no direct control, because they are creatures of the States, and not of the national Government, might become members of the system if they met certain specified requirements, but it was purely voluntary with them. But, no way was provided for a State bank to withdraw from the system after it once became a member. So that although there were over 15,000 State banks, and Trust companies, in the United States, only 65 of them up to June, 1917, had become members of the Federal Reserve system. The held back. They would say, "we do not know enough about this experiment." Some of them thought pretty well of it, but they did not like to get into a place from which they could not get out; and it was not until the United States entered the war and not until Congress amended the Act by providing that State banks might withdraw on six months' notice, that they came in; and even then, only a comparatively small number, I think about 1,600 or 1,700 State banks and Trust companies are members of the system but in this number are included most of the larger institutions.

The capital stock of the Federal Reserve Bank is a variable quantity. Each member bank must subscribe for stock in the Federal Reserve Bank of its district to the amount of six per cent of its capital and surplus or rest, of which three per cent must be paid in and the other three per cent is subject to the call of the Federal Reserve Board. The Board has never called for the payment of this three per cent and I do not think it ever will. When a bank increases its surplus, it must subscribe for a proportionate additional amount in Federal Reserve Bank stock; it must increase its holdings there. And whenever a bank goes into liquidation, it must return its stock, receiving the cash plus the accrued dividend. At first only one bank, the Federal Reserve Bank of Richmond had sufficient borrowings to enable it to have sufficient earnings to pay a dividend. The banks were in arrears. They had dividends piling up, which had not been paid, and it was not until 1918, a year after we went into the war that all the banks had accumulated sufficient earnings to enable them to take up their back dividends.

There has always been a question in my mind as to what the development of the Federal Reserve system would have been if we had not gone into the war, because the war changed the whole situation. We had the First Liberty Bond issue, and then the second, third and fourth, and the Victory Loan issue. The national debt of the United States on April 2nd, 1917, was in round numbers, $1,000,000,000, on August 1st, 1919, the national debt of the United States stood at over $26,500,000,000, an increase of over $25,000,000,000 in a year and a half. That meant enormous expansion or inflation. We maintained the gold standard. Our Federal Reserve notes were always at a parity with gold, but the Federal Reserve System was obliged to adapt its policies to the needs of the Treasury. The Treasury policy was to finance the war one-third by taxation, and two-thirds by bond issues, and in order to float these tremendous bond issues the Federal Reserve Banks became great bond-selling organizations. The Governor of each Federal Reserve Bank was the organizer in his own district, and the member and non-member banks became large buyers of bonds, and urged their customers to buy bonds, and were encouraged to make loans on bonds and to rediscount with the Federal Reserve Banks. The Treasury fixed the rate of interest on the bonds low in order to save money, and it was necessary that the Federal Reserve Banks should fix their discount rates at a correspondingly low figure. The Reserve bank rate was much lower than if it had been considered from an economic standpoint, but in war time, one cannot stress economy or economics. War itself is the most uneconomic of all processes. We were in the fight and we were going to muddle through with it, so, we maintained a low rate, say, four per cent interest, all during the war, and during the Victory Loan period when the Treasury had to float

[Mr. W. P. G. Harding.]