

CHAPTER IV

SERVE ONE MASTER ONLY

The Pujo Committee has presented the facts concerning the Money Trust so clearly that the conclusions appear inevitable. Their diagnosis discloses intense financial concentration and the means by which it is effected. Combination,—the intertwining of interests,—is shown to be the all-pervading vice of the present system. With a view to freeing industry, the Committee recommends the enactment of twenty-one specific remedial provisions. Most of these measures are wisely framed to meet some abuse disclosed by the evidence; and if all of these were adopted the Pujo legislation would undoubtedly alleviate present suffering and aid in arresting the disease. But many of the remedies proposed are "local" ones; and a cure is not possible, without treatment which is fundamental. Indeed, a major operation is necessary. This the Committee has hesitated to advise; although the fundamental treatment required is simple: "Serve one Master only."

The evils incident to interlocking directorates are, of course, fully recognized; but the prohibitions proposed in that respect are restricted to a very narrow sphere.

First: The Committee recognizes that potentially competing corporations should not have a common director;—but it restricts this prohibition to directors of national banks, saying:

“No officer or director of a national bank shall be an officer or director of any other bank or of any trust company or other financial or other corporation or institution, whether organized under state or federal law, that is authorized to receive money on deposit or that is engaged in the business of loaning money on collateral or in buying and selling securities except as in this section provided; and no person shall be an officer or director of any national bank who is a private banker or a member of a firm or partnership of bankers that is engaged in the business of receiving deposits: Provided, That such bank, trust company, financial institution, banker, or firm of bankers is located at or engaged in business at or in the same city, town, or village as that in which such national bank is located or engaged in business: Provided further, That a

director of a national bank or a partner of such director may be an officer or director of not more than one trust company organized by the laws of the state in which such national bank is engaged in business and doing business at the same place."

Second: The Committee recognizes that a corporation should not make a contract in which one of the management has a private interest; but it restricts this prohibition (1) to national banks, and (2) to the officers, saying:

"No national bank shall lend or advance money or credit or purchase or discount any promissory note, draft, bill of exchange or other evidence of debt bearing the signature or indorsement of any of its officers or of any partnership of which such officer is a member, directly or indirectly, or of any corporation in which such officer owns or has a beneficial interest of upward of ten per centum of the capital stock, or lend or advance money or credit to, for or on behalf of any such officer or of any such partnership or corporation, or purchase any security from any such officer or of or from any partnership or corporation of which such officer is a member or in which he is financially interested, as herein specified, or of any corporation

of which any of its officers is an officer at the time of such transaction."

Prohibitions of intertwining relations so restricted, however supplemented by other provisions, will not end financial concentration. The Money Trust snake will, at most, be scotched, not killed. The prohibition of a common director in potentially competing corporations should apply to state banks and trust companies, as well as to national banks; and it should apply to railroad and industrial corporations as fully as to banking institutions. The prohibition of corporate contracts in which one of the management has a private interest should apply to directors, as well as to officers, and to state banks and trust companies and to other classes of corporations, as well as to national banks. And, as will be hereafter shown, such broad legislation is within the power of Congress.

Let us examine this further:

THE PROHIBITION OF COMMON DIRECTORS IN POTENTIALLY COMPETING CORPORATIONS

1. *National Banks.* The objection to common directors, as applied to banking institutions, is clearly shown by the Pujo Committee.

“As the first and foremost step in applying a remedy, and also for reasons that seem to us conclusive, independently of that consideration, we recommend that interlocking directorates in potentially competing financial institutions be abolished and prohibited so far as lies in the power of Congress to bring about that result. . . . When we find, as in a number of instances, the same man a director in half a dozen or more banks and trust companies all located in the same section of the same city, doing the same class of business and with a like set of associates similarly situated, all belonging to the same group and representing the same class of interests, all further pretense of competition is useless. . . . If banks serving the same field are to be permitted to have common directors, genuine competition will be rendered impossible. Besides, this practice gives to such common directors the unfair advantage of knowing the affairs of borrowers in various banks, and thus affords endless opportunities for oppression.”

This recommendation is in accordance with the legislation or practice of other countries. The Bank of England, the Bank of France, the National Bank of Belgium, and the leading

banks of Scotland all exclude from their boards persons who are directors in other banks. By law, in Russia no person is allowed to be on the board of management of more than one bank.

The Committee's recommendation is also in harmony with laws enacted by the Commonwealth of Massachusetts more than a generation ago designed to curb financial concentration through the savings banks. Of the great wealth of Massachusetts a large part is represented by deposits in its savings banks. These deposits are distributed among 194 different banks, located in 131 different cities and towns. These 194 banks are separate and distinct; not only in form, but in fact. In order that the banks may not be controlled by a few financiers, the Massachusetts law provides that no executive officer or trustee (director) of any savings bank can hold any office in any other savings bank. That statute was passed in 1876. A few years ago it was supplemented by providing that none of the executive officers of a savings bank could hold a similar office in any national bank. Massachusetts attempted thus to curb the power of the individual financier; and no disadvantages are discernible. When that Act was passed the aggregate deposits in its savings banks were

\$243,340,642; the number of deposit accounts 739,289; the average deposit to each person of the population \$144. On November 1, 1912, the aggregate deposits were \$838,635,097.85; the number of deposit accounts 2,200,917; the average deposit to each account \$381.04. Massachusetts has shown that curbing the power of the few, at least in this respect, is entirely consistent with efficiency and with the prosperity of the whole people.

2. *State Banks and Trust Companies.* The reason for prohibiting common directors in banking institutions applies equally to national banks and to state banks including those trust companies which are essentially banks. In New York City there are 37 trust companies of which only 15 are members of the clearing house; but those 15 had on November 2, 1912, aggregate resources of \$827,875,653. Indeed the Bankers' Trust Company with resources of \$205,000,000, and the Guaranty Trust Company, with resources of \$232,000,000, are among the most useful tools of the Money Trust. No bank in the country has larger deposits than the latter; and only one bank larger deposits than the former. If common directorships were permitted in state banks or such trust companies, the

✓
✓
Suff.

charters of leading national banks would doubtless soon be surrendered; and the institutions would elude federal control by re-incorporating under state laws.

The Pujo Committee has failed to apply the prohibition of common directorships in potentially competing banking institutions rigorously even to national banks. It permits the same man to be a director in one national bank and one trust company doing business in the same place. The proposed concession opens the door to grave dangers. In the first place the provision would permit the interlocking of any national bank not with one trust company only, but with as many trust companies as the bank has directors. For while under the Pujo bill no one can be a national bank director who is director in more than one such trust company, there is nothing to prevent each of the directors of a bank from becoming a director in a different trust company. The National Bank of Commerce of New York has a board of 38 directors. There are 37 trust companies in the City of New York. Thirty-seven of the 38 directors might each become a director of a different New York trust company: and thus 37 trust companies would be interlocked with the National Bank of

Commerce, unless the other recommendation of the Pujo Committee limiting the number of directors to 13 were also adopted.

But even if the bill were amended so as to limit the possible interlocking of a bank to a single trust company, the wisdom of the concession would still be doubtful. It is true, as the Pujo Committee states, that "the business that may be transacted by" a trust company is of "a different character" from that properly transacted by a national bank. But the business actually conducted by a trust company is, at least in the East, quite similar; and the two classes of banking institutions have these vital elements in common: each is a bank of deposit, and each makes loans from its deposits. A private banker may also transact some business of a character different from that properly conducted by a bank; but by the terms of the Committee's bill a private banker engaged in the business of receiving deposits would be prevented from being a director of a national bank; and the reasons underlying that prohibition apply equally to trust companies and to private bankers.

3. *Other Corporations.* The interlocking of banking institutions is only one of the factors

which have developed the Money Trust. The interlocking of other corporations has been an equally important element. And the prohibition of interlocking directorates should be extended to potentially competing corporations whatever the class; to life insurance companies, railroads and industrial companies, as well as banking institutions. The Pujo Committee has shown that Mr. George F. Baker is a common director in the six railroads which haul 80 per cent. of all anthracite marketed and own 88 per cent. of all anthracite deposits. The Morgan associates are the *nexus* between such supposedly competing railroads as the Northern Pacific and the Great Northern; the Southern, the Louisville & Nashville and the Atlantic Coast Line, and between partially competing industrials like the Westinghouse Electric and Manufacturing Company and the General Electric. The *nexus* between all the large potentially competing corporations must be severed, if the Money Trust is to be broken.

**PROHIBITING CORPORATE CONTRACTS IN WHICH THE
MANAGEMENT HAS A PRIVATE INTEREST**

The principle of prohibiting corporate contracts in which the management has a private interest

is applied, in the Pujo Committee's recommendations, only to national banks, and in them only to officers. All other corporations are to be permitted to continue the practice; and even in national banks the directors are to be free to have a conflicting private interest, except that they must not accept compensation for promoting a loan of bank funds nor participate in syndicates, promotions or underwriting of securities in which their banks may be interested as underwriters or owners or lenders thereon: that all loans or other transactions in which a director is interested shall be made in his own name; and shall be authorized only after ample notice to co-directors; and that the facts shall be spread upon the records of the corporation.

The Money Trust would not be disturbed by a prohibition limited to officers. Under a law of that character, financial control would continue to be exercised by the few without substantial impairment; but the power would be exerted through a somewhat different channel. Bank officers are appointees of the directors; and ordinarily their obedient servants. Individuals who, as bank officers, are now important factors in the financial concentration, would doubtless resign as officers and become merely directors.

The loss of official salaries involved could be easily compensated. No member of the firm of J. P. Morgan & Co. is an officer in any one of the thirteen banking institutions with aggregate resources of \$1,283,000,000, through which as directors they carry on their vast operations. A prohibition limited to officers would not affect the Morgan operations with these banking institutions. If there were minority representation on bank boards (which the Pujo Committee wisely advocates), such a provision might afford some protection to stockholders through the vigilance of the minority directors preventing the dominant directors using their power to the injury of the minority stockholders. But even then, the provision would not safeguard the public; and the primary purpose of Money Trust legislation is not to prevent directors from injuring stockholders; but to prevent their injuring the public through the intertwined control of the banks. No prohibition limited to officers will materially change this condition.

The prohibition of interlocking directorates, even if applied only to all banks and trust companies, would practically compel the Morgan representatives to resign from the directorates of the thirteen banking institutions with which they

are connected, or from the directorates of all the railroads, express, steamship, public utility, manufacturing, and other corporations which do business with those banks and trust companies. Whether they resigned from the one or the other class of corporations, the endless chain would be broken into many pieces. And whether they retired or not, the Morgan power would obviously be greatly lessened: for if they did not retire, their field of operations would be greatly narrowed.

APPLY THE PRIVATE INTEREST PROHIBITION TO ALL
KINDS OF CORPORATIONS

The creation of the Money Trust is due quite as much to the encroachment of the investment banker upon railroads, public service, industrial, and life-insurance companies, as to his control of banks and trust companies. Before the Money Trust can be broken, all these relations must be severed. And they cannot be severed unless corporations of each of these several classes are prevented from dealing with their own directors and with corporations in which those directors are interested. For instance: The most potent single source of J. P. Morgan & Co.'s power is the \$162,500,000 deposits, including those of 78 interstate railroad, public-service and industrial

corporations, which the Morgan firm is free to use as it sees fit. The proposed prohibition, even if applied to all banking institutions, would not affect directly this great source of Morgan power. If, however, the prohibition is made to include railroad, public-service, and industrial corporations, as well as banking institutions, members of J. P. Morgan & Co. will quickly retire from substantially all boards of directors.

APPLY THE PRIVATE INTEREST PROHIBITION TO
STOCKHOLDING INTERESTS

The prohibition against one corporation entering into transactions with another corporation in which one of its directors is also interested, should apply even if his interest in the second corporation is merely that of stockholder. A conflict of interests in a director may be just as serious where he is a stockholder only in the second corporation, as if he were also a director.

One of the annoying petty monopolies, concerning which evidence was taken by the Pujo Committee, is the exclusive privilege granted to the American Bank Note Company by the New York Stock Exchange. A recent \$60,000,000 issue of New York City bonds was denied listing

on the Exchange, because the city refused to submit to an exaction of \$55,800 by the American Company for engraving the bonds, when the New York Bank Note Company would do the work equally well for \$44,500. As tending to explain this extraordinary monopoly, it was shown that men prominent in the financial world were stockholders in the American Company. Among the largest stockholders was Mr. Morgan, with 6,000 shares. No member of the Morgan firm was a director of the American Company; but there was sufficient influence exerted somehow to give the American Company the stock exchange monopoly.

The Pujo Committee, while failing to recommend that transactions in which a director has a private interest be prohibited, recognizes that a stockholder's interest of more than a certain size may be as potent an instrument of influence as a direct personal interest; for it recommends that:

“Borrowings, directly or indirectly by . . . any corporation of the stock of which he (a bank director) holds upwards of 10 per cent. from the bank of which he is such director, should only be permitted, on condition that notice shall have

been given to his co-directors and that a full statement of the transaction shall be entered upon the minutes of the meeting at which such loan was authorized."

As shown above, the particular provision for notice affords no protection to the public; but if it did, its application ought to be extended to lesser stock-holdings. Indeed it is difficult to fix a limit so low that financial interest will not influence action. Certainly a stockholding interest of a single director, much smaller than 10 per cent., might be most effective in inducing favors. Mr. Morgan's stockholdings in the American Bank Note Company was only three per cent. The \$6,000,000 investment of J. P. Morgan & Co. in the National City Bank represented only 6 per cent. of the bank's stock; and would undoubtedly have been effective, even if it had not been supplemented by the election of his son to the board of directors.

SPECIAL DISQUALIFICATIONS

The Stanley Committee, after investigation of the Steel Trust, concluded that the evils of interlocking directorates were so serious that representatives of certain industries which are largely

dependent upon railroads should be absolutely prohibited from serving as railroad directors, officers or employees. It, therefore, proposed to disqualify as railroad director, officer or employee any person engaged in the business of manufacturing or selling railroad cars or locomotives, railroad rail or structural steel, or in mining and selling coal. The drastic Stanley bill, shows how great is the desire to do away with present abuses and to lessen the power of the Money Trust.

Directors, officers, and employees of banking institutions should, by a similar provision, be disqualified from acting as directors, officers or employees of life-insurance companies. The Armstrong investigation showed that life-insurance companies were in 1905 the most potent factor in financial concentration. Their power was exercised largely through the banks and trust companies which they controlled by stock ownership and their huge deposits. The Armstrong legislation directed life-insurance companies to sell their stocks. The Mutual Life and the Equitable did so in part. But the Morgan associates bought the stocks. And now, instead of the life-insurance companies controlling the banks and trust companies, the latter and the bankers control the life-insurance companies.

HOW THE PROHIBITION MAY BE LIMITED

The Money Trust cannot be destroyed unless all ~~classes~~ of corporations are included in the prohibition of interlocking directors and of transactions by corporations in which the management has a private interest. But it does not follow that the prohibition must apply to every corporation of each class. Certain exceptions are entirely consistent with merely protecting the public against the Money Trust; although protection of minority stockholders and business ethics demand that the rule prohibiting a corporation from making contracts in which a director has a private financial interest should be universal in its application. The number of corporations in the United States Dec. 31, 1912, was 305,336. Of these only 1610 have a capital of more than \$5,000,000. Few corporations (other than banks) with a capital of less than \$5,000,000 could appreciably affect general credit conditions either through their own operations or their affiliations. Corporations (other than banks) with capital resources of less than \$5,000,000 might, therefore, be excluded from the scope of the statute for the present. The prohibition could also be limited so as not to apply to any

industrial concern, regardless of the amount of capital and resources, doing only an intrastate business; as practically all large industrial corporations are engaged in interstate commerce. This would exclude some retail concerns and local jobbers and manufacturers not otherwise excluded from the operation of the act. Likewise banks and trust companies located in cities of less than 100,000 inhabitants might, if thought advisable, be excluded, for the present if their capital is less than \$500,000, and their resources less than, say, \$2,500,000. In larger cities even the smaller banking institutions should be subject to the law. Such exceptions should overcome any objection which might be raised that in some smaller cities, the prohibition of interlocking directorates would exclude from the bank directorates all the able business men of the community through fear of losing the opportunity of bank accommodations.

{An exception should also be made, so as to permit interlocking directorates between a corporation and its proper subsidiaries. And the prohibition of transactions in which the management has a private interest should, of course, not apply to contracts, express or implied, for such services as are performed indiscriminately for

the whole community by railroads and public service corporations, or for services, common to all customers, like the ordinary service of a bank for its depositors.

THE POWER OF CONGRESS

The question may be asked: Has Congress the power to impose these limitations upon the conduct of any business other than national banks? And if the power of Congress is so limited, will not the dominant financiers, upon the enactment of such a law, convert their national banks into state banks or trust companies, and thus escape from congressional control?

The answer to both questions is clear. Congress has ample power to impose such prohibitions upon practically all corporations, including state banks, trust companies and life insurance companies; and evasion may be made impossible. While Congress has not been granted power to regulate *directly* state banks, and trust or life insurance companies, or railroad, public-service and industrial corporations, except in respect to interstate commerce, it may do so *indirectly* by virtue either of its control of the mail privilege or through the taxing power.

Practically no business in the United States can

be conducted without use of the mails; and Congress may in its reasonable discretion deny the use of the mail to any business which is conducted under conditions deemed by Congress to be injurious to the public welfare. Thus, Congress has no power directly to suppress lotteries; but it has indirectly suppressed them by denying, under heavy penalty, the use of the mail to lottery enterprises. Congress has no power to suppress directly business frauds; but it is constantly doing so indirectly by issuing fraud-orders denying the mail privilege. Congress has no direct power to require a newspaper to publish a list of its proprietors and the amount of its circulation, or to require it to mark paid-matter distinctly as advertising: But it has thus regulated the press, by denying the second-class mail privilege, to all publications which fail to comply with the requirements prescribed.

The taxing power has been resorted to by Congress for like purposes: Congress has no power to regulate the manufacture of matches, or the use of oleomargarine; but it has suppressed the manufacture of the "white phosphorous" match and has greatly lessened the use of oleomargarine by imposing heavy taxes upon them. Congress

has no power to prohibit, or to regulate directly the issue of bank notes by state banks, but it indirectly prohibited their issue by imposing a tax of ten per cent. upon any bank note issued by a state bank.

The power of Congress over interstate commerce has been similarly utilized. Congress cannot ordinarily provide compensation for accidents to employees or undertake directly to suppress prostitution; but it has, as an incident of regulating interstate commerce, enacted the Railroad Employers' Liability law and the White Slave Law; and it has full power over the instrumentalities of commerce, like the telegraph and the telephone.

As such exercise of congressional power has been common for, at least, half a century, Congress should not hesitate now to employ it where its exercise is urgently needed. For a comprehensive prohibition of interlocking directorates is an essential condition of our attaining the New Freedom. Such a law would involve a great change in the relation of the leading banks and bankers to other businesses. But it is the very purpose of Money Trust legislation to effect a great change; and unless it does so, the power of our financial oligarchy cannot be broken.

But though the enactment of such a law is essential to the emancipation of business, it will not *alone* restore industrial liberty. It must be supplemented by other remedial measures.