder's liability, it merely requires the Bank to return the Depositors' money any time they call for it by levying a reasonable tax upon the Banks for that purpose. It puts the Banks in a position to meet any demand their depositors may make and that which is most important, removes the dangerous elements of fear and distrust from the depositors mind which at the same time, removes his desire to withdraw his deposits more rapidly than he needs them in his daily use.

The Government would never pay a dollar out of the People's Treasury but would simply act as a Trustee to receive and disburse this insurance fund.

Does the farmer or the merchant or the manufacturer receive a National charter from the Government, that the Governent should guarantee his business? No. Why have you National Bankers asked for a Federal charter? Because you believe it is an advantage for you to do so and because you believe it inspires greater confidence upon the part of the public. The great structure of the Banking Business of the country is built upon confidence. Any law or any condition which helps to increase public confidence by surrounding the business with fundamental safeguards is a good law and will work a great benefit not only to the country but will bring about greater profits to the banks themselves. Furthermore, the merchant, the manufacturer or the farmer may fail, but his failure has to do only with himself and his immediate creditors but when a Bank fails it involves the stockholders, the depositors and the business interests of the whole community.

With the [illegible] of a federal charter authorizing [illegible] to establish a national bank your business is no longer a private business but becomes a [illegible]. You have asked for the charter because you believe it will insure greater profits to you as stockholders. Therefore it is but fair, right and equitable that the government shall act as a medium for the public welfare in conserving the mutual interests of the stockholders, the officers, depositors and borrowers of the community.

Cause of Bank Failures.

Banks never fail except for one of three specific causes—violation or neglect of the banking laws upon the part of the officers or directors; bad investments, which is one cause of a hundred or embezzlement upon the part of the cashier or officers. In either of these cases a failure might have been prevented by a close surveillance upon the part of the Government. This being true, I hold that the Government is, to a certain extent, an accessory before the fact in every national bank failure, and the **United States Government should either withdraw entirely from the banking business OR ASSUME ITS** rights and privileges by guarding the business in the interest of the public welfare still more closely.

The national banking business of this country is operated upon a strictly scientific basis and properly officered and the present laws lived up to there is no reasonable excuse for any national bank failure, and in all the history of American banking we have yet to record the first failure of any national bank where the laws have been rigidly observed.

A Bank That as Once Been Successful Should Never Be Closed.

Banks will make bad loans and meet with losses just the same as a manufacturer or merchant will make bad sales and have his losses, but where a bank is so located as to supply a public necessity and with a line of deposits to make it profitable there is no reason under the sun why that bank should close its doors, and under the operation of my proposed bill there will never be any more bank failures or suspensions.

The application of the proposed law would work with automatic and scientific precision, and if losses have been sustained to the extent of impairing the surplus and capital of a bank, the Comptroller has it in his power to remove the cause and, **Instead of closing the doors, the banks go on doing business.** There has never yet been a bank failure within the limit of my observation or knowledge, but, the cause of the failure being removed, the **business reorganized, public confidence restored,** the bank has invariably recovered its losses and continued as a dividend paying proposition to its stockholders. A most striking proof of this truth is found in the recent Knickerbocker Trust Company suspension which closed by the arbitrary action of a clearing house committee, and within eight months is found in a solvent condition and is now doing a prosperous business with nearly forty million of deposits.

In providing a Government guarantee there would never be an additional tax levied to meet any loss, for there never would be any extraordinary withdrawal of deposits, and so long as the banker can rely with a reasonable degree of certainty that his deposits will remain at a normal state he can tell with very great accuracy just how for he can extend his accommodations to the merchant and manufacturer and general borrower, and thus increase his earning capacity to the fullest limit. He can tell what loans can be safely renewed, as well as what new loans can be made. Our recent panic, as far as the country at large is concerned, was caused more by fright upon the part of the banker than upon the part of the depositor. The average banker is not only an honest man, but a man of the highest character in his community and one who prides himself upon being able to give his depositors their money when they ask for it. So, when a condition of panic exists each conservative banker wants to keep his own institution strong, and is forced **to call in outstanding loans, and to refuse to grant any new loans.** While in many cases there is no real justification for this procedure, and notwithstanding the harm he works upon his individual community and as an integral part of the banking system of the country contributes his share of harm toward the country, yet he cannot be censured, for the reason that he does not know how soon his depositors may be frightened and line up in front of his window demanding cash, so a form of a guarantee which will satisfy the depositor under any and all conditions is just as essential for the benefit of the banker as it is for the depositor, and still more **is it essential for the fair interests of the borrower.**

In the individual management of an incorporated bank and the laws which govern [illegible], there are four separate interests to be conserved, viz: The Government either National or State, the stockholders, the depositors and the borrowers. Under our modern system of banking there seems to have developed a new type of bank manager who believes that the sole right in a bank is centered entirely within the stockholder. This type may justly be styled the Wall Street Banker.

So filled are they with the "divine right" idea that Bankers of this class look upon their deposits as their own money and therefore for their exclusive benefit. They chafe under any and all governmental restraint and are usually opposed to any form of banking legislation that looks to the welfare of the depositor and borrower. This principle seems to underlie every financial measure which has been favorably considered by the last session of Congress and is most strikingly exemplified by the distinguished Senator from Rhode Island, the Republican leader in the Senate, the author of the Aldrich-Vreeland Bill, the sole arbiter of American Legislation, in his speech, delivered in the Senate on March 20, 1908 Congressional Record, page 4152.

In discussing the question of a Federal guarantee of bank deposits, he said:

"The people of the States of the Union are not interested in this question. They are not the depositors. I refer to the common people. The people who deposit in the banks and the people who borrow the resources of the banks are business men who can take care of themselves, and there is no reason why we should run mad in his idea of paternalism."

I submit in all fairness to you men as practical bankers that if any banker would come before you and make a similar statement, "that the people of the states of the Union are not interested in this question, that they are not depositors," you would be forced to admit that he didn't know the primary principles underlying true banking success and that if he did not understand the primary principles he would not be fit to participate in bank management much less to become the sole maker of laws covering the currency and banking questions of the great American people. Yet it is this type of bankers who now oppose a Federal Guarantee and you cannot disguise the fact that your opposition is not based upon sound economic principles but is founded upon absolutely selfish motives.

The true mission of a bank is one of public good. It presents the true spirit of scientific co-operation. An honestly managed bank helps men to help themselves and when a bank is established in a community it should be so organized and managed and the stock so widely distributed that the greatest number may share in its profits and bring to the bank the widest possible degree of public confidence, hence any antional law which will further the true mission of a bank such as a Federal Guarantee of deposits is a law in the interest of the public welfare and one that will increase the profits of the banks as well.

Would a Form of Federal Guarantee Help, or Retard the True Mission of a Bank?

When men organize a bank, their primary object is one of profit they find, however, that in addition to their own capital they must receive from the public that it not only increases their profits but increases the usefulness of the bank as a community builder. Idle money in a community—like idle men, is an economic loss to a community. Idle money is one of the principle causes of idle men for it takes money to employ men. Therefore, no community will rise to its highest degree of financial and moral development unless the money of the community is kept in circulation. It is estimated that there is one billion dollars of idle money—money hidden at home and not in circulation, which would represent four billion dollars of additional commercial credits. Now isn't it better to try to get and keep this hidden money—which is real money—into circulation than to try the dangerous experiment of issuing a new kind of money as provided under the Aldrich-Vreeland Bill, at a high rate of tax which means a tax upon production?

Before men will put their money into a bank they must first have confidence in the management of the institution. So long as times are good and business conditions proceed undisturbed they are satisfied and willing to leave their money remain on deposit, but even under the most favorable conditions, there is a large number of people in every community who are afraid to trust their savings in any bank and those who have already deposited their savings are afraid the moment there is talk of a panic or a business depression, and [illegible] deposits.

In the removal of this fear in the public mind lies the great necessity for a Federal Guarantee. As far as actual losses are concerned in the past the percentage of losses to depositors and to the general public has been less, perhaps, than any other public loss in other lines of business but a law of this kind is not intended either for the profit of the bank or for the profit of the individual but it is intended as a economic factor for the public good.

If Mr. Aldrich is right in his statements, and you men who bow before the shrine of Wall Street in following his leadership, unite in believing that the people are not depositors in the banks, that the banks don't need the deposits of the people, then I am wrong and you are right, but if upon the other hand you do need the money of the people to carry on your business and if the people have a right to withdraw that money when they choose and destroy your business, it seems to me to be an unanswerable argument that a Federal Guarantee of Deposits will help further the true mission of the bank and in so doing help advance the interests of the great American people for both go hand in hand.

Will It Pay?

Now we come to that part of the question which appeals to you as practical bankers more than the question of public good—will it pay? During the recent session of Congress I had the honor to prepare and present a Bill, a copy of which I mailed to each bank in Pennsylvania and with which you are no doubt familiar. The Bill provides a semi-annual tax upon the capital stock of the one tenth of one percent or a two mill tax a year upon capital stock of each year upon the capital stock of each bank. My bill alos permits state banks to participate in the benefits by submitting to the same laws governing national banks as applied to examinations, publication of reports, reserves and surplus fund. It should also limit the maximum amount of interest on time deposits. What we need in banking legislation a greater unanimity and uniformity of bank management.

One state for instance will have a law fixing five per cent. of lawful reserves, another will have 10 per cent., another 15, while all national banks are compelled to carry 15 and 25 per cent. lawful reserves. In a time of panic the burden of support falls largely upon the national bank reserves and the drains upon them are such that they cannot maintain their lawful reserve and therefore become insolvent under the law. If any federal law can be framed such as is proposed, to help amalgamate the banking business and yet preserve to each state bank and each national bank its own individuality and its own control under its separate charter, it will be a good law and work to the benefit of the general banking business. There should be some law to demand an uniform percentage of reserves in all banks and an uniform percentage of undivided surplus in addition to the capital and a maximum rate of interest on deposits. A bank failure is worse than a fire—it not only incurs a direct loss but it involves a still greater indirect loss both to the bank and community through the loss of confidence and the arousing of those destructive elements in men of fear and distrust. Since 1865 the average yearly national bank losses have not exceeded $850,000. My proposed bill which levies a tax of two mills upon the capital stock provides a fund of Two Million Dollars annually or about two and a half times as much money as past experience has proved we need. I agree that it would be more fair to have this tax based upon deposits instead of upon capital stock, but if based upon deposits it would seem so insignificant that the public mind would not consider it as a sufficient tax to give them the protection which they want.

With the average bank of a hundred thousand capital, a two mill annual tax would mean a tax of $200 per year. Now counting the net profit which you make on your deposits, after deducting all fixed charges including your depositors interest account, at one per cent., your bank would have to secure an increased amount of deposits of twenty thousand dollars or increase its loaning capacity to the extent of $5,000 either way you want it.

Is there any banker here who is willing to make the statement that he believes he cannot increase his deposits upon the ratio of $20,000 per $100,000 capital or that he cannot increase his loaning capacity to the **extent of $5,000 when** his bank is backed by a federal guarantee to depositors and he knows that he is not going to have any extraordinary demand from his depositors for their money

Under [illegible]ment and associated banks are first protected by the capital stock investment; second, by the surplus and undivided profits; third, by the stockholders' liability representing three times the capital stock, and I should like to ask if any banker here knows of any banking institution anywhere that he would not be willing today to take its business over upon that basis. This is what we propose under my bill. Instead of liquidating the affairs of a bank and creating losses we continue the business without drawing a dollar from the National Treasury, and **apply the earnings of the bank to repay the losses before the stockholders get any dividends.** As a business proposition I know that you would be willing to take over the banking business of the country today upon that basis, and especially so would you take it over if you could have the privilege which you have under this bill of examining the conditions of the bank before it is permitted to receive this guarantee. The general average of bank stock dividends or net earnings throughout the United States is 15 per cent. annually. The annual tax provided herein is two mills on the capital stock.

So the argument against the tax falls in the evidence of past history and our general knowledge of the banking business. But even suppose the banks were obliged to bear this small tax, if it can be shown to be in the interest of the public welfare, the tax would be justifiable. Though it would seem to be beyond all argument and the widest possible stretch of imagination that the bankers would not receive through the increased deposits which would come into their vaults because of a guarantee of this kind and a larger loaning and earning capacity because of more steady volume of deposits, sufficient to increase their net earnings very much greater than any possible tax which might be imposed. Therefore, I claim that a Federal Guarantee will not only work to the public good but the benefit of all banks and I challenge my opponent to produce astisfactory evidence to the contrary.

Wall Street Argument Against Depositor's Guarantee.

In his effort to produce the evidence in answer to my challenge and in addition to his claim that if the government should guarantee one business it should guarantee all, which I have already answered, my opponent will urge that it will encourage and increase "wild cat" banking.

Second, that it is unfair to tax good banks for the loss of poor ones.

Third, that it will give the small bank an unfair advantage.

Fourth, that it is paternalism and unsound as a bank principle.

Wild Cat Banking.

As to the question of this proposed law encouraging wild-cat banking, it will have the opposite effect, because each bank in a community will then have an interest in every other bank and will be on guard as to its own affairs as well as its neighbor's affairs. The same argument would be just as reasonable as applied against life insurance, that a man would be more disregardful of his health because his life is insured, or it could be applied to fire insurance, that a man would be more careless of his property because his property was insured. If business history teaches us anything, we have learned that insurance is a fundamental and economic principle, and the question of this insurance is not so much to prevent the loss as to prevent the wide spread of harm which comes from a loss of this character, and the opposition of banks to this bill is not because of a fear of loss to themselves, but because of a selfish fear of competitors' possible gain.

Fewer Bank Losses in Future Than in the Past.

This recent agitation for reform, judging from actual results, has been used more as a political asset than for the accomplishment of real good to the masses, and has included within its realms various attacks upon the general banking business. True, men in high places have proved faithless to the trust and confidence imposed in them by their business associates and by the general public. Isolated cases of this kind always have existed and always will exist. There is one element of good, however, which will come from this panic and this general business reorganization. Corporate management of all kinds, whether applied to industrial pursuits or to the general banking business, will be cleaner and of a higher personal order than at any time in the past, and that, too, without any change whatever in existing laws.

Losses through national bank failures will be less in the future than they have been in the past. Men are growing better, and the standard of [illegible] honor among all classes of business men is higher today than ever before. It is impossible, therefore, to concede that because the possibility of loss is removed from his depositors the banker is going to take greater risks than he ever did before. The banker of the present day has no thought of the depositors' loss at all. He is concerned entirely and solely for his stockholders, and, knowing as he does that before the government can supply the loss to his depositors that he must first give up the earned surplus of his bank and call upon the stockholders of his bank to pay an assessment of 100 per cent. upon their stock, the same degree of conservatism will exist as before, and more so, for the reason that the Comptroller of the Currency will have authority to remove any officer or director from any bank whose conduct has been in direct opposition to the best interest of the bank.

Unfair to Tax Good Banks for the Fairure of Poor Banks.

I believe I have already answered the argument which my opponent will produce that it is unfair to tax good banks for the losses due to bad bank management. I have tried to show that there is no excuse for any bank failure. That there always have been and always will be bank losses. But where a bank has once had a paying line of business it is just as much of an economic waste to close up the bank and destroy its patronage as it would be to burn down a factory because a certain factory manager had robbed the Treasury. But, are bankers to be a specially favored class of men who first want a government to give them special privileges through which they can make very large profits and yet refuse to contribtue their share toward the maintenance of their government or the prosperitly of our people?

In this scheme of human government each citizen assumes his share of responsibility. Who supports our hospitals, our insane asylums, our homes for indigent persons? The people. Every personal or business failure in life means that the burden of the loss of that failure must be borne by somebody. So in our American government the burden of this social and economic life is distributed throughout all stratas of society through the medium of taxation. The banking business being a public business, it is better for the public good that the burden of loss, if losses there may be, shall be distributed throughout and rest with