Shared Roots:
The Federal Reserve System and the Farm Credit System

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> **The agricultural credit system, created by the Federal Farm Loan Act, was modeled upon the federal reserve system in its general outline as well as in many details.**
>
> W. Stull Holt, 1924, p. 8.

Introduction

On December 23, 1913, President Woodrow Wilson signed the Federal Reserve Act (FRA) into law creating the Federal Reserve System. Just thirty-one months later, on July 17, 1916, he signed the Farm Loan Act (FLA) into law, the first step in creating the Farm Credit System. The Federal Reserve celebrated its Centennial in 2013-14 and the Farm Credit System will do so in 2015-16.

The close timing of the passage of the Federal Reserve Act and the Farm Loan Act was no random coincidence. Passage of the Federal Reserve Act was also the opening act of the legislative history of the Farm Loan Act. By reluctantly throwing their support behind the Federal Reserve Act, agrarian advocates gained political IOUs that later helped to ensure passage of the Farm Loan Act. The Federal Reserve Act became the template for the Farm Loan Act, launching a Farm Credit System committed to serving the financial needs of agriculture and rural America.

The Federal Reserve System and the Farm Credit System share much common history from the early 1900s:

- The enabling Acts for both Systems were instigated by economic events from the preceding decade. Indeed, frustrations well back into the 1800s created momentum for both Acts.
- Both Acts were passed in the first Wilson Administration (1913-17).
- The FRA was passed in the 63rd Congress and the FLA in the 64th Congress, both controlled by the Democratic Party.

1. This work is an independent research work and any opinions expressed are solely those of the author.

- Both initiatives were highly controversial. Many of the same key Congressional players were involved in the complex compromise that mustered majorities for passage in both chambers.
- Agrarian interests in Congress nearly killed the Federal Reserve Act in the summer of 1913. However, they ultimately exerted substantial leverage in its shaping, while gaining certain provisions for agricultural credit.
- These agrarian interests also extracted a political IOU from President Wilson for his support of a "rural credits act." That commitment would languish on the backburner of the Wilson Administration's agenda until early 1916.
- The architects of the Farm Loan Act of 1916 borrowed heavily from the conceptual framework of the Federal Reserve Act of 1913. (Holt, 1924, p. 8)
- Even today, both Systems still retain the cornerstone of the 1913 compromise that enabled passage of the FRA. The bank institutions comprising both Systems are privately owned, but politically regulated and overseen by the Federal government.
- Today both Systems still retain their original public policy purposes. However, the Federal Reserve's mission has vastly expanded beyond that envisioned in 1913. Subsequent Congressional amendments and creative interpretation by assertive Federal Reserve Boards have greatly expanded the Fed's role through the years.

The Federal Reserve System Today

The Federal Reserve System ("the Fed") impacts each of us every day by:

- Setting US monetary policy – managing the money supply
- Issuing paper currency - the familiar US dollar bills in our wallets are Federal Reserve Notes.
- Setting short term interest rates via the discount rate and the Federal Funds rate through open market operations.
- Serving as backstop provider of liquidity to Fed member banks in the event of a liquidity crunch.
- Serving as depository bank to the US government and largest purchaser of US government bonds in the post-2008 era
- Operating our nation's payments system, including the clearing of check, draft, wire and other transactions;
- Regulating much of the US banking system's assets, including all of the largest banks and bank holding companies.
- Substantially impacting financial markets, including the stock and bond markets. Because America is a leading economic power, Fed policy greatly influences global financial markets

Since opening for business in late 1914, the Fed has been the dominant player in US central banking and monetary policy. Over time, its role and its powers have greatly expanded. For example, the 1929 stock market crash and subsequent Great Depression led to expanded powers via the Banking Act of 1935.

During the 2007-09 financial panic, the Fed's role again greatly expanded in response to the severity of rapidly unfolding events. This expanded role as well as its prolonged expansionary policy since late 2008 has once again put the Federal Reserve in the political spotlight. At least one recent Presidential primary candidate called for doing away with the entire System. Also, there are serious Congressional proponents of limiting the rather extensive powers of today's Fed.

The story of how the Federal Reserve came to be is complicated and colorful.

Controversial From the Start

Today, most developed economies have a central bank that leads monetary and banking policy. The Riksbanken, Sweden's central bank, is the oldest dating back to 1668. The Bank of England is the second oldest, dating from 1694, and would have been familiar to our American founding fathers at the birth of our Republic.

Central banking has been controversial since the birth of the American Republic. In 1791 the first Congress legislated, and President George Washington signed, the law establishing the First Bank of the United States, but not without significant controversy. When this Bank's twenty-year charter expired in 1811, a Congress dominated by a different party, the Democratic-Republicans, allowed it to die.

After major fiscal challenges during the War of 1812, however, the Democratic-Republicans had a change of heart. In 1816, Congress established the Second Bank of the United States. Starting in 1833, President Andrew Jackson became determined to destroy the Second Bank. In 1836 its twenty-year charter expired in 1836 without further Congressional action. For nearly eighty years thereafter, the United States had no central bank.

Recurring Financial Panics Create Impetus

In the decades following the Civil War, the United States enjoyed exponential growth in manufacturing, transportation, banking and agriculture. However, this epoch was periodically plagued by financial panics and deep recessions, notably in 1873, 1893 and 1907. These financial panics damaged all segments of the rapidly developing American economy, including agriculture. As these panics developed, banks would increase their liquidity in gold reserves to cover anticipated increases in depositor withdrawals. Banks would also stop making new loans and not renew existing loans as they came due. Loans that had been made “on demand” would be called.

Country banks typically discounted loans with nearby city banks, and these banks in turn often borrowed from the New York City banks. So, as the banks in New York began to call in their loans from the regional city banks, and these city banks in turn called their loans with the country banks, the rural areas were the first to be impacted during a banking panic. In the deepening liquidity crunch, the weakest banks would fail and close their doors – generally those with the least liquidity that were otherwise vulnerable. As these events accelerated, it created additional depositor “runs” on the surviving banks resulting in even more bank failures, further deepening the crisis and invariably leading to an economic recession.

New York City had cemented its role as America’s financial capital in the post-Civil War era. The final decades of the 1800s into the early 1900s were the heyday of John D. Rockefeller, Andrew Carnegie and other capitalists who vigorously pursued business consolidation, often through the formation of trusts concentrating ownership control in railroads, steel, oil and meat packing.

JP (John Pierpont) Morgan was the most famous banker of this era. Not only was he banker to major industrialists as they pursued their trust-building ventures, he was also the de facto leader among New York bankers (The Morgan name remains quite familiar today through JPMorgan Chase Bank and Morgan Stanley.) When summoned to the White House in 1902, Morgan famously told President Teddy Roosevelt, "If we have done anything wrong, send your man to my man and they can fix it up."

At the crucial moment during both the Panic of 1893 and again in the Panic of 1907, it was JP Morgan who organized the major Wall Street financial players to intervene, thereby preventing a bad situation from getting worse – while the President of the United States and the Secretary of the Treasury feebly looked on from Washington. In the absence of a chartered central bank, JP Morgan led the Wall Street banking community as de facto central banker – ultimately with success in both 1893 and 1907.

Agrarian Opposition to Central Banking

Throughout the 1800s, farmers/rural America strongly opposed central banking. This was particularly so in the Midwest and the South where bankers were disliked, especially the city bankers and foremost the “Wall Street” bankers. The Populist Movement of the 1890s gave political voice to this anger. The Populists advocated governmental regulation of railroads, banks, food processors and the various industrial trusts to protect the interests of farmers and other common people. Starting in 1890, the Populists also advanced their version of a farm lending system known as the sub-treasury plan which would have loaned federal money against farmers' commodities stored in designated warehouses.

In the 1890s, William Jennings Bryan of Nebraska emerged as the voice of the Midwestern and Southern agrarian interests, running as both the Populist and the Democratic candidate for US President in 1896. He lost that election, and the Populist Party quickly withered into oblivion. Most of its adherents ultimately re-affiliated with the Democratic Party's Progressive wing. Bryan, nicknamed the Great Commoner, was again the unsuccessful Democratic candidate for President in 1900 and 1908.

In 1912, Bryan came to the Democratic National Convention with substantial influence as the leader of its Progressive wing. After the 9th ballot, he threw his support to the trailing Governor Woodrow Wilson of New Jersey who eventually became nominee on the 46th ballot. After winning the three-way Presidential race in 1912, Wilson rewarded Bryan with the cabinet post of Secretary of State in 1913.

After the Panic of 1907, support for central banking gained traction among the Eastern Establishment and the money center banking interests. However, the nation's farm/rural communities continued to oppose, suspecting that it would become just another tool by which "Wall Street" would exploit rural America.

Interest in rural credit reform dated back into the late 1800s. However, the Panic of 1907 gave rise to a more focused Rural Credits Movement in the years leading up to 1916. The Rural Credits folks advocated a dedicated, federally chartered financial system to serve America's farmers, but were also very interested in having a strong voice in any central banking proposal.

Seeking a Better Way

The initial support for central banking had emerged from the Northeast and within the Republican Party. For the next six years there was sharp national debate about central banking. JP Morgan and the New York City banking community wanted the Federal government to charter a single central bank, owned and dominated by banking interests.   Progressives, trust busters, farm/rural interests and much of the Democratic Party came to accept that banking reform might be necessary. These same interests adamantly opposed any central banking proposal that might be controlled by Morgan and the New York City "Money Trust." In general, these groups wanted government control of a decentralized central banking system in which "Wall Street" influence would be minimized. Much of the agrarian community opposed <u>any</u> central banking legislation, at least until after passage of rural credit legislation.

In the aftermath of the Panic of 1907, Congress passed the Aldrich-Vreeland Currency Act, and President Theodore Roosevelt signed it into law. Among its provisions, the Act established a National Monetary Commission to study:

- The need for central banking in the US and the dynamics of the currency and banking system
- Central banking institutions in other countries and how those models might fit the American economy
- Recommendations for a central banking system and banking reform to be considered by Congress.

Between 1909 and 1912, the National Monetary Commission, aka the Aldrich Commission, conducted an extensive study and issued some 30 voluminous research reports. (Its chairman and driving force was Republican Senator Nelson Aldrich of Rhode Island, a powerful leader of the Republican Senate majority.) The Aldrich Commission undertook an extensive "road trip" to study European central banks in 1909. In its reports, the Commission also called attention to rural credit systems in Germany, France and elsewhere. This information further fueled the Rural Credits Movement's growing interest in a dedicated credit system for American agriculture.

The Aldrich Plan resulted from the Commission's investigation and proposed establishment of a National Monetary Association to be controlled by the banking industry. Introduced during 1912, the plan was defeated in the Senate and not even considered in the Democrat-controlled House. Democrats and Progressives reacted vehemently to chartering a system that would greatly expand the power of the "Money Trust" over the US financial system. Opposition was again especially strong among farm/rural interests.

The 1912 Democratic Platform strongly opposed the Aldrich Plan but called for some sort of "currency reform" to mitigate future financial panics. That year, New Jersey Governor Woodrow Wilson was elected President, with the Democrats also gaining control of the Senate. The stage was set.

1913: The Federal Reserve System Born

Wilson's short Inaugural Address on March 4, 1913 cited **"things that ought to be altered…"** Second on the list was: **"a banking and currency system based upon the necessity of the Government to sell its bonds fifty years ago and perfectly adapted to concentrating cash and restricting credits…"** (Wilson, 1913) "Fifty years" refers to the 1863 passage of the National Banking Act during the height of the Civil War.

It is ironic that President Wilson oversaw the birth of both the Federal Reserve System and the Farm Credit System. Prior to election as Governor of New Jersey in 1910, he had been a college professor of constitutional law and government, and then president of Princeton University. He had no roots in finance, economics or agriculture, nor had he demonstrated much interest in those disciplines prior to being elected President. Interestingly, in 1896 when Bryan ran for President the first time in sharp opposition to the Gold Standard, Wilson had supported an alternative "Gold Democrat" candidate.

Now Secretary of State Bryan would play a major role in the inner negotiations within the Administration and the Democratic Congressional majority. Reflecting his Midwest roots and national advocacy for agrarian interests, Bryan advocated that the Federal Reserve must be under political control and not under that of the bankers; that it had to be decentralized as much as possible; and that the role of the New York City banks ("Wall Street") must be minimized.

It took much of 1913 to achieve a compromise within the Democratic Party that would gain Congressional majorities. Congressman Carter Glass of Virginia was the key figure in brokering within the Democratic Congressional majority. The final act is also known as the Glass-Owens Act, after Glass and Senator Robert Owens, the Senate sponsor. (Glass's name would show up frequently in financial legislation over the next three decades.) Treasury Secretary William McAdoo was also a key figure in achieving consensus.

Bryan played a major behind-the-scenes role. Initially, he avidly supported a decentralized reserve system with twenty regional banks under political control. He got much of what he wanted – political control for the Federal Reserve Board and a decentralized structure, even though the individual banks would be owned by their commercial bank members. Once that point was agreed upon, he became a highly influential supporter of the compromise, especially among the agrarian interests who continued to balk.

Agrarian Revolt Nearly Derails the Glass-Owens Act

Shortly after the proposed legislation was introduced in the summer of 1913, a group of Democratic congressmen from the rural South and Midwest attempted to kill it in committee. Texas Democratic Representative Robert L. Henry was the leader of this agrarian revolt.

> **…this group demanded that the Wilson Administration destroy the "Money Trust" before setting out to reform banking and currency. Moreover, these Democratic agrarians disliked the Federal Reserve bill's provisions for private control of the regional reserve banks, believing that this would be a private financial trust operating under government protection.**

Most important, however, the dissidents protested that the Federal Reserve bill made no provision for agricultural credit, giving the farmers little hope of eliminating the state of debt that had ensnared them since the aftermath of the Civil War. "'The bill as now written, Representative Henry said in July, "is wholly in the interest of the creditor classes, the banking fraternity and the commercial world, without proper provision for the debtor classes and those who toil, produce and sustain the country."

Johnson, 2010, p. 26

After the agrarians scored some initial success in derailing the legislation in the Banking Committee, Wilson intervened:

He invited the agrarian leaders to the White House and mollified them, in part at least, by agreeing to work for the prohibition of interlocking directorates among the banks in the forthcoming antitrust bill. With a combination of pleas, promises, and perhaps even threats Wilson was able to beat back much of the opposition from the agrarian bloc, and in early August the House Banking and Currency Committee reversed the direction it had taken a few weeks earlier and overwhelmingly approved the Federal Reserve bill.

Johnson, 2010, p. 26-27

Representative Henry continued to oppose the bill. However, Secretary Bryan decisively intervened, urging his agrarian constituency to support the bill, thereby defusing the revolt and enabling the Federal Reserve Act to move forward.

Wilson's White House meeting with the agrarian stalwarts that August day is a critical event in the eventual passage of the Farm Loan Act. In return for the agrarians' support of the Federal Reserve Act, Wilson committed support for rural credits legislation. In a lengthy statement to "the farmers of the country" that fall, Wilson pledged:

There is no subject more important to the welfare and industrial development of the United States; there is no reform in which I would myself feel a greater honor or privilege to take party because I should feel that it was a service to the whole country of the first magnitude and significance. It should have accompanied and gone hand in hand with reform of our banking and currency system, if we had been ready to act wisely and with full knowledge of what we were about.

Our farmers must have similar means afforded them of handling their financial needs easily and inexpensively. They should be furnished, these facilities, before

their enterprises languish, not afterwards. And they will be. This is our next task and duty.

The Congress and the executive working together will certainly afford the necessary machinery or relief and prosperity to the people of the countryside and that very soon.

Wilson, 1913, p. 4

Despite the flowery language and the implied urgency of moving "very soon" to enact rural credits legislation, the President's commitment languished until January 1916. Sensing a close Presidential race that year which might well be decided by the farm vote in the Midwest and West, President Wilson sent word to his Democratic allies in Congress that he was now eager to fulfill his pledge.

Compromise

In the fall the House of Representatives passed its version of the Federal Reserve Act, followed by the Senate in December. The Senate version included several more farmer-friendly details that ultimately prevailed in Conference Committee. The Conference process was swift. The reconciled bill was passed by both the House and Senate within two days and signed by President Wilson on December 23. It would take another eight months to organize and charter the Federal Reserve System, but America once again had a central banking system.

The Federal Reserve Act's stated public purpose is straightforward:

An Act to provide for the establishment of Federal reserve banks, to furnish an elastic currency, to afford means of rediscounting commercial paper, to establish a more effective supervision of banking in the United States, and for other purposes.

US Congress, 1913

President Wilson, Congressman Glass and others had crafted a delicate compromise during the long months of political maneuver:

The final structure included Wilson's compromise—a politically appointed Federal Reserve Board in Washington and regional banks in principal centers, run by bankers, with no clear division of authority between the two. As part of the compromise, Wilson proposed a Federal Advisory Council consisting of bankers, appointed by the reserve banks, to serve as advisors to the Board. As with the First Bank and the Second Bank of the United States, Congress did not want to grant a

> **permanent charter, so the initial charter was for 20 years. Permanence was not granted until the McFadden Act of 1927.**
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> Meltzer, 2003, p. 67

Public oversight combined with private ownership of the Federal Reserve System was the critical compromise:

> **Congress chartered the Federal Reserve Banks for a public purpose. The Reserve Banks are the operating arms of the central banking system, and they combine both public and private elements in their makeup and organization. As part of the Federal Reserve System, the Banks are subject to oversight by Congress.**
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> Board of Governors, 2005, p. 19

This public/private approach would again be employed with the Farm Loan Act in 1916.

While President Wilson and the Congressional Democrats had condemned the original Aldrich Plan during the 1912 election, the final legislation retained many of its features. As the Federal Reserve System developed, the New York City Federal Reserve Bank assumed a role of being the preeminent District Bank with strong ties to Wall Street. Given the controversial history of central banking and all of the competing political forces, the Federal Reserve Act had clearly struck a grand compromise. Compromise would again be critical to passage of the Farm Loan Act thirty-one months later.

A Start on Rural Credits Reform

The Federal Reserve Act included several provisions specifically targeted to agrarian and rural interests:

- For the first time, national banks were authorized to make mortgage loans, including farm real estate, for up to five years maturity at no greater than 50% loan to appraised value and within certain bank capital limits.
- The Federal Reserve Banks were authorized to discount agricultural paper (loans) of up to six months maturity in the same manner as commercial paper was eligible for discount. The Federal Reserve Board was encouraged to be expansive in how this was implemented, and it later implemented discounting procedures in this spirit.

While President Wilson and others may likely have viewed these provisions as “enough,” those in the rural credits movement did not see these FRA provisions as anything more than first steps.

Organizing the New System

Most of 1914 was spent getting organized. The twelve District Federal Reserve Banks opened for business on November 16, 1914. The Act had appointed a Reserve Bank Organization Committee (RBOC) consisting of Secretary of the Treasury William G. McAdoo, Secretary of Agriculture David F. Houston and Comptroller of the Currency John S. Williams. Their first tasks were to designate between eight and twelve cities as Federal Reserve Bank cities and then to apportion a like number of territories around each of the new district banks.

The RBOC quickly decided to designate twelve reserve banks and then conducted an exhaustive process to determine the cities and respective districts. They spent six weeks traveling 10,000 miles, holding public hearings in eighteen cities that generated more than 5,000 pages of testimony. About forty cities actively competed for the prestige of being home to a Federal Reserve Bank, although some, such as Lincoln, Nebraska, and Springfield, Massachusetts, were never serious contenders. The Committee also surveyed national banks regarding their locational preference as to their district Reserve Bank.

In April 1914, the committee recommended twelve cities and districts that remain nearly the same today. (Federal Reserve Board, 2005) These are a 1914 snapshot of regional banking centers, economic activity and population. A case in point, the San Francisco Federal Reserve District covered seven states (now nine) while the Cleveland District included only Ohio, western Pennsylvania, the northern panhandle of West Virginia, and eastern Kentucky. States were often split between Federal Reserve Districts. Politics played a role, with Richmond of Congressman Carter Glass's home state of Virginia, winning over Baltimore. Missouri gained two Federal Reserve Banks (St. Louis and Kansas City), likely due to pivotal Congressional support for the FRA from that state.

Baltimore and New Orleans had expected to be designated as Reserve Bank cities, and each made a strong case relative to Richmond and Atlanta respectively. While their protests were to no avail, it is interesting to note that three years later, they were among the twelve cities designated for Federal Land Banks.

Federal Reserve Banks – Owned by Member Banks

All national banks are required to become members of the Federal Reserve System. State banks are allowed to become Fed members under the same conditions as national banks, and in so doing, come under the joint regulation of their state and the Federal Reserve. As of June 30, 2013, Federal Reserve System membership included 2,012 banks as follows:

- 1,193 national banks accounting for 66% of total US commercial banking system assets

- 819 state-chartered banks accounting for another 15% of total commercial bank assets

Combined, the Fed's 2,012 member banks accounted for 81.3% of US commercial banking assets. (Board of Governors (2014) p. 290)

Member banks purchase stock in their District Federal Reserve Bank in the amount of 6% of their capital and surplus, half paid in and half subject to call by the Board of Governors. This stock is much like stock in a cooperative such as a Farm Credit institution. Stock purchase is legally required to become a member of the Federal Reserve and may not be bought, sold or pledged as collateral. It enables the member bank to vote for Class A and Class B directors of the Federal Reserve Bank. Unlike stock in Farm Credit institutions, Fed member banks receive a 6% annual dividend on their stock.

Federal Reserve member banks must comply with System reserve requirements, which may be changed from time to time. Today, this basically means that some specified percentage of their checking account balances must be held as cash in their district Federal Reserve Bank.

Each Federal Reserve Bank is governed by a board of nine directors, none of who can be from bank management. These boards provide diverse representation of the banking, commercial, industrial, consumer, agricultural and public interests within that district:

- Three Class A directors represent the bank members of that District and are elected by the member banks.
- Three Class B directors represent the public interest and are elected by the member banks from candidates approved by the Federal Reserve Board of Governors.
- Three Class C directors represent the public interest and are appointed by the Federal Reserve Board of Governors. One of these is elected Chairman of the Board. Class C directors (through their employer) may not own any stock in federal reserve banks and are thus outside directors in practice.

Note the mixed nature of this board structure, with the privately owned member banks having a strong say in determining three of the director seats, and shared control (election) over the three Class B directors. The politically appointed Board of Governors has an absolute say over the three public directors and shared control (nomination) over the three Class B directors.

The Board of Governors – Political Control from the Top

The Board of Governors (the Board or "the Fed") is usually in the headline news while the day-to-day workings of the twelve Federal Reserve Banks are far less visible. The Board is the political entity born of the 1913 compromise that oversees and regulates the Federal Reserve System. Its Chair is the spokesperson for Fed policy. There are seven members of the Board of

Governors, each serving a fourteen-year term. They are nominated by the President and confirmed by the Senate. Likewise, the Chairman and Vice Chairman are nominated by the President from among the seven Board members and confirmed by the Senate for six-year terms.

The Board of Governors assures the public policy purpose and regulates the twelve Federal Reserve Banks and their member banks for safety and soundness, just as the Farm Credit Administration Board of Directors carries out the intent and provisions of the Farm Credit Act of 1971 as amended.

The Federal Reserve Open Market Committee (FOMC) is the final component of the Fed architecture. This twelve-member committee meets every other month to discuss economic and financial outlook and to then determine the Federal Funds target rate, as well as the discount rate by which member banks can borrow from their District Bank. The FMOC consists of the seven members of the Board of Governors, the President of the New York Fed, and four other Federal Reserve Bank Presidents who rotate through one-year terms.

Overlapping Timelines

Both the Federal Reserve and the Farm Credit System were born out of events of the late-1800s. After the Panic of 1907, their timelines are closely connected.

	Federal Reserve	**Farm Credit**
1908	• Aldrich-Vreeland Act • National Monetary Commission (aka Aldrich Commission) formed	• Country Life Commission (CLC) appointed • CLC completes its work. Report forwarded to President T. Roosevelt late year
1909-1911	• Aldrich Commission studies central banking and publishes extensive reports	• Rural credits movement in its infancy
1910	• Secret "insider" meeting at Jekyll Island, GA develops National Reserve Association Plan, aka the Aldrich Bill	

	Federal Reserve	Farm Credit
1912	• Aldrich Bill introduced in US Senate…and defeated • Congressional hearings on the New York Money Trust – the Pujo Hearings • Democratic Party opposes Aldrich Bill in its national platform • Governor Woodrow Wilson of New Jersey elected President, beating incumbent President Taft (R) and former President T. Roosevelt (Bull Moose)	• David Lubin addresses Southern Commercial Congress (SCC) on European rural credit systems. SCC creates American Commission to study & report on European models • President Taft directs Ambassador to France David Herrick to study and report on European rural credit systems • All three major parties include platform planks supporting study of rural credit systems • Pres. Taft convenes White House conference on rural credit reform with state governors in December
1913	• President Wilson calls for central banking under political control in his Inaugural Address • Congressman Carter Glass and Wilson broker compromise • "Agrarian Revolt" to central banking thwarted during summer • Owen-Glass Federal Reserve Act passed by Congress and signed into law by Wilson on Dec. 23	• US Commission established to study European rural credit systems in cooperation with the American Commission (both chaired by Senator Duncan Fletcher D-FL) • Commissions conduct their extensive European tour and issue reports • President Wilson issues his "Our farmers must have similar means afforded them" statement • Fletcher introduces first Rural Credits bill in Congress
1914	• Federal Reserve System organized and chartered. Operations begin in November • Outbreak of the Great War (WWI) in Europe although US did not enter until 1917 • Financial crisis. New York stock market suspended for six months. Emergency provisions of Aldrich-Vreeland Act invoked	• Various reports issued and Congressional hearings held, but no substantial progress on rural credits legislation

	Federal Reserve	Farm Credit
1915		• Rural Credits legislation remains deadlocked in Congress between competing approaches • Congressional joint study committee appointed to resolve Rural Credits issues
1916		• In January, Wilson urges Congressional allies to complete Rural Credits legislation • Legislation advances for two parallel systems – cooperative (Federal Land Banks/National Farm Loan Associations) and investor-owned (joint stock land banks) • Wilson signs Farm Loan Act July 17 • Farm Loan Board announces twelve FLB cities and districts Dec. 27
1917	• US enters the Great War, aka World War I	• Federal Land Banks (FLB) chartered and begin operations • First FLB loan made to farmer in Larned, Kansas

Shared Genetics: Federal Reserve and Farm Credit Systems

1. In creating both Systems, Congress recognized compelling public policy purposes that the private sector was incapable of addressing. Indeed, the Federal Reserve Act of 1913 set in motion a burst of new federally sponsored financial institutions over the next twenty-five years including the Farm Loan Act (1916); the Agricultural Credits Act (1923); the Federal Home Loan Act (1932); the McFadden Act (1927); the Banking Act of 1933, aka Glass-Steagall (FDIC); the Farm Credit Act (1933); the Securities Act (1933); the Securities Exchange Act (1934); the Federal Credit Union Act (1934); and the National Housing Act of 1938 which chartered the Federal National Mortgage Association (Fannie Mae).

2. The Panic of 1907 was catalyst for the Federal Reserve System, which in turn created conditions for passage of the Farm Loan Act two years later.

3. Both Systems are public-private hybrids. With the Federal Reserve, Congress legislated a system of twelve District Banks to be owned by the national banks (and state banks opting

in), all overseen by a politically appointed Federal Reserve Board. With the Farm Credit System, Congress provided the start-up capitalization for twelve District Federal Land Banks that were intended to someday become owned by National Farm Loan Associations (NFLAs). The NFLAs were to be organized once the Federal Land Banks were operational and would be owned by their farmer-borrowers.

4. The final shape of both Systems was the result of hard-fought compromise. National versus regional, private versus public, and Wall Street versus Main Street were issues balanced within the Federal Reserve Act. Investor-owned joint stock land banks, cooperative-owned National Farm Loan Associations and direct government lending were all contending approaches in the debate leading to the Farm Loan Act. Its final version chartered two parallel financial systems, the joint stock land banks which were to be investor-owned and the Federal Land Bank/NFLAs which were to become borrower-owned over time (The joint stock land bank system flourished for only a few years and then got into trouble in during the agricultural depression of the 1920s. The Emergency Farm Mortgage Act of 1933 put the remaining joint stock land banks into receivership under FCA, which ultimately disbanded this system.).

5. Both authorizing bills were passed during the first Wilson Administration. The Glass-Owen Federal Reserve Act was passed by the 63rd Congress while the Hollis-Bulkley Farm Loan Act was passed in the 64th.

6. Key leaders were involved in the passage of both Acts. In addition to President Wilson, several Federal Reserve Act players reprised major roles in the Farm Loan Act:
   - Congressman Carter Glass chaired the Joint Committee on Rural Credits and the House Committee on Banking and Currency, as well as serving on the Conference Committee that reconciled the House and Senate versions of the Farm Loan Act;
   - Senator Robert L. Owen served on the Joint Committee on Rural Credits, chaired the Senate Committee on Banking and Currency, and also served on the Conference Committee;
   - Secretary of the Treasury McAdoo's department housed the fledgling Farm Loan Board, and he played a major role in getting the Federal Land Banks launched;
   - With his strong agrarian background, William Jennings Bryan might have been a key player in forging the Farm Loan Act. That was not to be as he and President Wilson had a falling out in 1915 over US policy toward Germany during the second year of the Great War (World War I). Bryan had resigned his position and was no longer a political force within the Wilson Administration in 1916.

7. Henry Parker Willis was the primary drafter of the language in the Federal Reserve Act, working closely with Chairman Carter Glass. Willis was a Ph.D. economist who had held

academic posts and had also been a newspaper/magazine correspondent prior to serving as "expert" to the House Banking and Currency Committee in its drafting of the Federal Reserve Act in 1912-13. Willis later participated in the technical drafting of the Hollis-Bulkley Bill for rural credits in 1915. This bill became the basis for the Farm Loan Act, especially that part of the bill that chartered the twelve Federal Land Banks and provided for establishment of local National Farm Loan Associations. It is no surprise then, that much of the structural DNA of the Federal Reserve Act found its way over to the Farm Loan Act. (Holt, 1924, p. 8)

8. The Federal Reserve Act exempted the twelve District Banks from "Federal, State, and local taxation, except taxes upon real estate." The Farm Loan Act similarly exempted the Federal Land Banks and National Farm Loan Associations from income taxation on their income while requiring them to pay real estate taxes.

9. The Farm Loan Act in 1916 was not the last time in which Congress repurposed the institutional DNA of the Federal Reserve Act. It established twelve Federal Intermediate Credit Banks in 1923. In 1932, twelve District Banks were established under the Federal Home Loan Banking System to address housing finance challenges. In the Farm Credit Act of 1933, Congress established thirteen Banks for Cooperatives (twelve district and one central bank), as well as twelve District Production Credit Corporations, all based on the original Federal Land Bank districts from 1916.

100 Years Later

Both the Federal Reserve and Farm Credit Systems grew up from the turbulent debates of 1913-16. As the US economy and financial system expanded and modernized, punctuated by periodic financial/economic events, the Federal Reserve System acquired greatly expanded powers and responsibilities, sometimes legislated by Congress but also asserted by forceful Federal Reserve Chairmen at critical times. The Farm Credit System also grew and modernized in response to the changing needs of the farm sector, with major Congressional updates in 1923, 1933, 1971 and 1987, as well as Congressional amendments in other years.

Unquestionably, the Federal Reserve System's mission and role has expanded to a far greater extent than that of the Farm Credit System. For example, as of December 31, 2013, the twelve member-owned Federal Reserve Banks held $2.36 trillion in US Treasury securities and another $1.53 trillion of mortgage-backed securities on their consolidated balance sheets as a consequence of the Federal Reserve Board's massive quantitative easing in the aftermath of the Great Recession. (Board of Governors, 2014, p. 334) This would have been unthinkable in 1913 in an era when the extent of Federal power was far less reaching.

Still, if one looks at the basic building blocks of both Systems, it is clear that they continue to share a great deal of common institutional DNA. Ironically, commercial bank trade group critics often cite Farm Credit System structure as "unfair" when these very same attributes were modeled from the Federal Reserve System, often to the substantially greater advantage of its commercial bank owners.

Capacity of the Systems Compared

Perhaps the best way to compare the two Systems' respective capacities today is through the Federal government's definition of a government-sponsored enterprise (GSE), established in the Omnibus Reconciliation Act of 1990. Each of the following subsections paraphrases the points of the GSE typology and assesses the two Systems accordingly. (Kosar, 2007)

Has a Federal charter authorized by law. Both Systems clearly have Federal charters dating from the respective Acts in 1913 and 1916, subsequently updated by Congress at key junctures.

Privately owned, as evidenced by capital stock owned by private entities or individuals. The twelve Federal Reserve Banks are owned by about 2,000 private sector commercial banks. These owners had a consolidated $55 billion of capital invested in the twelve District Banks as of 12/31/2013. (Board of Governors, 2014, p. 334) The four Farm Credit Banks (including CoBank, ACB) are similarly owned by seventy-six Farm Credit associations as well as the cooperative and rural utility owners of CoBank. In turn, the seventy-six FCS associations are owned by nearly 500,000 farmer-borrowers.

Under the direction of a board of directors, a majority of which is elected by private owners. Each of the twelve Federal Reserve Banks is governed by a nine-member board, of which six directors are elected by the member banks with the other three appointed by the Federal Reserve Board. Farm Credit institutions are also governed by Boards with most directors elected by their members, with a requirement for outside directors elected by the respective board. (Farm Credit boards did have federally appointed directors earlier in their history.)

Financial institution with power to (I) make loans or loan guarantees for limited purposes such as to provide credit for specific borrowers or one sector. Federal Reserve Banks are critical to ensuring liquidity and monetary reserves to their individual member banks in the normal course of business and of injecting liquidity into the financial system during times of great financial turmoil, as they did in 2008-09. They are not permitted to directly lend to nonmembers such as corporations, other nonmember financial institutions (such as the Farm Credit System or credit unions), or individuals. Farm Credit System institutions are similarly limited to lending to agriculture, cooperatives, rural utilities, commercial fishermen, farm-related businesses and rural residents (for residential purposes). Going beyond the forgoing specifics, there are critical differences. The Federal Reserve System does not lend directly other than to its member banks, while Farm Credit institutions lend directly to their eligible owner-borrowers. However, the member banks of the Federal Reserve System have broad authority to lend across all sectors, industrial, commercial, agricultural, consumer and governmental. Farm Credit institutions have very limited lending authority as previously cited.

Financial institution with power to (II) raise funds by borrowing (which does not carry the full faith and credit of the Federal Government) or to guarantee the debt of others in unlimited amounts. Congress granted the Federal Reserve the ultimate power to raise funds. It controls America's money supply with the ability to issue Federal Reserve Notes and engage in open market operations buying/selling securities to control liquidity in the financial system. This is all directed by the politically appointed Federal Reserve Board and not by the privately controlled Federal Reserve Banks, although they are an integral part of the overall monetary mechanism. In recent years, the Federal Reserve Board's innovative quantitative easing initiative was predicated on the ability to house purchased US Treasury and mortgage-backed securities on the balance sheets of the banker-owned Federal Reserve Banks. Clearly the Farm Credit System's authority to sell securities backed by loans pales in comparison to the funding capability of the Federal Reserve System.

Does not exercise powers that are reserved to the Government as sovereign (such as the power to tax or to regulate interstate commerce). Clearly the Federal Reserve Board, the political arm, does exercise sovereign powers such as control of the money supply, regulatory authority over its member banks, and control over the interstate and global aspects of the US financial system. The privately owned District Reserve Banks do not exercise sovereign powers, but certainly they and their member banks greatly benefit from being part of a System in which the political arm has been delegated a substantial amount of the Federal sovereign power. The Farm Credit System does not enjoy any sovereign powers. This was affirmed by the US Supreme Court in the 1921 landmark case ***Smith v. Kansas City Title & Trust Co.***

Does not have the power to commit the Government financially. The Federal Reserve Board in its role as monetary arm of the Federal government has this power. The twelve Federal Reserve Banks and the four Farm Credit System Banks do not have the power to commit the Government financially.

Has employees whose salaries and expenses are paid by the enterprise and are not Federal employees subject to title 5. Employees of both the Federal Reserve Banks and Farm Credit System are private sector employees paid by their respective institutions. They are not Federal employees in either case.

Conclusion

Both Systems were originally conceived and have subsequently evolved to serve necessary public purposes under the sponsorship of the Federal government. Clearly both are public-private sector hybrids. Indeed, most US financial institutions operate under special charters and close supervision of Federal and/or state governments. This practice dates to the birth of our nation necessitated by:

1. The pivotal importance of the financial system to the overall economy.
2. The American people's collective financial security relies on the banking system for deposit services, credit, mortgages and custodianship of various investments.

The sometime assertion that Farm Credit System institutions have some sort of special advantage over the commercial bank members of the Federal Reserve System is pure political rhetoric. Given the tremendous institutional capacity chartered within the Federal Reserve System, it is highly dubious to conclude that its commercial bank owners came up short relative to the farmer-owners of the Farm Credit System.

Indeed, the starkest contrast between the two Systems is who ultimately benefits from their respective Federal charters:

- For the Federal Reserve System, economic value flows through the District Banks' income statements and is either paid out in dividends to their commercial bank owners or added to surplus. Ultimately the incremental economic value accrues to commercial bank investor-owners as either dividends or enhanced market capitalization of their stock.
- For the Farm Credit System, economic value flows through the income statements of Associations and/or Banks, and is either paid out in patronage dividends to their farmer-owners, or added to capital for their future benefit. These patronage dividends are taxable income to FCS customer-owners.

For nearly 100 years, Americans have benefited greatly from both the Federal Reserve System and the Farm Credit System. Each effectively performs a critical role within our modern financial and banking system. Both share common institutional DNA dating to their original legislation a century ago. Both remain relevant today and will hopefully grow and change to meet the evolving financial needs of America in the future.

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