

## Banking Act of 1933 (Glass-Steagall Bill)

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by the writer that the courts will be more apt to follow these interpretations than cause their reversal.<sup>15</sup>

The Securities Act, it is true, is not a panacea for all the ills and abuses of the present financial system—this would be impossible. It does, however, insure the investor against certain aforementioned fraudulent practices of issuers and underwriters and also enables him to obtain the true and complete statement of condition of the corporation in which he is to invest his money.

ALFRED HECKER.

BANKING ACT OF 1933<sup>1</sup> (GLASS-STEAGALL BILL).—No bill with the possible exception of the National Industrial Recovery Act, that has been passed by the last Congress, has met so varied a reception as the Glass-Steagall Bill. It is condemned by the American Bankers' Association as a high mark in legislative intermeddling, yet other informed circles entertain serious doubts as to whether it has gone far enough in seeking to protect American industry from a recurrence of the cycles of business depression largely referable to uncontrolled credit expansion and contraction. While Senator Glass and the administration fear that certain features, notably the deposit insurance provision, are bound to react unfavorably upon the Act itself and even upon the Federal Reserve System upon which it is based, while powerful member banks threaten liquidation and secession from the System because of the insurance feature, nevertheless, the majority of Congress feels with Representative Steagall that "this bill rests upon the theory that banking which is unsafe for the depositors ought to be prohibited by law. Banking is not the individual right of a citizen and when we charter an institution to engage in banking to receive the deposits of the public, it is the duty of the government to see that deposits of the public are protected."<sup>2</sup>

These divergent views are presented merely to point out that at the next session of Congress we can expect vigorous onslaughts upon the bill in an effort to eliminate or at least to considerably alter various provisions, and indeed, movements are already under way toward that objective.

Before we enter into any consideration of the bill itself, it would be best to ascertain what forces brought it about. The bill sought

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<sup>15</sup> See article in the New York Times of October 15, 1933, by Arthur H. Dean; see also a copy of the address by Mr. Dean, delivered at the Financial Advertisers Association Convention, New York, on the economic and legal aspect of the Securities Act.

<sup>1</sup> Act of June 16, 1933, c. —, 48 Stat.

<sup>2</sup> See N. Y. Times, June 25, 1933, §VIII, p. 3.

to correct a chaotic banking structure which if not instrumental in bringing about the depression, was at least unable to overcome or cope with it. This disorganization was born out of the very system of government under which we live. Each of the forty-nine legislative bodies imposed varying degrees of supervision, and granted all too liberal privileges. The ease of incorporation by banks of no great financial resources, the utter incompetency and irresponsibility of directorships, the susceptibility of bank supervisors to political control, all contributed in bringing about a competition in laxity, and inevitably led to numerous bank failures.

Also, the Federal Reserve System itself was weak. It was powerless to curb stock speculation, powerless to supervise the great preponderance of state banks over which the system had absolutely no control, and to which in times of stress it could grant no aid.

It is the purpose of the Glass-Steagall Bill to establish a more uniform system of banking by greatly augmenting the powers of the Federal Reserve Board and the Comptroller of the Currency, by curbing and controlling security speculation by banks and by making reforms designed to encourage sound banking practices.<sup>3</sup>

The most important feature of the Banking Act is the deposit insurance plan.<sup>4</sup> A Federal Deposit Corporation has been created to liquidate the assets of the suspended national banks and state member banks<sup>5</sup> and to insure the deposits of all banks admitted to the benefits of the plan, beginning July 1, 1934.<sup>6</sup> Deposits are insured only in the following manner: One hundred per cent of the net amount up to \$10,000; seventy-five per cent of the amount above \$10,000 and up to \$50,000; fifty per cent of the amount above \$50,000.<sup>7</sup> This plan thus provides for the complete insurance of ninety-nine per cent of all depositors. When a participating bank fails, the corporation is appointed receiver and immediately organizes a new national bank, transferring the deposits from the defunct bank to the new national bank.<sup>8</sup> The depositor may permit his deposit to remain in the new bank or may withdraw the whole or any part of it as he pleases. The new bank takes over all the assets of the closed bank and may issue stock. If subscribed for and paid in cash sufficient in amount to permit it to engage in business as a new national bank, upon application it may be permitted to do so. If this is impossible the new bank may sell its assets to another institution of that locality, or if that fails, the new bank will itself be liquidated within two years.<sup>9</sup> The permanent system of deposit in-

<sup>3</sup> *New Republic*, July 5, 1933, p. 195.

<sup>4</sup> *Supra* note 2.

<sup>5</sup> *Supra* note 1, §8; Amending the Fed. Res. Act, by inserting between sections 12 and 13 (U. S. C., tit. 12, §§261, 262, 342) thereof subd. 12B (a).

<sup>6</sup> *Ibid.*, §8, subd. 12B (e, f, g).

<sup>7</sup> *Ibid.*, subd. 12B (1).

<sup>8</sup> *Ibid.*

<sup>9</sup> *Ibid.*

surance will go into effect July 1, 1934, but on January 1, 1934, a temporary insurance fund insuring all deposits up to \$2,500 will go into effect.<sup>10</sup>

The Federal Deposit Corporation will be financed to the extent of approximately \$500,000,000 which is to be secured from three sources. The United States Treasury will appropriate \$150,000,000.<sup>11</sup> Each Federal Reserve Bank will subscribe one-half of its surplus as of January 1, 1933; one-half of that is payable immediately and the other one-half subject to call.<sup>12</sup> The third source of revenue is to come from the participating banks.<sup>13</sup> Whether these banks be members of the Federal Reserve Bank System or not they may participate in the plan and their depositors will receive the benefits of the insurance, but before a bank will be permitted to participate it will be required to secure a certificate of solvency and must submit to examination by the Corporation.<sup>14</sup>

These participating banks then, must subscribe to one-half of one per cent of total deposits, one-half payable on July 1, 1934, the remainder subject to call.<sup>15</sup>

A second important provision of the Banking Act is that which treats of the extension of branch banking. Now member banks are permitted to establish branch banks in states already permitting the same to its own banks.<sup>16</sup> It is hoped that many state banks not now members of the Federal Reserve System will join and submit to regulation, supervision and control; thus an attempt is made to remove an inherent weakness of the Federal Reserve System, a paucity of member banks.

It is clear that nearly all of the provisions of the Glass-Steagall Bill are dependent upon the inclusion into the Federal Reserve System, of an increasing number of member banks.<sup>17</sup> It is to be here noted that after July 1, 1936, only members of the Federal Reserve System, or those having applied for membership, will be permitted to participate in the insurance benefits.<sup>18</sup> It is evident that this is another device to increase the membership of the Federal Reserve System; for it is believed that no depositor will be willing to deposit in any bank that is not a recipient of the insurance benefits.

The third provision is evidently aimed at the Morgans and the moribund security affiliates of commercial banks,<sup>19</sup> for the Act provides that within one year national and member banks must divest

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<sup>10</sup> *Ibid.* subd. 12B (y).

<sup>11</sup> *Ibid.* subd. 12B (c).

<sup>12</sup> *Ibid.* subd. 12B (e).

<sup>13</sup> *Ibid.* subd. 12B (f).

<sup>14</sup> *Supra* note 12.

<sup>15</sup> *Supra* note 10.

<sup>16</sup> *Supra* note 1, §23.

<sup>17</sup> *Supra* note 3.

<sup>18</sup> *Supra* note 1, §8, subd. 12B (f, 1).

<sup>19</sup> *Supra* note 3.

themselves of securities affiliates, and after one year it shall be unlawful for any securities company to engage in banking and henceforth no banking institution shall exercise both functions.<sup>20</sup>

The relationship of member banks to holding companies and subsidiary affiliates shall be carefully and thoroughly scrutinized. At any time the Federal Reserve Board may request reports and may make examinations of the existing relationship to prevent any illegal transfer of assets.<sup>21</sup> Such transfers were formerly possible when the relationship was not so easily detected or controlled.

No longer will any national bank stock carry double liability, for the Act provides that any new national bank stock issued after this law goes into effect will carry only single liability, just like stocks of any other private corporation.<sup>22</sup>

In line with the efforts of the bill to impress upon the directors of the bank a greater degree of responsibility, four measures were passed which attempted to fix responsibility squarely upon the shoulders of the directors. These were that (1) the number of directors shall not be less than 5 or more than 25,<sup>23</sup> (2) that each director must be a bona fide owner of not less than \$1,000 of stock in the bank,<sup>24</sup> (3) the Federal Reserve Board may remove any director from office, after granting him a hearing, because of unsafe or unsound banking practices,<sup>25</sup> (4) no director may receive loans from his bank.<sup>26</sup> An attempt was made to give the minority stockholders representation on the board by providing that vote for directors shall be by cumulative ballot.<sup>27</sup>

These are the principal provisions of the Banking Act. Manifestly the bill attempts to tighten many loopholes in the Federal Reserve System to devise more rigid supervision of the capital structure and the investment policies of the banks, and to lay a foundation for far-reaching changes in our financial structure. It is an attempt to place the responsibilities of management where they belong, and to "compel banks in general to adopt and insist upon sound banking. It would make bankers the principal advocates of strict government regulation of banks, strict inspection and strict enforcement of banking laws."<sup>28</sup>

What changes will be wrought by the next Congress and how far the bill will succeed in practice after the alterations are made, we cannot now foretell.

CARL E. ALPER.

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<sup>20</sup> *Supra* note 1, §20.

<sup>21</sup> *Ibid.* §19, amending REV. STAT. §5144 (U. S. C., tit. 12, §61).

<sup>22</sup> *Ibid.* §22.

<sup>23</sup> *Ibid.* §31.

<sup>24</sup> *Ibid.*

<sup>25</sup> *Ibid.* §30.

<sup>26</sup> *Ibid.* §12.

<sup>27</sup> *Supra* note 21.

<sup>28</sup> Literary Digest, June 24, 1933, quoting the Star and Times of St. Louis.