Chapter 3
Establishment of the FDIC

> The adoption of nationwide deposit insurance in 1933 was made possible by the times, by the perseverance of the Chairman of the House Committee on Banking and Currency, and by the fact that the legislation attracted support from two groups which formerly had divergent aims and interests—those who were determined to end destruction of circulating medium due to bank failures and those who sought to preserve the existing banking structure.[13]

Banking Developments, 1930 – 1932

An average of more than 600 banks per year failed between 1921 and 1929, which was 10 times the rate of failure during the preceding decade. The closings evoked relatively little concern, however, because they primarily involved small, rural banks, many of which were thought to be badly managed and weak. Although these failures caused the demise of the state insurance programs by early 1930, the prevailing view apparently was that the disappearance of these banks served to strengthen the banking system.

This ambivalence disappeared after a wave of bank failures during the last few months of 1930 triggered widespread attempts to convert deposits to cash. Many banks, seeking to accommodate cash demands or increase liquidity, contracted credit and, in some cases, liquidated assets. This reduced the quantity of cash available to the community which, in turn, placed additional cash demands on banks. Banks were forced to restrict credit and liquidate assets, further depressing asset prices and exacerbating liquidity problems. As more banks were unable to meet withdrawals and were closed, depositors became more sensitive to rumors. Confidence in the banking system began to erode and bank "runs" became more common.

During this period, the Federal Reserve did little to ease the liquidity problems of banks. The failure of the Federal Reserve to adopt an aggressive stance with respect to either open market purchases of securities or its discount window operations has been ascribed to several factors.[14] Most notably, it was generally believed that bank failures were an outgrowth of bad management and, therefore, were not subject to corrective action by the Federal Reserve. Concern within the Federal Reserve also was muted because most failed banks in 1930 were nonmembers for which Federal Reserve officials felt no responsibility.

---

[13]Golembe, "The Deposit Insurance Legislation of 1933," p. 182.

[14]A discussion of the Federal Reserve System's attitude appears in Milton Friedman and Anna J. Schwartz, *A Monetary History of the United States, 1867-1960* (Princeton, New Jersey: National Bureau of Economic Research, 1963), pp. 357-359. Much of the discussion relating to the events preceding the nationwide bank holiday is based on this source.

In all, 1,350 banks suspended operations during 1930 (Table 5).[15] Bank failures during the previous decade had been confined primarily to agricultural areas; this no longer was the case in 1930. In fact, the Bank of United States, one of the nation's largest banks based in New York City, failed that year. The large jump in bank failures in 1930 was accompanied by an even greater increase in depositor losses.

Table 5
Commercial Bank Suspensions, 1921 – 1933
($ Thousands)

Year	Number of Suspensions (1)	Deposits (2)	Losses Borne by Depositors (3)	Losses as a Percent of Deposits in All Commercial Banks (4)
1921	506	$172,806	$59,967	0.21%
1922	366	91,182	38,223	0.13
1923	646	149,601	62,142	0.19
1924	775	210,150	79,381	0.23
1925	617	166,937	60,799	0.16
1926	975	260,153	83,066	0.21
1927	669	199,332	60,681	0.15
1928	498	142,386	43,813	0.10
1929	659	230,643	76,659	0.18
1930	1,350	837,096	237,359	0.57
1931	2,293	1,690,232	390,476	1.01
1932	1,453	706,187	168,302	0.57
1933	4,000	3,596,708	540,396	2.15

Sources: Columns (1), (2) and (3), FDIC; column (4), Friedman and Schwartz.

As liquidity pressures subsequently eased during the early months of 1931, the number of bank failures declined sharply, but the decrease proved to be short-lived. Bank failures again rose between March and June as the public resumed converting deposits into currency and banks sought to meet withdrawal demands. During the second-half of the year, another, more serious, liquidity scramble occurred.

Once again, the Federal Reserve failed to inject sufficient liquidity into the banking system. In 1931, policymakers were primarily preoccupied with international monetary matters. The abandonment by Great Britain of the gold standard in September

[15]The terms "bank suspensions" and "bank failures" often are used interchangeably. For the most part, this practice is followed throughout the chapter. Technically, however, "suspensions" include all banks that are closed because of financial difficulties, whereas "failures" are limited to those suspended banks that were placed in the hands of receivers and liquidated. Some of the suspended banks were reorganized or restored to solvency and resumed operations. In either instance, the assumption is that the suspended bank actually failed, though rehabilitation later occurred.

1931 aroused general fears that other countries might follow. These fears caused many foreigners with U.S. bank accounts to convert deposits to gold in the New York money market. To stem the ensuing gold outflow, the Federal Reserve Bank of New York sharply increased its rediscount rate. Although this action achieved the desired effect, no steps were taken to augment already depleted bank reserves through extensive open market purchases of securities. By ignoring domestic financial considerations, the Federal Reserve added to the banking industry's woes.

The effects of these liquidity crises were reflected in the bank failure statistics. About 2,300 banks suspended operations in 1931. The number of failures thus exceeded the average number for the 1921-1929 period by almost threefold. Losses borne by depositors in 1931 exceeded losses for the entire 1921-1929 period.

In an attempt to ease bank liquidity problems, the National Credit Corporation was organized by private-sector bankers in October 1931 to extend loans to weakened banks. However, the corporation failed within a matter of weeks. Business leaders appealed to the federal government for assistance. The Hoover Administration responded by recommending two measures. The first resulted in the creation, in January 1932, of a new major federal lending agency, the Reconstruction Finance Corporation (RFC). One of its primary functions was to make advances to banks. By the end of 1932, the RFC had authorized almost $900 million in loans to assist over 4,000 banks striving to remain open. The RFC might have assisted more banks had Congress not ordered it to disclose publicly the names of borrowers, beginning in August 1932. Appearance of a bank's name on the list was interpreted as a sign of weakness and frequently led to runs on the bank. Consequently, many banks refrained from borrowing from the RFC.

The second measure supported by the Hoover Administration – the Glass-Steagall Act of February 27, 1932 – broadened the circumstances under which member banks could borrow from the Federal Reserve System. It enabled a member bank to borrow from a Federal Reserve Bank upon paper other than that ordinarily eligible for rediscount or as collateral for loans. Although the amounts subsequently borrowed were not large in the aggregate, the measure did aid individual banks.

The generally improved banking situation during the ensuring months was marked by a significant drop in both the number of bank failures and depositor losses. However, other signs suggested that the industry's troubles were far from over. Waves of bank failures still occurred during the year. Another disquieting sign was the emergence of bank moratoria. Initially, they were declared by individual local communities. Later that year, Nevada proclaimed the first statewide moratorium when runs on individual banks threatened to involve banks throughout the state. Similar moratoria were to play a role in the events that culminated in the nationwide bank holiday of 1933.

The Banking Crisis of 1933

During the winter of 1932-1933, banking conditions deteriorated rapidly. In retrospect, it is not possible to point to any single factor that precipitated the calamitous events of this period. The general uncertainty with respect to monetary and banking conditions undoubtedly played the major role, although there were specific events that tended to increase liquidity pressures within the system. Banks, especially in states that had declared bank moratoria, accelerated withdrawals from correspondents in an attempt to strengthen their position. Currency holdings increased significantly, partially in anticipation of additional bank moratoria.

Additional liquidity pressures were brought about by concern relating to the future of the dollar. With the election of Franklin D. Roosevelt in November 1932, rumors circulated that the new administration would devalue the dollar, which led to an increase in speculative holdings of foreign currencies, gold and gold certificates. Unlike the period of international monetary instability in 1931, a significant amount of the conversions from Federal Reserve notes and deposits to gold came from domestic sources. These demands placed considerable strain on New York City banks and, ultimately, on the Federal Reserve Bank of New York.

It was the suddenness of the withdrawal demands in selected parts of the country that started a panic of massive proportions. State after state declared bank holidays. The banking panic reached a peak during the first three days of March 1933. Visitors arriving in Washington to attend the presidential inauguration found notices in their hotel rooms that checks drawn on out-of-town banks would not be honored. By March 4, Inauguration Day, every state in the Union had declared a bank holiday.

As one of his first official acts, President Roosevelt proclaimed a nationwide bank holiday to commence on March 6 and last four days. Administration officials quickly began to draft legislation designed to legalize the holiday and resolve the banking crisis. Early in their deliberations they realized that the success of any proposed plan of action primarily would hinge on favorable public reaction. As noted by Raymond Moley, a key presidential adviser who attended many of the planning sessions:

> We knew how much of banking depended upon make-believe or, stated more conservatively, the vital part that public confidence had in assuring solvency.[16]

To secure public support, officials formulated a plan that relied on orthodox banking procedures.

Few members of Congress knew what was contained in the Administration's bill when they convened in extraordinary session at noon on March 9. In fact, Henry B. Steagall, Chairman of the Committee on Banking and Currency, purportedly had the only copy of the bill in the House. Waving the copy over his head, Steagall had entered the House chamber, shouting, "Here's the bill. Let's pass it."[17] After only 40 minutes of debate, during which time no amendments were permitted, the House passed the bill,

---

[16]Raymond Moley, *The First New Deal* (New York: Harcourt, Brace & World, Inc., 1966), p. 171.

[17]Ibid., p. 177.

known as the Emergency Banking Act. Several hours later, the Senate also approved the emergency legislation intact.

The Emergency Banking Act legalized the national bank holiday and set standards for the reopening of banks after the holiday. The Act expanded the RFC's powers as a means of dealing with the crisis then threatening the banking system. It authorized the RFC to invest in the preferred stock and capital notes of banks and to make secured loans to individual banks.

To ensure an adequate supply of currency, the Act provided for the issuance of Federal Reserve Notes, which were to be backed by U.S. government securities. The Federal Reserve Banks were empowered to advance the new currency to member banks without requiring much collateral. After the Act was signed into law, the Bureau of Engraving and Printing promptly went into 24-hour production to manufacture the currency.

The President subsequently issued a proclamation extending the holiday in order to allow time for officials to reopen the banks. In his first "fireside chat," delivered on March 12, President Roosevelt reviewed the events of the past several days and outlined the reopening schedule. Following proper certification, member banks in the 12 Federal Reserve Bank cities were to reopen on March 13. Member banks in some 250 other cities with recognized clearinghouses were to reopen on March 14. Thereafter, licensed member banks in all other localities were to reopen. The President indicated that the Secretary of the Treasury already had contacted the various state banking departments and requested them to follow the same schedule in reopening state nonmember banks. Before concluding his radio address, the President cautioned that he could not promise that every bank in the nation would be reopened. About 4,000 banks never reopened either because of the events of the previous two months or the bank holiday itself.

The task of implementing the Emergency Banking Act primarily was the responsibility of the Secretary of the Treasury. Under the Act, licenses for all member banks, both national and state, were to be issued by the Secretary. (State nonmember banks were to be licensed by the state banking departments.) The Treasury, however, demanded that each of the Federal Reserve Banks approve of the reopening of banks in their respective districts. The Federal Reserve Board balked at this demand, preferring instead that the Treasury Department shoulder the entire burden of reopening member banks. The controversy was resolved in the Treasury Department's favor. It was agreed that licenses would be issued by the Secretary of the Treasury upon the recommendation of the district Federal Reserve Bank, the chief national bank examiner and the Comptroller of the Currency. Several hundred banks soon reopened for business on the certification of the Treasury. As the reopening proceeded, public confidence increased significantly and widespread hoarding ceased.

Federal Deposit Insurance Legislation

After some semblance of order had returned to the financial system, efforts were renewed in Congress to enact deposit insurance legislation. Although a deposit insurance bill had been passed by the House in 1932, the Senate had adjourned without acting on the proposal. Insurance proponents hoped that legislative efforts would prove successful this time, since the banking crisis was still fresh in the public's mind. In their view, recent events had shown that a system of federal deposit insurance was necessary to achieve and maintain financial stability.

One of the chief proponents of federal deposit insurance in Congress was Representative Steagall. He has been credited with proposing the legislation that created the Federal Deposit Insurance Corporation, leading the fight for its adoption in the House and helping to effect a compromise when chances for passage of the bill appeared doomed. Steagall's achievement was all the more remarkable in view of the formidable opposition confronting the proponents of deposit insurance. Opposition emanated from the Roosevelt Administration, segments of the banking industry and from some members of Congress.

Arguments offered against deposit insurance reflected both practical and philosophical considerations. Opponents asserted that deposit insurance would never work. They pointed to the defunct state-level deposit insurance programs to substantiate their argument. Another widely held view was that deposit insurance would remove penalties for bad management. Critics also charged that deposit insurance would be too expensive and that it would represent an unwarranted intrusion by the federal government into the private sector.

Within the Roosevelt Administration, the Secretary of the Treasury Woodin was strongly opposed to the idea of federal deposit insurance. While historians have asserted that the Secretary's views were partially responsible for President Roosevelt's opposition to deposit insurance, accounts differ regarding the nature and extent of Roosevelt's opposition. However, the Administration was not of one mind on the issue. Support was voiced by Vice President John Nance Garner and Jesse H. Jones of the RFC, among others. Prior to Roosevelt's inauguration, Garner, then-Speaker of the House, had appealed to the President-elect to support deposit insurance. When Roosevelt declined, stating that it would never work, Garner predicted that deposit insurance legislation eventually would be passed.[18]

Banking interests, particularly those representing the larger banks, generally viewed federal deposit insurance with distaste. The President of the American Bankers Association declared that deposit insurance was "unsound, unscientific and dangerous."[19] The banking industry's views had only limited effect since banking at that time was held in low esteem. The industry's already tarnished image was not helped by disclosures of

[18] Ibid., pp. 318-319.

[19] "Wires Banks to Urge Veto of Glass Bill," *The New York Times*, June 16, 1933, p. 14.

unsavory security market dealings on the part of certain New York banks which came to light when deposit insurance was being considered in Congress.

More formidable opposition to deposit insurance came from several influential Congressmen. One of the most vociferous opponents was Carter Glass of Virginia, Chairman of the Senate Banking and Currency Committee. He had been Roosevelt's initial choice to serve as Secretary of the Treasury, but declined the Cabinet offer. Although Senator Glass was intent on passing banking reform legislation, federal deposit insurance was not one of the reforms he supported or sought. In opposing federal deposit insurance, Glass pointed to the record of the defunct state insurance programs. Nevertheless, he subsequently allowed bank deposit insurance to be written into a banking bill that he had sponsored. One business journal during the period reported that Glass simply had yielded to public opinion:

> It became perfectly apparent that the voters wanted the guarantee [deposit insurance], and that no bill which did not contain such a provision would be satisfactory either to Congress or to the public. Washington does not remember any issue on which the sentiment of the country has been so undivided or so emphatically expressed as upon this.[20]

In mid-May both Senator Glass and Representative Steagall formally introduced banking reform bills, which included provisions for deposit insurance. The two bills primarily differed with respect to the conditions for membership in the deposit insurance corporation that was to be created. Whereas membership in the Federal Reserve was a precondition for obtaining deposit insurance under the Senate bill, it was not a prerequisite in the House version. Both bills incorporated the demands made by the Roosevelt Administration that (1) deposit coverage be based on a sliding scale, and (2) there be a one-year delay in the start of the insurance corporation.

Later that month, however, the Glass bill was amended to incorporate Senator Arthur Vandenberg's proposal calling for the creation of a temporary deposit insurance fund. Vandenberg opposed a delay in the start of deposit insurance because "the need is greater in the next year than for the next hundred years."[21] On the day Vandenberg introduced his proposal, Vice President Garner was presiding over the Senate, which was sitting as a court of impeachment in the trial of a district judge. Garner had heard that Vandenberg had formulated a deposit insurance plan that would accomplish the same goals as those contained in an insurance bill which Garner had pushed through the House in 1932. Desiring that deposit insurance be implemented as soon as possible, Garner therefore approached Vandenberg during the impeachment proceedings and inquired whether he had the deposit insurance amendment in his possession. After Vandenberg responded affirmatively, Garner instructed him to introduce the amendment when signaled. Several minutes later, Garner suspended the court proceedings and ordered the Senate into regular session to consider more banking legislation. With Garner sitting by

[20]"Deposit Insurance," *Business Week*, April 12, 1933, p. 3.
[21]"Bank Bill Debate to Open in Senate," *The New York Times*, May 19, 1933, p. 4.

his side, Vandenberg then offered his deposit insurance amendment, which was overwhelmingly adopted.

The amendment stipulated that, effective January 1, 1934, the temporary fund would provide insurance coverage up to $2,500 for each depositor and would function until a permanent corporation began operations on July 1, 1934. If demands on the temporary fund exceeded available monies, the Treasury would be obligated to make up the difference. The amendment also provided that solvent state banks could join the fund.

The inclusion of the Vandenberg amendment in the Senate bill almost resulted in the defeat of deposit insurance in Congress. When the banking reform bills that had been passed by both houses were sent to a joint conference committee for resolution of differences, an impasse promptly developed. The House conferees opposed the Vandenberg amendment contained in the Senate version of the bill, particularly the provision calling for the immediate establishment of a temporary insurance corporation. Another issue that split the conferees was whether Federal Reserve membership should be a precondition for obtaining deposit insurance.

A compromise finally was reached on June 12, after the Senate conferees threatened to remove all deposit insurance provisions from the bill. They feared that the impasse over deposit insurance could endanger all of the banking reform measures contained in the bill. In order to save the bill, the House conferees reluctantly accepted the Senate's version as well as an additional provision desired by the Senate conferees to liberalize the branching restrictions governing national banks. This provision reflected widespread public disillusionment with the failure-prone independent banking system. Proponents of branch banking maintained that geographic diversification of lending risks and the deposit base would result in a lower bank failure rate.

The bill agreed to by the conferees passed both houses of Congress on the following day. Some opponents of deposit insurance had not yet thrown in the towel, though. The American Bankers Association wired its member banks, urging them to telegraph President Roosevelt immediately to request his veto of the legislation. Nevertheless, Roosevelt signed the measure, known as the Banking Act of 1933, into law on June 16, 1933. Section 8 of the Act created the Federal Deposit Insurance Corporation through an amendment to the Federal Reserve Act. The Banking Act of 1933 also created the Federal Reserve Open Market Committee and imposed restrictions on the permissible activities of member banks of the Federal Reserve System.

Deposit Insurance Provisions of the Banking Act of 1933

Section 12B of the Federal Reserve Act as amended created the Federal Deposit Insurance Corporation and defined its organization, duties and functions. It provided for two separate plans of deposit insurance: a temporary plan which was to be initiated on January 1, 1934, and a permanent plan which was to become effective on July 1, 1934.

Capital necessary to establish the FDIC was to be provided by the United States Treasury and the 12 Federal Reserve Banks. The Treasury was to contribute $150 million. Each of the Federal Reserve Banks was required to subscribe to Class B capital stock in an amount equal to one-half of its surplus as of January 1, 1933.

Management of the FDIC was vested in a Board of Directors consisting of three members. The Comptroller of the Currency was designated a member *ex officio*; the other two members were to be appointed by the President for six-year terms with the advice and consent of the Senate. One of the two appointive directors was to serve as Chairman of the Board, and not more than two members of the Board could be members of the same political party.

The temporary plan of deposit insurance initially limited protection to $2,500 for each depositor. Banks admitted to insurance under the temporary plan were to be assessed an amount equal to one-half of 1 percent of insurable deposits. One-half of the assessment was payable at once; the rest was payable upon call by the FDIC.

All Federal Reserve member banks licensed by the Secretary of the Treasury under terms of an Executive Order of the President, issued March 10, 1933, were required by law to become members of the temporary fund on January 1, 1934. Other banks were authorized to join the fund upon certification of their solvency by the respective state supervisory agencies and after examination by, and with the approval of, the Federal Deposit Insurance Corporation.

The original permanent plan, while it never took effect and was superseded by a new permanent plan in the Banking Act of 1935, contained certain features of historical interest. Banks participating in insurance under the original plan were to subscribe to capital stock of the FDIC and be subject to whatever assessments might be needed to meet the losses from deposit insurance operations. The plan provided for full protection of the first $10,000 of each depositor, 75 percent coverage of the next $40,000 of deposits, and 50 percent coverage of all deposits in excess of $50,000. In order to retain their insurance, all participating banks were required to become members of the Federal Reserve System within two years. Thus, with regard to financing, degree of protection and supervisory provisions, the original plan differed significantly from both the temporary plan and the permanent plan that became effective with the Banking Act of 1935.

Formation of the Federal Deposit Insurance Corporation

One of the first tasks facing the FDIC was the formation of an operating organization. As provided in the Banking Act of 1933, the Comptroller of the Currency, J. F. T. O'Connor, was designated as a director. He served as the FDIC's chief executive until the appointment of the other two directors.

In September, the President appointed as the other directors Walter J. Cummings, then-special-assistant to Secretary of the Treasury Woodin, and E. G. Bennett, a

Republican banker and businessman from Utah. The directors organized on September 11, 1933, and elected Cummings to serve as Chairman of the Board. As was his intent, Cummings' chairmanship lasted only through the initial organization of the FDIC. In January 1934, he left the FDIC to assume the chairmanship of Continental Illinois National Bank & Trust Company in Chicago.

Bank examination consumed nearly all of the FDIC's efforts in the months before the establishment of the temporary fund on January 1, 1934. The hastily assembled examination force had to examine almost 8,000 state-chartered nonmember banks in three months in order for the FDIC to meet its responsibilities under the Banking Act of 1933. The task of completing these admission examinations was largely accomplished as intended by the end of 1933. Of the 7,834 applicant nonmember banks, 83 percent were approved for insurance, 12 percent were rejected, 4 percent were still pending decisions, and less than 1 percent remained to be examined.

The Temporary Federal Deposit Insurance Fund

Admission standards. Actual insurance of bank deposits became effective on January 1, 1934. The Temporary Federal Deposit Insurance Fund opened with 13,20l banks insured (or approved for insurance). Of these, 12,987 were commercial banks and 214 were mutual savings banks. These represented 90 percent of all commercial banks and 36 percent of all mutual savings banks.

The lower participation rate among savings banks was attributable to several factors. Many savings banks questioned whether they needed deposit insurance. Unlike commercial banks, savings banks had not been seriously affected by bank runs since they legally could restrict deposit withdrawals. In several states mutual savings banks legally could not subscribe to stock in the FDIC. In other instances, savings banks objected to FDIC membership on philosophical grounds. As summed up by one savings banker, "I for one want none of this FDIC. If it's New Deal, that damns it as far as I'm concerned."[22]

Pursuant to the intent of Congress, the FDIC accepted for insurance all banks that it found to be solvent. However, it was recognized that a great many banks lacked sufficient capital, which posed a huge risk for the insurance fund. Some banks were admitted upon a commitment to increase their capital, either from the RFC or local interests. A program of reexamination and rehabilitation was carried on throughout the year by the FDIC.

Organizational changes. Following the departure of Walter J. Cummings, E. G. Bennett served briefly as acting chairman of the FDIC. In February 1934, Leo T. Crowley, a 46-year-old bachelor, became chairman. As former owner of several Wisconsin banks during the Depression, he had organized and headed the Wisconsin Banking Review Board. In December 1933, he journeyed to Washington, D.C., seeking

[22]Oscar Schisgall, *Out of One Small Chest* (New York: AMACOM, 1975), p. 146.

aid for several hundred Wisconsin banks so they could qualify for deposit insurance. His role in restoring the health of Depression-struck banks in his native state brought him to the attention of the Roosevelt Administration.

The appointment of Crowley proved to be especially felicitous. An imposing man, he possessed both a witty personality and exceptional administrative skills. He left an indelible imprint on the FDIC during his 12-year term as chairman.

Legislative developments. The Banking Act of 1933 provided for termination of the Temporary Federal Deposit Insurance Fund and the inauguration of the permanent insurance plan on July 1, 1934. However, in the early part of 1934, FDIC officials recommended that the Temporary Federal Deposit Insurance Fund be extended for another year and that the law be amended in certain minor respects to facilitate administration. It was considered advisable to give the states additional time to adopt legislation to enable state banks to enjoy the full benefits of federal deposit insurance. FDIC officials also desired to gain more experience with the administration and operation of an insurance plan prior to the inauguration of the permanent plan. Moreover, the capital rehabilitation program for banks could not have been completed by July 1934, as required, to permit all banks insured with the Temporary Federal Deposit Insurance Fund to qualify for insurance under the permanent plan.

On June 16, 1934, Congress extended the life of the Temporary Federal Deposit Insurance Fund, and the effective date of the permanent plan was postponed one year, to July 1, 1935.[23] Insured nonmember banks were allowed to terminate their membership in the Temporary Federal Deposit Insurance Fund on July 1, 1934, provided they gave adequate notice to the FDIC. Provision was made for refunding the assessments collected from the banks that withdrew. Only 21 commercial banks elected to withdraw from the fund.

There had been some doubt as to the legality of some mutual savings banks qualifying as members of the permanent plan of deposit insurance. Furthermore, many mutual savings banks considered themselves preferred risks and wished to avoid assessment at the same rate as commercial banks. For these and other reasons, 169 mutual savings banks withdrew from the Temporary Federal Deposit Insurance Fund at the end of June 1934. Of these, 133 were located in New York State. Only two New York mutual savings banks, Emigrant Savings Bank and Franklin Savings Bank, kept their insurance with the FDIC.

Effective July 1, 1934, insurance protection was increased from $2,500 to $5,000 for each depositor at an insured institution, except in the case of certain mutual savings banks. Insurance protection remained at $2,500 for each depositor at a mutual savings

[23]The life of the temporary plan subsequently was extended for an additional two months. The second extension was approved June 28, 1935, while the Banking Act of 1935 was under consideration, and was designed merely to continue the temporary plan until that Act could be approved.

bank except that any mutual savings bank could, with the consent of the FDIC, elect to be insured up to $5,000.

At the discretion of its Board of Directors, the FDIC was authorized to set up a separate fund for mutual savings banks to be known as the Fund For Mutuals. The Temporary Federal Deposit Insurance Fund was not to be subject to the liabilities of the Fund For Mutuals, and *vice versa*. A separate Fund For Mutuals was established by the Board of Directors on July 14, 1934, effective July 1, 1934. Upon inception of the permanent plan in 1935, this fund and the fund for commercial banks were consolidated.

Under the previously existing law, insured nonmember banks were required to apply to become members of the Federal Reserve System on or before July 1, 1936, in order to continue their insurance. With the one-year delay in the establishment of the permanent fund, this requirement was changed by pushing the date back to July 1, 1937.

Banks in the territories of Hawaii, Puerto Rico, Alaska and the Virgin Islands were made eligible for insurance. In addition, the language authorizing the FDIC to act as receiver in the case of failed insured banks was clarified. By a new provision of the law, each insured bank was required to display signs to the effect that its deposits were insured by the Federal Deposit Insurance Corporation. The intent of this practice, which continues today, was to make the absence of such a sign conspicuous.

Deposit Insurance and Banking Developments in 1934

Total deposits in insured and uninsured licensed commercial banks increased during 1934 by about $7.2 billion dollars, or 22 percent. This growth in deposits had rarely been equaled in the past and restored to the banking system approximately half of the decline in deposits that had occurred during the preceding three years.

The growth in bank deposits was accompanied by changes in the character and quality of the assets held by insured banks. Cash, amounts due from other banks and holdings of direct obligations of the United States government increased considerably. The average quality of the assets of insured commercial banks improved as large amounts of worthless and doubtful assets were written off. Increased earnings and new capital, which was obtained from the RFC and local interests, maintained banks' capital positions. At the close of 1934, insured banks held 98 percent of the assets of all licensed commercial banks.

The liquidity buildup undertaken by banks during 1934 caused FDIC officials some concern. They feared that excessive holdings by banks of cash and government securities could stifle economic recovery. Speeches given by the FDIC's directors during that period frequently contained exhortations urging bankers to expand their loan portfolios.

Only nine insured banks and 52 uninsured licensed banks suspended operations during 1934. All but one of the insured banks and most of the uninsured licensed banks that failed during 1934 were small institutions. More than 900 banks that were not licensed after the holiday were placed in receivership or liquidation. More than half of these banks had a part of their assets and liabilities taken over by successor banks.

In its 1934 *Annual Report*, the FDIC rather modestly attributed the small number of failures of licensed banks to factors other than deposit insurance. It noted that many banks were able to survive because they had received necessary financial assistance from the RFC and other governmental agencies. Secondly, events during 1933 had weeded out many weak banks. Third, improved economic conditions also had played a role in keeping down the failure rate. The FDIC warned that the low rate of failures could not be expected to continue.

During 1934, the fierce opposition of the banking industry faded in the face of the success of deposit insurance. The industry's changed attitude was reflected in the public endorsement of the temporary insurance plan by the Executive Council of the American Bankers Association in April of that year. Public sentiment continued to support deposit insurance.