CHAPTER FIVE

JEKYLL ISLAND AND THE ALDRICH BILL

Two and one-half years had passed and the National Monetary Commission had still not made its report to Congress. Henry Davison, a Morgan partner and consultant to the commission, suggested to Aldrich that a few trusted advisers form a working party for the purpose of drafting a banking reform bill that could be presented to Congress as the result of the work of the National Monetary Commission. The ideal location, he thought, was a remote private island off the southeastern coast of Georgia, which J. P. Morgan and other wealthy moguls used as a hunting and recreation retreat. According to Davison’s biographer, Thomas Lamont (1933, p. 97), Aldrich agreed and asked Davison to select the participants; they were sworn to secrecy by Aldrich and were to travel incognito to avoid contact with the press. Stephenson (1930, p. 376) relates that when the party arrived at Brunswick, Georgia, the station master greeted them with a surprising remark: “We know who you are and reporters are waiting outside.” Davison is reported to have said “Come out, old man, I will tell you a story . . .” We do not know what Davison told the station master, but when he returned smiling, he said “they won’t give us away.” The reporters disappeared and no more was heard of the Jekyll Island rendezvous until it was revealed by Stephenson in his biography of Nelson Aldrich published in 1930.

The participants included Aldrich, his personal secretary Arthur Shelton, Henry Davison, Frank Vanderlip, Paul Warburg, and A. Piatt Andrew. Vanderlip (1935, p. 213) in his memoirs claimed that a seventh person was also present, Benjamin Strong, vice-president of Bankers Trust and future governor of the Federal Reserve Bank of New York: “Those who had been asked to go were Henry Davison, Paul Warburg, Benjamin
Strong and myself. From Washington came A. Piatt Andrew who was then Assistant Secretary of the Treasury." There is no reference to a Jekyll Island meeting in Chandler’s (1952) biography of Strong. Nor does Stephenson (1930, p. 375) identify Strong as a participant. In an oral interview Andrew granted Everett Case he failed to mention Strong as a member of the working party: “The first rough draft of a bill was actually evolved at the famous meeting at Jekyll Island, attended by Mr. Davison, Mr. Warburg, and Mr. Vanderlip, as well as the Senator, his secretary and myself. This was in the Winter of 1909 [sic], I think, and the meeting was kept secret lest it be charged that Wall Street was dictating the bill.” In a private memorandum prepared for Davison’s biography by Thomas Lamont (1933, p. 98), Paul Warburg wrote:

The small party, consisting of Senator Aldrich, Mr. Shelton, secretary, and Professor A. Piatt Andrew, special assistant to the Monetary Commission, Davison, Frank A. Vanderlip, and myself, set out on its trip to Jekyl [sic] Island in November, 1910. It spent a week in complete seclusion and privacy, and it developed and formulated then and there the first draft of what later became known as the Aldrich bill.

The evidence seems to point clearly in the direction that Strong was not at Jekyll Island. But it leaves unexplained Vanderlip’s lapse of memory. Neither Vanderlip nor Warburg was associated with the National Monetary Commission. Davison had acted as a special consultant to Aldrich on banking matters and had accompanied the commission on its trip to Europe in the summer of 1908. And Andrew had been a special assistant to the commission, but at the time of Jekyll Island he was assistant secretary of the treasury. There is no record of the proceedings of the Jekyll Island meeting. Aldrich’s private secretary, who was also present, took stenographic minutes, but they were either lost or destroyed. Aldrich’s request for absolute secrecy was honored. Even after the veil of secrecy was lifted with the publication of Stephenson’s biography of Aldrich, we still do not know what each of the participants contributed, with the possible single exception of Warburg, who had published a draft of a central bank proposal. Vanderlip, as quoted by Stephenson (1930, p. 484), wrote many years later: “none of us knew certainly what Mr. Aldrich wanted in the way of a new banking bill. As a matter of fact Mr. Aldrich knew about as little of what he wanted as we did.” But that uncertainty did not extend to the necessity for a central bank. As we have seen, Aldrich had become a convert after the visit of the commission to Europe in the summer of 1908. Vanderlip and Warburg were already on record as favoring a central bank
that could issue an asset-based currency. What the working party had to decide was: What kind of central bank?

The Jekyll Island meeting was remarkable for a number of reasons: not only was the public not informed about such a meeting but also members of the Monetary Commission remained in the dark as well; Andrew was serving as assistant secretary of the treasury, and his participation was unknown to Secretary of the Treasury Franklin C. MacVeigh. The idea that an official of the Taft administration was directly involved in the drafting of a banking reform bill without knowledge of the administration was probably without precedent. Even more anomalous was the fact that three Wall Street bankers were enlisted to draft a banking reform bill! Had their presence become known, Aldrich’s credibility would have suffered a serious setback. Aldrich certainly understood the political risk he was taking in convening a secret meeting of Wall Street bankers. Only Aldrich’s conceit and contempt for the contribution of the members of the commission could have induced him to undertake such a daring and risky adventure. Although the participants with the exception of Andrew were well known in their day, time has not been kind to any of them. To remove some of this ignorance, I provide brief sketches of each member of the group, beginning with its leader Senator Aldrich.

NELSON ALDRICH

Agitation for banking reform in the United States was almost continuous in this country after 1894. But the voices for reform rarely attained national attention. Proposals multiplied for an asset-based currency to replace the bond-secured currency mandated by the National Banking Act. Branch banking and deposit insurance were also considered as possible solutions to the banking panic problem. Numerous bills were introduced into Congress but without gaining congressional approval. Leadership was lacking. The tariff question preempted banking reform considerations, and there had been no serious banking panic since 1893. The archconservative leader of the Republicans, Senator Nelson Aldrich, according to his biographer Nathaniel Stephenson (1930, p. 223), preferred to “let sleeping dogs lie.” The sleeping dogs could no longer lie after the panic of 1907, which was a catalyst for banking reform. Thereafter, the pace of reform quickened, leading ultimately to the passage of the Federal Reserve Act.

The key player in the movement for banking reform was Nelson Aldrich, the six-term senator from Rhode Island (figure 1). His contributions to the establishment of the Federal Reserve System were deliberate-
ly obscured by Carter Glass (1927, pp. 239–44) and Parker Willis (1923, p. 523), who took great pains to denigrate his influence. To admit that Aldrich might have influenced the Glass-Owen bill would be to repudiate the plank in the Democratic platform that was opposed to a central bank and the Aldrich bill.

Aldrich was well qualified for the dauntless task before him. His experience in the Senate was unrivaled. No other Republican had dared challenge his leadership. Tariff legislation had been his chief claim to political and national recognition. Although a staunch conservative with a Hamiltonian conception of a strong central government, he had a firm grasp of the persuasive and other parliamentary skills for moving legislation successfully through Congress.

Before 1903, most of his attention was directed at tariff legislation and the protection of manufacturing interests. However, as early as 1903, Aldrich, according to Stephenson (1930, p. 216), “buckled down to the task of learning about the theories of banking and currency.” He had drafted a banking bill which gave the secretary of the treasury the power to use obligations other than those of the federal government as security for
deposits of public money. But it went nowhere. However, as a consequence of his lack of success, he appointed a subcommittee of the Finance Committee to consider the necessity for banking legislation. The subcommittee held one meeting. Nothing came of it except to turn Aldrich's interests in a new direction.

We hear no more from Aldrich about banking reform until the aftermath of the 1907 banking panic. He introduced a bill in the Senate to provide an emergency currency. The measure was intended only as an interim gesture until a more permanent solution could be worked out. The Aldrich-Vreeland Act (1908) created the National Monetary Commission—nine members of the Senate and nine members of the House with Senator Aldrich as Chairman—to study monetary and banking conditions both in the United States and abroad with a view to serving as a basis for discussion and fruitful legislation.

His senatorial experience was as much a weakness as it was a strength. It gave him a firm grip on senatorial power that was unrivaled, and with the sense of power a certain arrogance and aloofness and seeming indifference to the views of most of his colleagues in Congress. Aldrich was in the habit of having things his own way without having to defer to the judgment of others. His initiatives were rarely blocked, but it was becoming increasingly difficult to bring them to fruition.

Piatt Andrew (Gray, 1971, p. 73) recalled that the Monetary Commission was a “one man show completely dominated by Senator Aldrich who thought this was his one opportunity for enduring fame.” Aldrich expected little help from commission members, all of whom according to Andrew “he knew he could control.” He simply wanted to keep them happy until the bill was forthcoming and then get their approval. Nor did he expect much help from his colleagues in the Senate. He sought advice from bankers, financial writers, and economists.

In addition to the congressional members of the commission, Aldrich asked Henry Davison, a Morgan partner, to be a special consultant on U.S. banking practice, as well as George Reynolds, president of Continental Illinois Bank in Chicago. A. Piatt Andrew, an assistant professor, was enlisted with the aid of President Eliot of Harvard to be chief economist. These four were entrusted with the real work of the commission.

One of the first tasks of the commission during the summer of 1908 was to visit various European capitols and to conduct interviews with central bank officials and distinguished bankers. The stenographic minutes of these meetings were published among the twenty scholarly volumes for the commission. Davison played an important role in arranging these meetings, as stated previously.
Aldrich had partially overcome his strong commitment to a bond-secured currency when he agreed to sponsor an asset-based currency proposal in the Aldrich-Vreeland Act in 1908. But he still had to be persuaded of the desirability of a central bank. The commission's European trip convinced Aldrich of the necessity for a central bank and removed whatever doubts still existed about the desirability of an asset-based currency that would expand and contract to meet the needs of business. German banking practice was responsible for his conversion. Representative Theodore Burton of Ohio, a commission member, dated Aldrich's conversion to that visit.

Returning home from the foreign trip, he had formulated two of the cornerstones of fundamental banking reform: a central bank (on the order of the Reichsbank), and an asset-based currency—a necessary instrument to provide an elastic currency. The technical details of establishing a central bank and an asset-based currency he left to be worked out later.

As the time approached when the commission would have to report to Congress, Davison as we have seen suggested to Aldrich that a secret meeting be held at Jekyll Island with a view to preparing a bill. Aldrich knew what he wanted for his two cornerstones. And Warburg knew specifically what he wanted in the form of a central bank, for he had previously published his United Reserve Bank plan. The problem at Jekyll Island was to reconcile the conflicting conceptions of what ought to be done. There was no controversy as far as we know about the control problem. All agreed that the central bank should be controlled by the bankers and not by the government, though there was plenty of room between control by the banks and control by the government. The Jekyll Island meeting was a success. A tentative plan for banking reform emerged which became the basis for the Aldrich bill.

The remarkable feature of the Aldrich bill was how it came to be drafted. The National Monetary Commission was to study and report to Congress on needed banking reform. Autocrat that he was, Aldrich did not envision any substantive role for the commission members in drafting either the final report or the bill. Nor did he assign any significant role either to the House or Senate committees for banking legislation. The drafting of a bill was a matter for experts, not members of Congress inexperienced in banking and financial matters. The Aldrich strategy was to leave the work of preparing a report and a bill to himself and his chief aides, and then to keep members of the commission sufficiently informed about their progress to ward off any impending criticism. Only after the bill had been drafted did he show the bill to interested parties.

Unlike the case with other pieces of major legislation, the Congressional committees did not play an active role. There were no hearings to solicit
interested opinion prior to drafting the bill. The bill was put together, as we have explained, by Aldrich himself and his New York banking associates at the clandestine Jekyll Island rendezvous. Aldrich was confident that he could sidestep traditional procedures without jeopardizing the bill’s passage, but only if the Jekyll Island meeting remained absolutely secret. The entire political hubbub about the fear of influence exercised by Wall Street Aldrich ignored, inviting three of the most prominent New York bankers to participate in the drafting of the bill. No more arrogant gesture can be imagined. And only Senator Aldrich would have dared to pull it off. He and his associates argued that every precaution had been taken in the bill to keep the influence of Wall Street to a minimum and suggested that the fear of Wall Street control was groundless! No one knew that Wall Street bankers drafted the bill!

Despite Aldrich’s efforts to the contrary, the bill was regarded as a partisan political measure identified not only with Senator Aldrich but the Republican party as well. The Democratic platform specifically rejected both the Aldrich bill and the idea of a central bank. And Carter Glass never tired of insisting that the Democratic party had rejected the Aldrich proposals.

HENRY DAVISON

Henry Davison (figure 2) had been a Morgan partner for less than two years when, according to his biographer, he took the initiative to recommend to Senator Aldrich that a small group be assembled at the remote Jekyll Island Club for the purpose of crystallizing ideas about banking reform and perhaps formulating a draft of a bill. Lamont (1933, p. 97) stated: “Senator Aldrich eagerly accepted Davison’s suggestion and left him to make up the party.” It was Davison, not Aldrich, who selected the participants.

Aldrich had invited Davison to be an adviser to the National Monetary Commission; he accompanied commission members to Europe in the summer of 1908 and aided in questioning European central bankers who made themselves available for that purpose. He was not a technical adviser but “one who could bring to bear on the Commission’s study a common sense knowledge of banking as it was practiced in the financial center of the United States.”

What these skills were as specifically displayed at the Jekyll Island cabal was later described by Warburg in Lamont (1933, pp. 98–99): “Warburg emphasized Davison’s uncanny personal skills in handling people and getting things done. Moreover, he was able to defuse awkward moments
when tempers flared.” As a “facilitator” he kept the discussion on track. We do not know what contributions he made to the technical discussion. His people skills were well known.

We have further evidence of his special skills in the role that he played during the 1907 panic. At the time he was vice president of the First National Bank, of which George Baker was the head. As the chief protégé of Baker he gained the attention of J. P. Morgan, who along with Baker and James Stillman took the initiative in proposing various panic preventive measures. In a long letter to Lamont (1933, p. 83) Benjamin Strong described Davison’s contribution: “He was the commanding general over the forces in the field. Behind him was the general staff, primarily Mr. Morgan, Mr. Baker, and Mr. Stillman.” And “It was in dealing with the human equation that Harry’s supreme talent was shown. He reconciled different views, calmed the uneasy and anxious, he inspired the timid, sometimes disciplined the cowardly, but with it all his courage never flagged, his industry was unceasing and his good temper never failed him.” These were the qualities especially admired by Morgan and later by
Aldrich, who observed Davison at his best while interviewing European central bankers for the Monetary Commission and at Jekyll Island.

FRANK VANDERLIP

Frank Vanderlip (figure 3) was the chosen successor to James Stillman, president of National City, the largest bank in New York. But at the time of the Jekyll Island meeting he was still a vice president. Davison, Vanderlip, and Warburg represented a younger generation of successful bankers who were eager to assume the leadership mantle of their predecessors—Morgan, Stillman, and Baker. Davison and Warburg were partners in two of the largest investment banking houses—Morgan’s and Kuhn, Loeb, and Co.

Vanderlip’s preparation for his banking career was a sharp departure from traditional practice. He was a journalist by profession, who had served as a financial reporter for the Chicago Tribune and later became editor of the Chicago Economist. When Lyman Gage, a Chicago banker, became secretary of the treasury, he invited Vanderlip to join him and later serve as an assistant secretary. After his short stint at Treasury, James Stillman offered him a position at National City Bank with a view to making him his successor. At the time of his appointment he had no experience as a commercial banker, but he was undeterred by his lack of knowledge. He (Vanderlip, 1935, p. 102) wrote in his memoirs: “I knew more of the philosophy of banking than the whole bunch of them [officers of the bank]. I had read and written and thought a great deal about our banking system.” At least two of the “eminent men” to whom he referred were Adolph Miller, one of the first appointees to the Federal Reserve Board, and J. Lawrence Laughlin. If there were no evidence to the contrary, guilt by association might place Vanderlip squarely in the real bills camp, for Laughlin and Miller were both adherents of the real bills doctrine.

His enthusiasm for banking reform was expressed as follows (1935, p. 181): “Ben Strong was equally zealous in his advocacy of change, and I wrote articles, delivered speeches and argued with every banker with whom I came in contact.” He had played an active role in the Chamber of Commerce committee to study currency and banking reform; he had joined with them in the movement for banking reform by at least 1905, if not earlier. As a member of the New York Committee in 1906 he had joined in proposing a central bank as an alternative to Treasury control, the use of the discount rate as the appropriate instrument for controlling the expansion of bank credit, and an asset-based currency. He was also one
of the two Chamber of Commerce representatives to meet with the American Bankers Association considering banking reform. This latter committee recognized what was indeed remarkable at the time, that the issue of an asset currency did not entail a commitment to the strong form of the real bills doctrine. The committee considered the doctrine fallacious for the familiar reason that the same transactions could be the basis for a succession of commercial bills. We do not know whether Vanderlip agreed with the views of the committee, but if he did, it was a sharp turnabout from the views of his former teachers Miller and Laughlin.

**PAUL WARBURG**

Paul Warburg (figure 4), a member of a distinguished family of German bankers, moved to the United States in the fall of 1902 partly at the initiative of his American wife, Nina Loeb, daughter of the founder of Kuhn, Loeb and Co., investment bankers. He joined the investment banking firm as a general partner. His knowledge of European banking and of central banking in particular was unrivaled. From the time of the 1907 panic
Warburg began his campaign to reform the U.S. banking system. Shy at first and self-conscious about his German accent, he ventured slowly into the public arena. In speeches, articles in financial journals, and frequent contacts with leading New York bankers, he diagnosed our banking ills and suggested a remedy in the form of what he here called the United Reserve Bank, literally a blueprint of the technical clauses that were embodied in the Aldrich bill and later in the Federal Reserve Act. The United Reserve Bank was a central bank with 20 branches and a share capital of $100 million divided among the banks of the country, but dividends were limited to 4 percent. Local banking associations were to be created for the purpose of guaranteeing paper eligible for discount with the United Reserve Bank. The ideas of a central bank with branches financed by share capital with a fixed dividend were embodied in the Aldrich bill.

His most important recommendation, however, was the establishment of a discount market hitherto absent in the United States and, in his opinion, the cause of our banking woes. Most U.S. banks possessed no liquid asset upon which an elastic currency could be based. The promissory
note—the credit instrument predominant among American bankers—was not a marketable asset and could not be disposed of easily in an emergency. The promissory note might be a “real bill,” that is, a bill created for the specific purpose of financing goods in transit, presumably self-liquidating, but without endorsement. Warburg insisted that neither promissory notes nor any other bank asset could be liquidated in an emergency. The only ultimate source of liquidity in a banking or financial crisis was a central bank which was conspicuously absent in the United States before 1914. To establish a discount market, two revolutionary changes in American banking practice were necessary: (1) the replacement of the promissory note by a bill of exchange similar to bills of exchange in France, Germany, and Great Britain in the portfolios of commercial banks; and (2) the creation of a central bank that would stand ready to purchase these bills at the discretion of the seller. The two could not in his opinion be separated.

Warburg made it quite clear that profit should not be a prime motivating force in the operation of the United Reserve Bank. To avoid the possibility that earnings considerations would dictate behavior, he recommended that the government should contribute to the expenses of the United Reserve Bank such a lump sum that it will be able to pay shareholders the fixed 4 percent dividend.

In his 1930 book Warburg refers to the Jekyll Island meeting, though not by name. He wrote: “Though 18 years have gone by, I do not feel free to give a description of the most interesting conference concerning which Senator Aldrich pledged all the participants to secrecy.” He knew that Stephenson’s biography of Aldrich was about to be published. True to his word he does not tell us what went on at the conclave, but he did comment on Senator Aldrich as a person and as a politician. Warburg was especially impressed with Aldrich’s nonpartisan approach. His great political power he attributed to “his indefatigable, painstaking willingness to ascertain the facts down to their last details.” Although Aldrich seemed committed at the outset to a full-fledged central bank in the European sense, by the time the conference ended that rigid model had been abandoned. He indicated the items in the Aldrich bill with which he most disagreed—namely, the question of control. He preferred more government representation. He also took exception to a uniform discount rate.

Unlike the other Jekyll Island participants, at least some of Warburg’s contributions are readily identifiable. Provisions of his United Reserve Bank proposal (March, 1910) appear directly in the Aldrich bill:

1. The creation of local associations and central bank branches in the cities where the head offices of the local associations were located
2. Share capital as a source of funding
3. Creation of a discount market with two-named commercial paper not having more than 28 days to maturity
4. Fixed dividends of 4 percent with excess earnings returned to the U.S. Treasury
5. Purchase and sale of government securities

The resemblance between the provisions of the United Reserve Bank and Aldrich’s National Reserve Association was not a coincidence. There were quite a number of differences as well. Nevertheless, the main blueprint for the Aldrich proposals had been laid out by Warburg, and he deserves more credit than the rest for the so-called technical contributions.

A. PIATT ANDREW

A. Piatt Andrew (figure 5) was an assistant professor of economics at Harvard University when he was recruited by Aldrich at the recommendation of Harvard’s President Charles W. Eliot to serve the National Monetary Commission in a variety of capacities: special assistant of the commission, consultant to Aldrich, research director and editor of more than 20 volumes sponsored by the commission. His more distinguished colleague at Harvard, Oliver Sprague, was also a money and banking specialist, but he had expressed earlier his opposition to a central bank. After completing his work for the commission Andrew did not return to Harvard. President Taft appointed him director of the mint in August 1909, and in the following year (June 1910) he became assistant secretary of the treasury. He was assistant secretary at the time of the Jekyll Island meeting.

In a special memorandum prepared for Stephenson’s biography of Aldrich, Andrew indicated that on the journey commission members made to Europe to study European central banking practice, he attempted to acquaint them with the basic principles of money and banking. He wrote (Stephenson, 1930, p. 335): “Many of its members were no real students of monetary matters.”

A parallel with Parker Willis, Carter Glass’ assistant in the preparation of the Glass bill, readily suggests itself. Both were economists whose specialty was money and banking. Willis was the principal drafter of the Glass bill, whereas that responsibility fell collectively on the Jekyll Island participants. Willis was an adherent of the real bills doctrine. Andrew was not. Both acknowledged the origins of the proposed legislation in the Clearing House Associations in the United States.
Andrew identified the multiple purposes of the Aldrich plan:

- To prevent banking panics
- To relieve seasonal stringencies in the money market
- To control stock market speculation by the diversion of funds from the money market
- To make bank notes and reserves more responsive to business needs
- To provide new facilities for foreign trade

These objectives differed in no important ways from those of the Glass-Owen bill.

He predicted that the suggested banking reform would create a larger market for short-term obligations, a more restricted market for stock exchange collateral, lower rates for commercial paper and higher rates for call loans, greater stability of interest rates, and a gradual convergence of regional interest rates. He was perhaps overly sanguine when he said the country would never again be obliged to suspend cash payment, and the banks would always be able to convert their sound commercial paper into...
Andrew pointed out that the recognition of broader responsibilities of the clearinghouses to include banking stability was distinctly an American tradition without a European counterpart. Moreover, the issue of control was resolved by employing the device of the federal principle already embodied in our political structure. Andrew concluded (Stephenson, 1930, p. 28): “The proposed plan in its narrow outlines is only a perpetuation, legalization, and rationalization of the ingenious but illegal local makeshift in the past.” The illegal makeshift to which he referred was the suspension of cash payment by the New York Clearing House.

These short sketches of the Jekyll Island participants are revealing. Senator Aldrich had recruited a younger generation of New York bankers as his special advisers but not without the implicit approval of Morgan, Baker, and Stillman. Vanderlip, Davison, and Warburg personified Wall Street; they represented two of the largest investment banking houses, Morgan’s and Kuhn, Loeb and Co., and the largest commercial bank in the city. No one in the United States was better qualified than Warburg, whose knowledge of European banking and European central banks was unmatched. He had produced the first, detailed concrete proposal for a U.S. style central bank. And Vanderlip had gone on record as an advocate of a U.S. central bank. We have seen that Aldrich himself had become a convert to a central bank after the Monetary Commission’s trip to Europe in the summer of 1908. The main issue, therefore, at Jekyll Island was not whether a central bank, but what kind. Aldrich had loaded the deck from the very outset. He also felt certain that the commission members would go along even if they had no idea how the Aldrich plan worked or by whom it had been devised. One of the great anomalies of U.S. financial history is how Wall Street bankers managed to play the role they did while politicians and the public were decrying Wall Street domination and influence! No one else but Aldrich would have attempted it. No one else would have succeeded.

Submission of Aldrich’s suggested plan to the Monetary Commission in January 1911 was the occasion for the preparation of a strategy by Aldrich and his Jekyll Island associates to obtain broad political support. Included in the strategy was a campaign to educate the public on the necessity for banking reform. Warburg was instrumental in the formation of a National Citizens’ League to serve such a purpose and to assure wide geographical participation. J. Lawrence Laughlin was enlisted to serve as executive director and to deflect attention away from Wall Street and the influence of the eastern financial interests. Laughlin, to the bewilderment of Warburg, conceived the league as nonpartisan and noncommittal about
the Aldrich bill. Tension ran high between Aldrich’s supporters over Laughlin’s conception of why the Citizens’ League had been created.

The strategy also included extensive speaking engagements by Senator Aldrich and his associates, especially to the large associations of bankers and businessmen. How successful the Aldrich strategy was in winning wide public support is still open to some dispute. But the campaign was highly successful in focusing public attention on banking reform and the leading issues in the debate. It contributed to molding public opinion favorably disposed to a U.S. style central bank, which would pay dividends when the Glass-Owen bill came up for consideration in 1913. When the Democratic administration assumed office in 1913, the groundwork had been laid by Aldrich and his supporters. All that remained to be done was to formulate a new proposal in the light of the preferences of the new administration.

THE ALDRICH PLAN

Barely two months after the Jekyll Island conclave Aldrich submitted a plan for banking reform to the National Monetary Commission entitled “Suggested Plan for Monetary Legislation.” The pamphlet was dated January 16, 1911. It was not a bill in legislative format but an outline of the structure of a new financial institution called the Reserve Association of America, whose objectives could be achieved “without the creation of such a central bank” as existed in Europe. Aldrich modified his “Suggested Plan” in October 1911. The final report of the commission was sent to Congress in January 1912 along with a bill—the Aldrich bill—introduced in the Senate at the same time. Aldrich’s original plan, the revised October version, and the formal 1912 bill were similar. A few important changes were made in each draft, but the substance remained unchanged. The name of the new institution was modified slightly from Reserve Association of America to National Reserve Association.

The January 1911 report muted the effect of the recommended changes by stating its aim was to liberalize the national banking system rather than to formulate a plan that would fundamentally change it. The Aldrich plan called for greater cooperation among the banks through a formalized structure, the effect of which should be the elimination of banking panics. The functions of the new institution included: to be the fiscal agent of the Treasury, the issue of paper money, the discount of commercial paper, centralization of the reserve, and the clearing and collection of checks.

The Aldrich plan for a central bank embodied two principles that distinguished the National Reserve Association from its European counterparts: the federal principle and democratic governance. Centralization and auto-
ocratic governance characterized European central banks. The division of the Aldrich system into local and district associations and a national association of banks reflected its federal structure, and the election of boards of directors by the member banks, its democratic control. A third principle—the principle of voluntarism—was reflected in the membership criteria. The earlier version of the Aldrich plan had confined participation to national banks on a purely voluntary basis with a minimum capital of $25,000. The October version extended membership to state bank and trust companies who were prepared to purchase stock in the association equal to 20 percent of their capital, the same as national banks. A fourth principle, if it may be called a principle, was embodied in the distribution of earnings, the principle of constrained profit maximization. Dividends were limited to 4 percent, additional earnings being apportioned to surplus with a fixed limit of 5 percent to shareholders; any excess beyond the specified distribution would accrue to the government in the form of a franchise tax.

Reflecting the federal principle, each participating bank belonged to a local association of banks no less than ten in number with a minimum capital of $5 million. The function of the local associations was to approve the application of each bank for a guarantee of the commercial paper that it desired to discount with the District Reserve Association. The local associations of banks were combined into 15 branches with the authority to discount notes and bills of exchange carrying the endorsement of the bank requesting the discount. These discounted notes would presumably have arisen out of commercial transactions having a maturity of no more than twenty-six days. The discount rate would be the same for all district branches. The authority, however, for raising and lowering the rates resides with the National Reserve Association, and not the separate branches. The function of the fifteen branches were: (1) to hold the reserves of the participating banks in the district; (2) to issue currency notes; (3) to discount paper; (4) to transfer balances between branches; and (5) to perform all operating functions including the clearing and collection of checks.

The principle of democratic control was embodied in provisions for the election of boards of directors at the local, district and national levels. At the base of the governance pyramid were local associations that elected a board of directors, three-fifths of whom were chosen on the one bank–one vote principle, the remaining two-fifths being chosen according to the number of bank shares, reflecting bank size. The selection of the directors of each of the fifteen branches was slightly more complex. Each local association would select one board member. In addition, a number of directors equal to two-thirds of the number of local associations within the district were selected, each bank having as many votes as its holding of shares in the National Reserve Association.
At the apex of the governance pyramid was the National Reserve Association, with power to set uniform discount rates, buy and sell securities, and supervise the operations of the fifteen branches. In the initial version there were forty-five directors of the National Reserve Association including six ex-officio members: the governor, two deputy governors, and the secretary of the treasury, secretary of commerce and labor, and the comptroller of the currency. An executive committee of nine members would be chosen by the directors and would be responsible for daily operations. The head of the association was the governor, who in the initial version would be chosen by the president from a short list submitted by the directors. In the original version he could be removed by the president. At the initiative of the ABA that was changed in the October version to removal by a two-thirds vote of the directors. None of the ex-officio cabinet members served on the Executive Committee.

The composition of the national board was modified in the final bill: fifteen directors were chosen by the branches to represent agriculture, commerce, industry and others; nine additional directors would be elected, with each branch casting as many votes as the number of shares held by the banks in that branch. A seventh ex-officio member was added, the secretary of agriculture. Control of the National Reserve Association was lodged with the banks. Although Aldrich acknowledged that the public had a vital interest in its behavior, control remained firmly in the hands of the bankers.

The Aldrich plan was an imaginative blueprint for a U.S. style central bank with distinguishing organizational and governance features. The fifteen branches were more than fifteen operating arms of the association. They were fully autonomous units in the administration of discounts, although they lacked the discretion to vary the discount rate. Banker control was manifest from the local to the national level. The whole governance apparatus was designed to minimize partisan political control as well as domination by a relatively small number of Wall Street banks. The Aldrich bill was the product of the clandestine Jekyll Island meeting of Wall Street bankers and not the work of members of the National Monetary Commission. The New York banks were able to exert more influence in molding a bank reform measure that anyone including themselves could have anticipated. Only Senator Aldrich could have carried off such a feat of political legerdemain.

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