The London School of Economics and Political Science

Doctoral Thesis

Banking Regulation in a Federal System: Lessons from American and German Banking History

Niels Frederik Krieghoff

A thesis submitted to the Department of Economic History
of the The London School of Economics and Political Science
for the degree of Doctor of Philosophy

Submitted: 23rd of April, 2013

[This version includes minor amendments added in July/August 2013]

Declaration of Authorship

I, Niels Frederik Krieghoff, certify that the thesis I have presented for examination for the MPhil/PhD degree of the London School of Economics and Political Science is solely my own work other than where I have clearly indicated that it is the work of others.

I warrant that this authorisation does not, to the best of my belief, infringe the rights of any third party.

I declare that my thesis consists of 99,996 words.

Abstract

This dissertation contrasts the development of the regulatory structure of the American and German banking systems until the mid-20th century. It explains why the countries' regulatory structures diverged into diametrically opposite directions, even though both countries had federal political systems and regularly observed the developments in the other country. Furthermore, after the Second World War, the American military government was even able to mold the German banking system into an idealized version of the American one. The thesis also provides an explanation why this assimilation attempt ultimately failed, and why there was a strong institutional persistency between Nazi Germany and West Germany instead.

The original contributions to knowledge are the following: (1) This thesis offers a novel perspective on the evolution of the structure of American banking regulation by interpreting it as being largely driven by constitutional conflict (2) it shows that prior to the Banking Crisis of 1931 there was no intention to introduce a comprehensive regulatory structure for the banking sector in Germany (3) It provides a reassessment of the origins of the German Credit Act of 1961 as a non-deterministic process (4) It interprets German banking regulation after the Second World War as a failed Institutional Assimilation, which provides evidence that the decentralized regulatory arrangement of the American banking system was held in place by strong states' rights. In the absence of strong states' rights such a system would not persist and, indeed, in Germany it did not (5) It re-interprets German post-war economic history as being driven by the need of the German federal government to re-establish supremacy over economic matters. This assigns a new important role for Ludwig Erhard in German post-war competition history, as being an enabler of liberalization rather than being a liberalizing force himself.

Keywords: Banking regulation, banking supervision, law and economics, political economy, institutional assimilation, financial crises, financial stability, path dependency, divergence, Olson Hypothesis, Weimar Germany, Third Reich, Germany, United States

JEL Classification: N20, G28, H77, P16

Acknowledgements

My gratitude goes to those who have helped me through this project in both tangible and intangible ways, including the many seminar, workshop and conference participants, as well as my two examiners, Jeffrey Fear and Stefano Battilossi, who gave me invaluable feedback on my work.

I especially thank my supervisor Albrecht Ritschl, who has guided me through this project with interest and enthusiasm, and whose intellectual breadth and curiosity is a source of inspiration second to none.

Furthermore, I particularly thank Katharina Gärtner, Eric Golson, Monia Manâa, Silvio Petriconi, Natacha Postel-Vinay and Peter Sims for providing me with constructive criticism on parts of this thesis and for their support throughout the PhD process.

This thesis grew out of an interdisciplinary research project on German regulatory history (*Gestaltung der Freiheit - Regulierung von Wirtschaft zwischen historischer Prägung und Normierung*) that was funded by the German Federal Ministry of Education and Research (funding code: 01UB0927) in the time period from 2009–2012. I hope that the reader finds that the investment in this project and me was public money well spent.

Contents

List of Figures

List of Tables

Abbreviations

ABC	Allied Banking Commission
AHC	Allied High Commission
BaFin	Bundesanstalt für Finanzdienstleistungsaufsicht
BArch	Bundesarchiv
BdL	Bank deutscher Länder
CCG	Control Commission for Germany / British Element
CCS	Combined Chiefs of Staff
CDU	Christian Democratic Union
CSU	Christian Social Union
DM	Deutsche Mark
DP	German Party (Deutsche Partei)
EAC	European Advisory Commission
ECB	European Central Bank
EU	European Union
FCIC	Financial Crisis Inquiry Commission
FDIC	Federal Deposit Insurance Corporation
FDP	Free Democratic Party
FHLB	Federal Home Loan Bank
FHLBB	Federal Home Loan Bank Board
FSLIC	Federal Loan Insurance Corporation
FRASER	Federal Reserve Archival System for Economic Research
J.C.S.	Joint Chiefs of Staff
KfW	Kreditanstalt für Wiederaufbau
NARA	National Archives and Records Administration
HICOG	High Commission for Occupied Germany

NMC	National Monetary Commission
NSDAP	National Socialist German Workers' Party
OMGUS	Office of the Military Government, United States
OTS	Office of Thrift Supervision
RFC	Reconstruction Finance Corporation
RG	Record Group
SEC	Securities and Exchange Commission
S&L	Savings and Loan Associations
SPD	Social Democratic Party
USHCG	United States High Commissioner for Germany

For Acácia

Chapter 1

Introduction

"[..] there is nothing more difficult to carry out, nor more doubtful of success, nor more dangerous to handle, than to initiate a new order of things."

– Niccolò Machiavelli in 'The Prince'[1]

1.1 Motivation

This thesis grew out of an observation known as *the long shadow of Hjalmar Schacht*.[2] Advocates of this view claim that the West German (henceforth Germany) economic structure looked much more similar to the corporatist economic structures implemented during the Third Reich than it has been suggested by the traditional literature.

Traditionally, the initial post-war period is seen as a major break in the German economic structure. In particular it is seen as a period of widespread economic liberalization by the ordoliberal movement, embodied by Economics Minister Ludwig Erhard

[1] The quote continues as follows: *"For the reformer has enemies in all those who profit by the old order, and only lukewarm defenders in all those who would profit by the new order, this lukewarmness arising partly from fear of their adversaries, who have the laws in their favour; and partly from the incredulity of mankind, who do not truly believe in anything new until they have had the actual experience of it."* See Machiavelli (1950, p. 21, Chapter VI).

[2] See Ritschl (2004). Hjalmar Schacht was a high profile German banker and policymaker during the inter-war period. He served as President of the central bank from 1923–1930, and again during the Third Reich from 1933 until 1939. From 1934–1937 he also held the office of acting Minister of Economics. Thus he was instrumental of many key economic reforms undertaken during the Third Reich.

and the idea of a 'social market economy'.[3] The ordoliberal movement, under the aegis of the American military government, is thought to have successfully destroyed encrusted interest groups that had monopolized the German economy in the past. Furthermore, the American military government and the ordoliberal movement are credited with introducing innovative regulatory structures that reduced regulations and exposed large swathes of the economy to strong competitive pressures. In turn, the increase in competition led to the mythical *Wirtschaftswunder*.[4] In a way, Ludwig Erhard is often depicted as the German equivalent of Britain's Margaret Thatcher.

Such an interpretation of German post war economic history is in line with the Olson hypothesis, which suggests that the Second World War provided a shock that destroyed encrusted interest group arrangements and allowed for socioeconomic reform and rapid economic growth.[5] As interest group coalitions began to encrust over time, economic performance was again retarded. This interpretation of the German growth experience has led to claims of a 'Fading Miracle'.[6]

One of the first to challenge the traditional view was Abelshauser. He emphasized that economic growth was underway well before Erhard allegedly liberalizing reforms took place. As a consequence, Erhard's reforms should not be seen as the principal driver behind the *Wirtschaftswunder*. Instead, he saw the principal driver in the reconstruction of the German economy and the return to Germany's growth potential. However, Abelshauser did not question the notion that a new and innovative economic framework was created by Ludwig Erhard. He merely acknowledged a persistence between pre- and post-war

[3]For an introduction into the ideas of the ordoliberal movement see for example Wünsche (1982) or the manifesto by Erhard (1958) himself. Ludwig Erhard was German Economics Minister from 20. 9. 1949 until 16. 10. 1963, after which he served as German Chancellor until 01.12.1966. Prior to his appointment as Economics Minister he was involved in the monetary and financial reconstruction of Germany. For biographies on Erhard see Hentschel (1998); Laitenberger (1986) and especially Mierzejewski (2004). Interestingly, after the end of his career they paint him as an exhausted and unfulfilled politician.

[4]Up until this day, the traditional view of the structural break in Germany's economic institutions is still influential within Germany. See for example Buchheim (1988), Klemm and Trittel (1987), Klump (1985, 1996), Prollius (2006, pp 50–109) or Wünsche (1986, 2001). A prominent exponent of the exceptionalism of the Third Reich's economic structure is also Temin (1991). More recently, Buchheim and Scherner (2006) have emphasized that the Nazi economy adhered to market principles to a large extent after all, and that it was by no means a totalitarian and monopolistic economic system it was often made to be. These findings somewhat relativize the magnitude of the structural break after the Second World War, but they do not call it into question altogether. Bel (2006) also highlights the remarkable privatizations undertaken by the Nazi government. For a comprehensive overview of the legislation of the Third Reich see Puppo (1988).

[5]For the seminal Olson Hypothesis see Olson (1982). For an application to the European and thus German scenario see also Olson (1996).

[6]See especially Giersch et al. (1992).

Germany in terms of the corporatist ideas and decision making.[7] More recently, an attempt has been made to synthesize the traditional view of the institutional liberlizations with that of reconstruction growth á la Abelshauser. The synthesis maintains the central importance of the alleged liberalization of domestic economic institutions, in order for reconstruction growth to take place.[8]

In the non-German literature a prominent view emerged that highlighted the commonality of the German growth experience. Indeed, it was much of Western Europe that experienced a period of extraordinarily high growth after the Second World War. Since not all the countries were successful in reforming their domestic institutional framework after World War II, they see the source of the rapid economic growth in a reallocation of productive resources. According to this view, resources had been misallocated due to a lack of trade and a failure to adopt the newest technologies in the preceding decades. After the Second World War, labour and capital was finally reallocated efficiently and modern production technologies were adopted. This enabled rapid economic growth and productivity catch-up with more advanced economies such as Britain and the United States, who had already undergone similar transformations and were closer to the technological frontier. Fast post-war economic growth in Germany and elsewhere in Western Europe is seen merely as the result of the closing of a productivity gap with the help of an improved international institutional framework.[9]

Proponents of the existence of a *long shadow of Hjalmar Schacht* in Germany acknowledge that the German currency reform of 1948 and the loosening of war-time price controls were important moves towards normalizing economic conditions. Yet, in their view, these reforms merely represented the necessary transition from a war economy to a peacetime economy, thus enabling reconstructive growth. At the same time they point out a number

[7]See Abelshauser (1975, 1979, 1983, 1991). Similarly see Manz (1968). Jánossy (1966, 1971) made a similar observation for Europe in general.

[8]See Lindlar (1997) for the German case. For a similar line of argumentation for Western Europe as a whole and the importance of the reform of international institutions see for example Eichengreen (1996) and Bradford and Eichengreen (1993).

[9]See for example Abramovitz (1986), Baumol (1986), Temin (2002) and Crafts and Toniolo (1996). The most prominent theoretical embodiment of such a view is the first generation neoclassical growth model. Eichengreen and Ritschl (2009, p. 194, fn. 4) point out that it was no coincidence that the Solow (1957) growth model emerged at the time it did. Dumke (1990) conducted an econometric analysis comparing the productivity gap hypothesis with the reconstruction hypothesis. He finds that the main driver of growth was reconstruction rather than catch-up, and especially so in the German case. Similarly see also Vonyó (2008).

of institutional persistencies, implying that the German economic institutional structure did not undergo much of a change after the Second World War after all. Instead, the economic framework of the Federal Republic of Germany constituted a return to the old path – the path initiated by Hjalmar Schacht during the Third Reich. Whichever novel, pro-market institutions Ludwig Erhard and the American military government might have introduced in the post-war period were soon dismantled and replaced with their Nazi-era sibblings. In several cases the economic institutions from Nazi Germany were adopted in post-war Germany without any modification whatsoever. Thus, the alleged uniqueness of the institutions of the social market economy cannot be seen as a driver of rapid German economic growth. Instead, the proponents of a long shadow of the Third Reich see the institutional persistence as stability inducing. And it is this stability, which allowed German reconstructive growth to take place at the pace it did.[10]

Existing explanations for such a strong path dependency emphasize that most economic regulations introduced during the Third Reich did not find their origins in Nazi ideology. Rather, they reflected an international tendency towards corporatist economic structures that was already exhibited by the late Weimar bureaucracy. This made it possible for the German political elite after the World War to successfully de-ideologize the Nazi economic reforms and to recycle the Nazi-era institutions, masquerading the long shadow of Hjalmar Schacht as a long shadow of the Weimar bureaucracy, or, alternatively, as innovative institutions that formed part of the new social market economy.[11]

But are the claims tenable that many of Germany's path dependent institutions took their shape in the early 1930s, and that Schacht and not Erhard, is consequently the father of the *Wirtschaftswunder*? Is postwar Germany just a linear extension of the Third Reich in terms of economic policy?[12] If there is indeed an institutional shadow of the Third Reich, one is left with a paradox. Given all the Thatcherite intentions of Ludwig Erhard and the American military government, why is it that pre-war German institutions were

[10] Eichengreen and Ritschl (2009, 2009–214) and Ritschl (2005, pp. 159–164) provide an overview of alleged economic institutional persistencies. Hardach (1980, pp. 140–160) also identifies many institutional continuities. A similar point about the importance of continuity and consistency in policymaking is also put forward by Wolf (1993). He argues that both France and Germany achieved rapid growth, despite pursuing radically different growth strategies.

[11] See for example Carlin (1996), Dornbusch (1993), Eichengreen and Ritschl (2009), Paqué (1993, 1996) and Ritschl (2004, 2005).

[12] See especially Ritschl (2004, 2005).

so persistent after all? If neither Ludwig Erhard nor the American military government were the forces shaping the institutional economic framework of postwar Germany, who or what did?

In order to find additional meaningful answers to this paradox one needs to look at specific sectors of the economy.[13] In particular the banking sector seems to have exhibited a strong degree of path dependency. After the Second World War, the American military government forced major structural changes onto the German banking system, assimilating it to the American state banking system. And even given this major exogenously-imposed institutional break, a return to the pre-war institutional arrangement takes place. Why did German policy makers choose to remain on the historical path? Why did they not introduce any structural innovations?[14] Such a development becomes even more remarkable, if one considers the fact that both Germany and the United States had federal political systems. Thus, the failure of the American institutional set-up to survive in a German constitutional context is intriguing not only for German banking history, but it holds important lessons for American banking history and its regulatory development as well. After all, the decentraliezd regulatory regime of the American banking sector was, until the integration of European capital markets, unique.

Indeed, this thesis may even be of interest not only to economic historians, but also to American and European policymakers today, who are working to reform the regulatory framework. In particular it can hold important insights insights for current EU debates with respect to the banking union. Up until the beginning of the financial crisis in 2007/08, the regulatory arrangement within the European Union was – and to a large extend still is – a decentralized set-up with a few harmonizing elements, such as the Basel rules or

[13] So far there has been relatively little targeted research into institutional persistencies between pre-war Germany and the Federal Republic of Germany. Some studies have analyzed the influence of the Allied intervention on the Antitrust Act of 1957, such as Berghahn (1986) and Murach-Brand (2004). Others have highlighted the immense institutional persistencies in the regulation of the energy sector, such as Künsberg (2012). Löffler (2002) provides evidence for personnel continuity within the Ministry of Economics, whereas Marsh (1992) documents the return of the old guard within the Central Bank. Grunenberg (2006) compiled evidence on the personnel persistency of the German business elite. However, these works rarely created a direct institutional link between the Third Reich and post-war Germany.

[14] That banking systems show a large degree of path dependency was already recognized in Bagehot's time: *"A system of credit which has slowly grown up as years went on, which has suited itself to the course of business, which has forced itself on the habits of men, will not be altered because theorists disapprove of it or because books are written against it."* Bagehot (1915, pp. 310–311) writing about the English Banking System in 1873.

coordination bodies at the European level, despite the efforts of the Lamfalussy process which began in the early 2000s. The current financial crisis intensified the drive towards a European banking union. The banking union aims to re-allocate regulatory powers by lifting actual regulatory and supervisory powers from the country to the European level. Of course, this attempt to change the regulatory structure and thus regulatory responsibilities is not free from conflict, as it directly affects the sovereignty of European countries. However, many of the (constitutional) issues debated today are indeed similar to those that arose in both Germany and the United States in the time periods under consideration in this dissertation. In particular the question of subsidiarity, i.e. the optimal level of decentralization in banking regulation, has been a source of constitutional conflict in the past.[15] Thus, the current banking union debate is not without historical precedent.

1.2 Theoretical background

Debates about the origins of regulatory institutions typically assume one of two starting points.[16] The traditional viewpoint is that of 'public interest', where a benevolent government aims to rectify shortcomings of the market process ('market failures') to restore economic efficiency.[17] These market failures may be be caused by asymmetric information, moral hazard, negative externalities, natural monopolies or other anti-competitive behavior.[18] Thus, any existing (banking) regulation would always be seen as the result of a government intervention that led to a pareto improvement over an unregulated (banking) sector, which was suffering from market failure. Otherwise such a regulation would not arise in the first place.

[15] For an introduction into the principle of subsidiarity see for example Bermann (1994). For an application of the subsidiarity principle to economic regulation see for example Laffont and Pouyet (2003).

[16] This is valid for financial as well as other types of regulation. For a general discussion of the two positive theories of government policy see for example Joskow and Noll (1981) or Peltzman (1989).

[17] Important contributions to this viewpoint were for example Pigou (1932) and Samuelson (1954). Gerschenkron (1962) would also be an example of this viewpoint of government policy in the banking sector.

[18] For an overview regulatory instruments used to rectify these market failures in traditional industries see Viscusi et al. (2005, Chapters 5,6). For an overview of the regulatory tools in the banking sector see for example Mishkin (2010, pp. 255–271) or Brunnermeier et al. (2009, pp. 29–56).

Since the late 1970s the 'private interest' viewpoint has become the preferred starting position.[19] It arose from observations of 'government failure' that the public interest viewpoint failed to explain. Regulatory intervention did not always improve efficiency, and in some cases even lead to adverse outcomes.[20] The primary reason for this government failure was found to be with the capture of regulatory institutions. Rather than being interested in the welfare of society as a whole, policymakers were now assumed to maximize their private interest.[21] While in office, policymakers are subject to influences by a number of interest groups, which also seek to extract rents. The 'tools' at the disposal of interest groups to influence policymakers are considered to be either direct or indirect. Direct measures may be contributions to campaign finance or votes, whereas indirect measures promise future cooperation with the policymaker, such as the promise of a well-paid job, once the policymaker leaves its current position.[22] It is this political market that determines the regulations that are eventually implemented. The outcome of this political bargaining process redistributes rents, creating winners and losers. However the regulations are often presented to the public as being in the best interest of society, thus concealing the underlying interests of policymakers or special interest groups to the public.[23] Advocates of the private interest view, generally propose the deregulation of markets to counter this kind of government failure. This 'remedy' has been a policy adopted in a number of markets since the 1970s.[24]

Ironically, the widespread success of the deregulation ideology may have shown the limitations of the private interest view, in the sense that certain regulations were abandoned even though they may have been in the interest of the vast majority of the regulated

[19] Influential works of this viewpoint were those of Becker (1983), Buchanan and Tullock (1962), Buchanan (1975), Peltzman (1976), Laffont and Tirole (1991) Olson (1971) and especially Stigler (1971).

[20] See for example the works of Meyer et al. (1959) and Stigler and Friedland (1962).

[21] Related to the private interest of policymakers is the "grabbing hands" hypothesis, which postulates that politicians seek control over banks to re-allocate capital according to their own preferences, to the detriment of society. See Fischer and Pfeil (2003, pp. 6–9), La Porta et al. (2002) and Shleifer (1994).

[22] For an overview of the tools see for example Laffont and Tirole (1991, pp. 1090–1091).

[23] Financial services are often seen to be one area with the most extensive activity of special interest groups. See for example Kane (1996), Kroszner and Stratmann (1998), Kroszner and Strahan (2001) or more recently Admati and Hellwig (2013).

[24] Scholars have noted that even the deregulatory processes themselves can be subject to capture and thus lead to inefficient outcomes after all. See for example Feijen and Perotti (2005) on the liberalization of finance in developing countries.

industry, and should not have been abandoned according to the private interest view.[25] Additionally, it has been pointed out that some of the private interest influenced research has overstated its explanatory power beyond what the evidence could support.[26]

More recently attempts have been made to move beyond the pure dichotomy of interpreting regulatory outcomes as those of either public interest attempting to alleviate market failure or of private interest engaging in rent seeking, by widening the objective functions of the political actors. One strand of research has identified ideology as a potentially important factor influencing policymakers decision-making.[27] Another has highlighted the role of the institutional arrangement, not only by influencing policy through its impact on the relative bargaining positions of interest group and policymakers, but also through its role in constituting markets in the first place. Regulation is no longer seen as merely market intervening, but can also be seen as market enabling.[28] Other scholars are experimenting with cooperative models of social and political behavior, which they often find to be just as powerful explanatory tools as the private interest models.[29]

The main challenge remains, however, to identify the circumstances under which private interest prevails over (an expanded definition of) the public interest. And in order to identify them we need to search for historical instances in which private interest did not trump public interest.[30] This thesis can contribute to that search by identifying the key players and their respective objective functions from a comparative perspective. Such a cross-country study allows for a comparison of the relative merits of either viewpoints in explaining the differences in the regulatory structure of both countries' banking sectors.[31]

[25] See Peltzman (1989). In related articles, Kroszner (2001) and Kroszner and Strahan (1999) argued that, at least in the banking sector, the private interest view could explain the deregulation after all.

[26] See for example Leight (2009), Wittman (2009) and especially Moss and Oey (2009), who point out that there are a number high profile-cases in which special interest group with lesser benefits and higher costs to organize have dominated those with more potential benefits from regulation and lower costs to organize. According to Stigler's theory of regulation this should not be possible.

[27] See for example the works of Gilligan et al. (1989) and Poole and Rosenthal (1993) on the regulatory debates in the 19_{th} century. Similarly see Furner (2009) and Fligstein (2009). They note that key regulatory developments were driven in both the United States and Europe were sometimes driven by ideological considerations relating to social and economic legitimization.

[28] See for example Weingast and Marshall (1988) on how legislatures are unlike markets and its impact on policymaking. See Carpenter (2009) for the role of institutions to constitute markets.

[29] See for example Benkler (2009). See the edited volume by Balleisen and Moss (2009) for an overview of the most recent trends in regulatory theory. The edited by Moss and Cisternino (2009) provides a number of suggestions on how to improve actual regulations, based on the recent insights from research.

[30] See Moss and Oey (2009, pp. 30–31).

[31] See Leight (2009, p. 21) for the value of cross-country studies.

Furthermore, this thesis has the unique advantage of benefitting from an intriguing interaction in the form of an assimilation of the German regulatory framework to the American one after the Second World War by the US military government.

1.3 Research Agenda

This work sheds light on the evolution of the regulatory structure in Germany and the United States from the early 19th century until the mid 20th century. It uses a comparative approach to identify the drivers behind the regulatory structure and the path dependency of the two banking systems. In this thesis I will use the term 'regulation' as the act of setting the specific rules banks need to adhere to, such as the act of imposing a minimum capital ratio (a 'regulatory tool'). The term 'supervision' is used for the day-to-day operations that implement the regulatory policies by verifying banks' compliance with the regulations. The term 'regulatory structure' refers to those government institutions with the power to supervise or regulate the banking sector.

The comparative perspective is interesting and relevant, because both are countries with federal political systems,[32] but their approach to regulating the banking sector followed diametrically opposed principles for much of their history, even though their banking history was closely intertwined. Indeed, after the Second World War the American military government even had the opportunity to impose their regulatory principles on the German banking sector, but the American institutions failed to persist.

The financial crises of the late 19th and early 20th century induced a spur of regulatory discussion and reform in both countries. In the United States it culminated in the Glass-Steagall reforms of 1933 and 1935, and in Germany in the Credit Act of 1934. What is striking is that both countries enacted different regulatory structures, even though during the respective debates they studied each other's banking systems in great detail.[33] In Germany it was decided to introduce a regulatory monopoly. Contrary to that the

[32] The exception were, of course, the years of the Third Reich, where political control was highly centralized.

[33] For example see the American and German banking commissions of 1911 and 1933, respectively: National Monetary Commission (1910a,b, 1911); Volkswirtschaftliche und Statistische Abteilung der Reichsbank (1933); Wilz (1933).

United States emerged from the Great Depression with a complex decentralized regulatory and supervisory system, where responsibilities were often overlapping between various institutions both at the state and the national level. There is no comparative account as to why this divergence took place. At first sight it seems that there was no agreement on regulatory best practices. Furthermore, these reforms to the banking regulations have an extremely long half-life time as they survive well into the 1970s and 1980s in both countries.[34] Path dependency seems to be the main driver of this development in both countries. But what is it that drives this path dependency?

After the Second World War, the Americans were effectively in control of much of West Germany. This allowed them to mold the German banking system to their liking. The Soviets did use their 'privilege' in East Germany and completely dismantled the existing banking system and established a nationalized banking system.[35] And indeed, during this time, the Americans were not inactive either. They undertook extensive efforts to impose an American-style banking system on Germany. This included the introduction of branching restrictions, the decentralization of the largest banks as well as the decentralization of the central bank and the regulatory authorities.[36] Effectively, the Americans attempted an institutional assimilation. Yet, when one looks at the German Credit Act of 1961 one cannot help but be struck by the similarities to its 27 year old brother from 1934. Branching restrictions were also repealed and the three largest universal banks had also 'miraculously' resurrected from their previous break-up into dozens of parts. Last but not least, the Bundesbank looks more like the centralist Reichsbank and less like its predecessor the *Bank deutscher Länder*, which was modelled along the lines of the decentral American Federal Reserve System. Thus, it seems as if in the case of banking, the American institutional assimilation has failed and that the *long shadow of Hjalmar Schacht* prevailed. Where do these strong path dependencies between the Third Reich and the Federal Republic of Germany come from? How large is, ultimately, the American

[34] The United States and Germany are by no means the only countries conducting extensive reforms to their banking regulations in the 1930s. Other European countries include, Austria, Belgium, Hungary, Italy, etc.. See (Cassese, 1984).

[35] See for example Adler (1949, pp. 333–334) for the Soviet approach towards the banking system in its zone.

[36] This is much like the Allies had tried in other sectors of the German economy, in particular the heavy industry and the chemicals. See Clay (1950, pp. 326–327) or Plumpe (1990, pp. 756–759).

influence on German banking regulation and to what extent are the Americans successful? In case they did not leave any mark on the German banking system, why is this so? What can we learn from the American experiment in Germany for the American regulatory structure?

1.4 Methodology & Sources

At the heart of this investigation lies the aim to analyze the decision-making processes that lead to changes in the respective regulatory structures. Thus, it is a history of economic decisions and therefore a history of the ideas and power struggles behind those decisions. For the German history, the basis of my qualitative reconstruction of these decision making processes relies to a significant extent on archival and digitalized government sources. The American history is reconstructed using congressional records, a number government publications, as well as the vast secondary literature on American banking history.[37]

In terms of German primary material, I am making use of records by the German Finance Ministry, the Economics Ministry and of the Chancellery of both the pre-World War II and post- World War II periods, as well as the records of the central bank of the pre-war period. For the pre-war era these are the records of the *Reichsbank (R2501)*, the *Reichsfinanzministerium (R2)*, and the *Reichswirtschaftsministerium (R3101)* found at the German National Archives, the *Bundesarchiv*, in Berlin-Lichterfelde. The majority of *Reichskanzlei (R43)* records are available digitally at the website of the Bundesarchiv.[38] For the post-war period the relevant German files are the records of the *Bundesfinanzministerium (B102)*, the *Bundeswirtschaftsministerium (B126)* and the *Bundeskanzleramt (B136)* found at the Bundesarchiv in Koblenz.

For the American occupation period of Germany after the Second World War, I am also making use the Records of the American Office of the Military Government (better known as 'OMGUS' - RG 260), the Records of the High Commissioner of the United States in Germany (RG 466) and the Records of the Foreign Service Posts of the Department of

[37] Literature reviews can be found in the introduction of each chapter.

[38] Available at http://www.bundesarchiv.de/aktenreichskanzlei/1919-1933/0000/index.html, last accessed on 07.03.2013.

State (RG 84). These were found at the National Archives and Records Administration in College Park, Maryland.[39]

Apart from internal government material, I am making extensive use of government hearings and other official publications. This includes printed materials of the German Bank Commissions of 1906/07 and 1933/34, the American National Monetary Commission of 1908-1913,[40] various hearings of the U.S. Senate and the House of Representatives as well a number of studies prepared by the Federal Reserve Committee on Branch, Group and Chain Banking, [41] and the documents prepared for the Board of Governors Federal Reserve Bank Suspension Study.[42]

1.5 Structure & Outline

This thesis consists of three closely linked, but otherwise self-contained chapters (Chapter 2, 3 and 4), followed by an Epilogue and a Conclusion. Conceptually, this dissertation is divided into two parts. The first part is a double biography of the regulatory structure in Germany and the United States up until 1935 (Chapter 2). It tries to explain why there was such a stark divergence of the regulatory structure between the two countries up until the Second World War. Why did German policymakers decide to introduce centralized banking regulation during the Great Depression, whereas policymakers in the United States did not? This comparative approach is chosen so as to be able to highlight the different regulatory and political traditions in both countries. This is especially important for the second part of this dissertation, when I try to explain why the American Institutional Assimilation failed.

The second conceptual part of my thesis is divided into two chapters that directly address the *long shadow of Hjalmar Schacht* in the banking sector. Chapter 3 examines

[39] For the pre-World War II era, I have also examined the Records of the U.S. Treasury (RG 56) and the personal papers of Adolf A. Berle and Henry Morgenthau, Jr., but this line of investigation did not yield novel insights. The personal papers were found at the Roosevelt Presidential Library in Poughkeepsie in New York State and the Records of the U.S. Treasury (RG 56) at the National Archives in College Park.

[40] The numerous volumes of the National Monetary Commission are available at via FRASER at `http://fraser.stlouisfed.org/topics/?tid=13`, last accessed on 04.03.2013.

[41] Available online via FRASER at `http://fraser.stlouisfed.org/author/?aid=1699`, last accessed on 04.03.2013.

[42] Also available via FRASER at `http://fraser.stlouisfed.org/publication/?pid=684`, last accessed on 04.03.2013.

the decision making behind the basic law determining the regulatory framework in post war Germany. Chapter 4 builds on the findings of the previous two chapters. It interprets German post-war banking regulation as an attempted Institutional Assimilation and looks for reasons why it failed. This episode provides important insights not only for German regulatory history, but also for American regulatory history. Chapter 5 serves as an epilogue, providing the reader with a brief presentation of the regulatory developments in the German banking sector in the immediate years after the passage of the Credit Act of 1961. Chapter 6 concludes this thesis by identifying implications from this piece of research. It also provides a link to today's discussions surrounding the reform of banking regulation in Europe and the United States.

Abstracts of the following chapters can be found below.

Chapter 2: Americans wanted it. Germans got it. Why Germany introduced centralized banking regulation and the U.S. didn't

The second chapter contrasts the development of the structure of banking regulation in the United States and Germany before the Second World War. In the United States leading politicians and government officials tried to introduce centralized banking supervision several times, however it failed to materialize. On the contrary, as 'regulatory ruins' from previous attempts to unify the regulation were not removed, the United States moved even further away from a centralized regulation of its banking system. Conversely, in Germany the introduction of a centralized regulatory framework encounters little resistance. The primary reason for this diverging development in Germany and the United States is to be found in the prevailing constitutional and political systems at the time, rather than diverging views on regulatory best practices. The American constitution secured the states' right to charter banks and thus required American policymakers to create incentives for state banks to subject themselves voluntarily to central regulation. The German constitution contained no such provision, allowing for outright centralization of regulatory powers.

Chapter 3: The (re-)birth of the German Credit Act of 1961

This chapter investigates the origins of the German Credit Act of 1961 that regulates the German banking sector. The Act of 1961 was essentially a re-birth of its older brother from 1934, even though the war and the subsequent Allied occupation of Germany had introduced important changes to the regulatory structure. This chapter shows that the reversal of Allied changes to the regulatory structure was not a conclusion foregone. The primary reason for the similarity of the banking acts is to be found in the government's desire to re-introduce a unified regulatory structure, for which it required a parliamentary supermajority. In order not to jeopardize the supermajority the government refrained from introducing potentially controversial "innovations". Furthermore, a key issue in the drafting process was to what extent competition should be allowed in the banking sector. This chapter provides evidence that the German private banking association successfully lobbied for a restriction to competition.

Chapter 4: A failed Institutional Assimilation: The American attempt to restructure German banking regulation after World War II

In the fourth chapter I am making use of a little-known episode in German banking history to test whether the reason that the American regulatory system developed into the decentral structure it did (and why the German banking system did not) was indeed primarily a function of the extensive states' rights – with respect to chartering banks – enshrined in the American constitution. This chapter also adds to the literature by presenting the history of German banking institutions from 1945 until 1961 from a unified perspective.

After the Second World War, a drastic and direct effort to change the West-German banking system was undertaken by the American military government. It restructured the entire banking system: its rules, its regulatory institutions, and its major financial institutions. The most important elements of the American state banking system were imposed on the German banking system exogenously with the help of military decrees. However, the new German constitution (the 'Grundgesetz') lacked similar provisions to those in the US constitution that guaranteed the states the right to charter banks. Thus, this American assimilation effort can provide important insights into American banking history, as it can be interpreted as a natural experiment testing whether the American regulatory system was a second-best arrangement that was held in place by strong state rights that would not survive in the absence of strong state rights.

And indeed, in the German political set-up one can observe a fierce struggle between the German states, who wanted to retain their newly gained rights, and the federal government, who wanted to re-centralize the regulatory structure. This struggle was ultimately decided in the constitutional court. If the constitutional court had ruled in favour of the states instead of the central government, parts of the American institutional structure could have survived in the German banking system. Instead, the American institutions disappeared completely. This implies that, indeed, the regulatory arrangement of the American banking system was only a second-best solution that was held in place by these strong state rights. In the absence of these institutional constraints, no such system would have persisted in the United States. Rather than portraying a supposed resilience of the German banking sector, this episode highlights the weakness of the American regulatory arrangement.

Chapter 5: Epilogue

The epilogue presents the regulatory developments in Germany in the aftermath of the passage of the Credit Act of 1961, which led to the removal of the main barriers to competition that had been in place since the early 1930s. The liberalization was preceded by a major dispute between the private banks and the public banks. Whereas the public banks demanded that restrictions to competition be dropped, the private banks wanted to maintain them for as long as the public banks' implicit and explicit government subsidies had not been abolished abolished. In the late 1960s the federal government proceeded to remove both the restrictions to competition and some of the preferential treatments the public banks had enjoyed in the past.

Chapter 6: Conclusion & Discussion

This thesis finds that the main driver for the diverging developments of the regulatory structure in Germany and the United States are not to be found with differing views of best practice regulation of the banking sector, but with the varying degree of constitutional states rights with respect to the chartering of banks. Whereas American policymakers attempted to implement a centralized regulatory system at various points in time, it failed to materialize as the central government was unable to strip the states from their rights to charter banks. In Germany, the introduction of a centralized regulatory system is only resisted after the Second World War, when the American military government had assigned the right to regulate the banking sector to the German states. Since the American military government failed to implement equivalent constitutional safeguards in the German *Grundgesetz*, the German central government was eventually able to recentralize regulatory control. This post-war episode provides further evidence for the weakness of the American regulatory arrangement and that it was indeed held in place artificially by strong states' rights, rather than by macro-prudential considerations.

The German need to recentralize control is also the primary reason why we see a *shadow of Hjalmar Schacht* in the banking sector. Any innovative regulatory reform, would have jeopardized the necessary supermajority to recentralize control over the banking sector, and was consequently left for the future. This is why we see a retreat to the pre-war status quo in 1961, which is then followed by a gradual liberalization of the banking sector. Such an interpretation of German post-war history also implies an inversion of the Olson hypothesis. It interprets the early after-war period as one of institutional sclerosis that was induced by the American decentralization of economic control, which led to a period of prelonged constitutional struggle between the states and the central government. Only after the central government was able to reestablish its control over the economy was it able to engage in truly liberalizing reforms. One of Ludwig Erhard's primary contributions to the German economy is thus seen in his ground-work to re-establish the central government's undivided primacy over economic matters.

Chapter 2

Americans wanted it. Germans got it.

Why Germany introduced centralized banking regulation and the U.S. didn't.

2.1 Introduction

Today there is much talk about the international harmonization of 'best practice' regulations.[1] Theoretical and empirical evidence suggests that in an integrated financial market a unified regulatory system is superior to a strongly decentralized regulatory system. Primarily, this is because under a decentralized regulatory regime, banking regulation yields externalities, which create incentives for individual regulators to lower their standards in an effort to promote banks under their supervision. Additionally, in times of crisis a central regulatory agency has easier access to the relevant information and greater flexibility in crisis resolution, as less coordination between numerous agencies is required.[2] Current

[1]See for example Brunnermeier, Crocket, Goodhart, Persaud, and Shin (2009) or the efforts of the Basel Committee to harmonize capital adequacy standards. For the limits to bank regulation and a critique to harmonization of so-called 'best practices' see for example Barth, Caprio, and Levine (2006) or in general Rodrik (2007).

[2]See for example Dell'Ariccia and Marquez (2006); Beck, Todorov, and Wagner (2011); Calzolari and Gyongyi (2011); Čihák and Podpiera (2007); Freixas (2003); Goodhart (2002); Goodhart and Schoenmaker (2009); Hackley (1966a,b); Holthausen and Rønde (2004); Kahn and Santos (2005); Padoa-Schioppa (1999); Rezende (2012) and Schoenmaker (2011). For the proponents of centralized regulation, the only remaining question is whether unified regulation should be the responsibility of the central bank or whether an independent agency should be tasked with this. See for example Čihák and Podpiera (2007), Masciandaro (2009) and Quityn et al. (2007). Others have argued that a decentralized system might be preferable over a centralized one for three reasons. First, a decentral structure might allow for better gathering and evaluation of soft (local) information on banks. Second, institutional competition might lead to more efficient regulatory institutions. Third, decentral institutions reduce the risk of regulatory capture. See Holthausen and Rønde (2004), Golembe (1967), Kane (1984), Laffont and Martimort (1999) and Rosen (2003). For an agnostic view see Grossman (2010).

developments in the wake of the Great Recession confirm this theoretical preference, as policymakers strive to introduce more centralized regulatory arrangements.[3]

One of the most striking features of the American banking system is the absence of a regulatory monopoly.[4] This is true today, and it was true in the 19th century. The contrary is true in Germany. For much of their history, the regulatory structures of the banking sector in Germany and the United States followed opposing approaches. Whereas in Germany a centralized structure was put in place, with only two federal institutions involved in the regulation and supervision of the banks, in the United States the structure was decentralized, with several chartering authorities and numerous regulatory and supervisory institutions at both the state and the federal level.[5]

This structural divergence becomes even more puzzling given the fact that, prior to the Second World War, both countries were discussing banking regulation at roughly the same times: after severe international financial crisis of 1907, and again in the early 1930s during the Great Depression. And even though they studied each others' banking systems extensively,[6] they still implemented different regulatory structures. Why did we not observe a harmonization of regulatory structures in Germany and the United States in the wake of the Great Depression?[7] Was it because policymakers in Germany and the United States had different perceptions as to which regulatory structure would be preferable? This question matters since the regulatory decisions taken then have largely persisted and continue to influence banking policy.[8] This chapter adds to the literature by tracing the idea of a centralized regulatory regime through history in both Germany and

[3]As part of its plans to form a banking union, the Eurozone struggling to introduce a more centralized regulatory structure . In the United Kingdom similar tendencies are also visible. See for example European Commission (2012a,b),The Economist (2012b) and HM Treasury (2011).

[4]See (White, 1982, p. 37).

[5]'Banking regulation' is defined as all the legal rules and institutions that are targeted directly at banks. Legal norms that apply to a wide range of businesses, such as corporate law, are not considered to be part of the banking regulations. The 'regulatory structure' consists of the set of all those government agencies that are tasked by law to establish, supervise or enforce the norms applying to the banking sector. 'Banking supervision' is understood as the 'policing' or enforcement of banks compliance with the regulatory norms.

[6]For example, see the American and German banking commissions of 1911 and 1933, respectively: National Monetary Commission (1910a,b, 1911); Volkswirtschaftliche und Statistische Abteilung der Reichsbank (1933); Wilz (1933).

[7]A similar question is asked by Di Martino, Paolo (2010) for the case of the evolution of Bankrupcty Laws and Procedures in Italy, the UK and the United States, and by Fear and Kobrak (2006), who analyze the divergence in accounting systems in the United States and Germany prior to the Second World War. See also Haber (2007), who compares the evolution of banking regulations in the United States and Mexico from 1781–1932. However, Mexico's constitutional set up was changing frequently throughout this period.

[8]See also Cassese (1984) for *"The long life of the Financial Institutions Set up in the Thirties".*

the United States, and by providing an explanation as to why it 'succeeded' in Germany and not in the United States.

The political economy of American banking regulation for the period up until the Second World War has been the subject of extensive research.[9] Seminal works in the area are Hammond (1957) for the time period to the American Civil War and White (1983) for the years from the Civil War until the beginning of the Great Depression.[10] The point of reference for the regulatory reforms undertaken during the Great Depression is the careful study by Burns (1974).[11] Calomiris (2006b) provides an historical overview on the political economy of all aspects of U.S. banking regulation from its beginnings up until the 1990s.[12] The recent work of White (2010) tries to identify the origins of the regulatory impulse in the United States. He argues that the nature of changes in regulation following financial crises in the United States were a function of the political equilibrium at the time, which in turn was upset by productivity surges.

In addition to these general studies, there are numerous other works analyzing specific aspects of the regulatory history. For example, there is research on deposit insurance by Golembe (1960), Calomiris (1990) and Calomiris and White (1994), on the seperation of investment banks by White (1986), Benston (1990) and Kroszner and Rajan (1994), or on branch banking by Sprague (1903), Chapman and Westerfield (1942), and Economides et al. (1996). Surprisingly however, the question, why the United States did not develop a centralized regulatory system, has hardly been tackled head on. The most prominent work is the historical dispute between Hackley (1966a,b, 1969) and Golembe (1967) on the optimality of the banking system. Whereas Hackley argues that there were attempts to centralize banking regulation, Golembe takes the opposite standpoint. He argues that all major regulatory changes taken were knowingly designed *to ensure a decentralized banking system*.[13] Golembe's view seems to have prevailed, as in recent accounts on the regulatory changes prior to the Second World War it is often assumed that there was never a serious

[9] For a general historiographical survey on U.S. commercial banking see Schweikart (1991).

[10] Redlich (1947, 1951) also provides a comprehensive history of regulatory ideas from independence until 1910. Fischer (1968) also provides a general overview of the American banking structure.

[11] Kennedy (1973) is often overlooked as it focuses on the Banking Crisis of 1933, rather than on the regulatory reforms in its entirety. Nevertheless, it is also an invaluable source.

[12] The official history of the office of the Comptroller of the Currency by Robertson (1968) also provides a long-term view up until the 1960s.

[13] See Hackley (1966b, pp. 824–830) and Golembe (1967, p. 1100).

attempt to centralize the regulatory structure of the United States.[14]

This chapter re-opens the Hackley-Golembe debate. It carefully re-considers existing research, underrepresented primary material,[15] and the relevant legislation, in an effort to lay bare any attempts to centralize the American regulatory structure prior to the Second World War. It argues that before the Second World War there were three major attempts by the federal government to introduce a centralized regulatory system.[16] First, with the establishment of the national banking system (1861–1865), second with the establishment of the Federal Reserve System (1910–1917) and finally with the establishment of the Federal Deposit Insurance (1930–1935). However, the federal government could not simply prohibit states from chartering and regulating banks. A constitutional barrier prevented it from outright assuming control of banking regulation. As a consequence, the government had to devise a system of regulation and economic incentives that would compel state banks to subject voluntarily to federal regulation in order to benefit from associated economic advantages that came with it. Unlike a direct assumption of control by the federal government, these incentive schemes could easily by circumvented by state regulators. Thus, every single of the three attempted centralizations prior to World War II failed, as they were loopholed soon after their establishment either by legislation or financial innovation. Furthermore, each unsuccessful attempt to build a national framework left behind institutions that were not torn down during subsequent efforts to reform the regulatory framework. These 'regulatory ruins' developed into full-fledged political actors. This is why the United States developed such a highly decentralized banking regulatory framework for its banking sector.

Contrary to the United States, Germany introduced a centralized regulatory regime.[17] However, the economic literature on the origins of the German regulatory structure is not as extensive as its American counterpart. There is little research which takes into account the entire regulatory discussion prior to the Second World War and that tries to

[14]See for example Calomiris and White (1994), Calomiris (2010), Wall et al. (2011) or White (1982). White (1983) acknowledges that there might have been an attempt during the introduction of the Federal Reserve System, but this aspect does not figure prominently in his work.

[15]This material includes Congressional Records, material by the National Monetary Commission and numerous reports by the Board of Governors of the Federal Reserve System.

[16]In the contemporary material this is often also referred to as the introduction of a 'unified commercial banking system under national supervision'.

[17]Indeed, this was the case in much of Europe. For an overview of regulatory developments in Europe and the U.S., see for example the edited volumes by Battilossi and Reis (2010) and Sylla et al. (1999).

explain why regulation took the structure it eventually did.[18] Several works deal with the development of the German banking system up until 1913, such as Edwards and Ogilvie (1996), Fohlin (2002, 2007); Guinnane (2002); Pohl (1982b,c) or Tilly (1986). These do shed some light on the regulatory structure and the discussions, but this is not their main focus. The closest the literature gets to a an evaluation of the regulatory discussion at the turn of the century are the contemporary works of Riesser (1911, Part III, Chapter II, Section 8) and Schachner (1910), and the modern Tilly (1999). Similarly, the period between 1914 and 1934 attracted numerous scholars analyzing the development of the banking sector as a whole, such as Balderston (1991); Hardach (1984, 1995a,b) or James (1985), or specifically the German financial crisis of 1931, such as Balderston (1993); Burhop (2011a); Born (1967); Ferguson and Temin (2001); James (1984); Kopper (2011); Ritschl and Sarferaz (2010); Schnabel (2004, 2005) or Temin (2008).

As part of his study of Nazi banking policy, Kopper (1995) was the first to examine the politico-economic origins of the German Credit Act of 1934 – the Act, which codified modern banking regulation in Germany.[19] His study presents the political discussions during the Nazi rule, but does not consider prior developments. The work of the legal historian Müller (2003) also focuses on the Credit Act of 1934, but also provides an overview of banking laws throughout German history, including the emergency measures taken during the financial crisis of 1931. However, his work does not provide a political economy analysis of the evolution of banking regulation.

By relying on archival and other primary material,[20] my work sheds new light on the long-term evolution of the regulatory structure in Germany. It shows that prior to the German financial crisis there existed little if any political intention to introduce a formal regulatory regime.[21] When the first regulations were introduced in the immediate aftermath of the German Banking Crisis of 1931, the problems of the decentralized structure of banking regulation in the United States served as a cautionary tale to policymakers within

[18] Mostly they tend to be the works of legal historians such as those of Manâa (2011) or Müller (2003). Büschgen (1982, pp. 368–384) contains a brief overview of the history of banking regulation from the perspective of an economic historian.

[19] In the influential work on the Nazi Economy by Barkai (1988), only few of pages are dedicated to developments in the banking sector.

[20] This includes the reports of two banking commissions as well as internal government documents from the Finance and Economics Ministries, the Chancellery and the Central Bank.

[21] Manâa (2011) argued that in the fields of corporate law and banking regulation the crisis merely served as the catalyst for reform, rather than being their immediate cause. A reform of corporate law was most certainly in the pipeline before the crisis, however this chapter finds little evidence that there was in terms of banking regulation. See also Bähr (2006) for the reform of German corporate law during the 1930s.

the central government not to follow the same route. Also, my research confirms more recent research that argued that the Credit Act of 1934 is not to be considered a Nazi piece of legislation, as it had been traditionally suggested.[22] Indeed, the Act is in line with the German corporatist tradition of regulating the economy. The comparative perspective with the United States also shows that the reason why we do not see a harmonization of the regulatory structures in Germany and the United States, lies primarily in the varying degrees of states rights.

This chapter is structured as follows. First, the regulatory discussion in the United States is presented up until the Second World War. Emphasis lies on discussions surrounding the centralization of the regulatory strucutre. This is followed by an equivalent section on the German regulatory deliberations. The final section discusses the findings of this double biography.

2.2 The United States

2.2.1 Early banking regulation (pre-1860)

The first banking services in the United States were carried out by private individuals or unincorporated associations often known as 'private bankers'.[23] With the American War of Independence (1775–1783) the first incorporated banking businesses were formed. Generally these required charters from the state governments to operate a banking business and were generally known as 'state banks'. In most cases the state charters were granted on a case-by-case basis.[24] Individual proprietorships or partnerships continued to operate throughout this period. Yet, after 1813, most states prohibited (unincorporated) private bankers from issuing their own banknotes. Only (incorporated) state banks with the appropriate charter were allowed to issue banknotes.[25] Thus, the term 'private banks'

[22] For the traditional view see Bähre (1982, p. 25) or Wandel (1982a, pp. 153–154).

[23] For a brief history of money and banking prior to the American War of Independence see Markham (2002, pp. 43–57).

[24] Not all incorporated banks were 'state banks', but the line between mutual savings companies, stock savings banks and trust companies vis-a-vis 'state banks' was often blurred. See Barnett (1911, pp. 9–11) for a detailed exposition of the term.

[25] These bank notes were (in theory) convertible into gold specie upon demand.

was generally used for unincorporated individuals or associations that operated a banking business without issuing notes.[26]

When chartering state banks, the states often maintained a right to sign part of the capital of newly formed banking corporations, and in some cases they even outright owned state banks. For a number of state governments, banks were an important source of income as well as a tool to support politically desirable projects. For frontier states in the South and West it was often also a way of promoting professional banking structures.[27] The charters hardly ever effectively restricted state banks' scope of operations. Only towards the middle of the century, after the panic of 1837[28] and the subsequent depression, did bank charters become more restrictive and their issue more homogeneous *within* states – but not across states. Many states began granting charters according to the 'free-banking' principle: anyone was given a charter to operate a banking business as long as certain pre-established conditions were met.[29] Other states began restricting incorporated banking altogether or replacing them with government-owned state banks. By 1863, however, most states had begun again to charter incorporated state banks on the free-banking principle.[30] State regulation of state banks was light at best. As a matter of fact, during the first half of the 19th century most banks' accounts were generally kept secret.[31]

Contrary to what often is believed, branching of banks was generally permitted. In some states, especially in newer states to the West and South, it was the predominant mode of operation for incorporated state banks. Before the Civil War, there was no widespread political or economic movement advocating the adoption of unit banking. On the contrary, it is possible that by the mid 19th century, branching was more widespread in the U.S.

[26]See Redlich (1951, pp. 60) for an exposition of early private banking. See Barnett (1911, p. 11) for a definition of the term private bank. While private banks had a period of relative importance in the 19th century, their influence waned in the 20th century until they became virtually insignificant by the late 1930s.

[27]Doti and Schweikart (1991, pp. 19–23) describe the unconventional banking services in the westernmost states. For the government stakes in banks and the states' fiscal interest in banks see Dewey (1910, pp. 33–35) and Legler et al. (1994, pp. 121–122, 126). For the banks as a tool of public policy see Sylla (1999, p. 264).

[28]For the origins of the panic of 1837 see Hammond (1957, pp. 451–457) or Rousseau (2002). For an interesting account of the effect of the panic on banks in the American South see Schweikart (1987, pp. 48–90).

[29]See Chapman and Westerfield (1942, pp. 54–55) and Dewey (1910, pp. 40–46). Robertson (1968, pp. 22–23) attributes the emergence of the free-banking laws to the sheer quantity of chartering requests the states received at that time. Also note that free-banking in the U.S. is not equivalent to a complete laissez-faire approach to banking. It merely meant that legislatures did not approve every single bank charter anymore, and that anyone could set-up a note-issuing bank as long as certain conditions were met.

[30]See Hammond (1957, pp. 605–617).

[31]See Dewey (1910, pp. 5–22, 126–127, 142–151), Hammond (1957, pp. 452) and Markham (2002, pp. 170–173).

than in any other European country, except Scotland.[32] Merely in a few north-eastern states, such as New York, was branching eventually restricted before the Civil War.[33] There was, however, a resentment towards corporate banking institutions per se. It was this resentment that even caused some states to prohibit incorporated banking altogether for some time.[34]

The only banks to have federal charters prior to 1863 were the First (1791–1811) and Second Bank (1815–1835) of the United States.[35] These were early attempts at establishing a public-private 'central bank'. The intention was to install a banking institution, modelled on the Bank of England, that made it easier for the U.S. federal government to attend to its fiscal needs. It directly engaged in business with private banks, but it also served as the federal government's fiscal agent. At the same time, its dominant position helped to unify the currency of the United States and it served as a regulating force on other state banks, much like the role the Bank of England had in the England. While other state banks were still allowed to issue banknotes, only the notes of the Bank of the United States were considered legal tender in payments to the US government. Even though both the First and the Second Bank of the United States were successful in their endeavours, they did not have their charters renewed by Congress. Both the First and Second Bank of the United States fell prey to political attacks. In particular the agrarian interests, represented by the Presidents Jefferson and Jackson, were in opposition to any corporation issuing paper money, but especially so to the two (allegedly monopolistic) federal banking corporations. In their attacks on the banks the Agrarians questioned the constitutionality of the banks,

[32] Chapman and Westerfield (1942, p. 48) quoting Melchior Palyi, *The Chicago Credit Market*, p. 144, Chicago: University of Chicago Press, 1937. See also the total number of banks and branches in operation in the United States, 1834–1861 in table 2 in Chapman and Westerfield (1942, p. 48).

[33] Possibly this was due to a provision contained in the free-banking acts that prevented a bank's branches from emitting notes. It was a measure that was meant to prevent an excessive emission of notes by banks. At the same time it made the operation of branches unattractive for state banks. See Board of Governors of the Federal Reserve System (1937a, p. 19).

[34] The resentment largely reflected the unreliable currency and the novel corporate way of organizing production. It is not quite clear what prompted some north-eastern states in the ante-bellum period to restrict branching at times. In part it was due to the fiscal interest of towns and states that expected a higher income from local monopolies on banking. And to some extent the lack of branches might also have been a factor of local economic conditions. In the case of Maryland, branching did not evolve, even though banks were free to establish them. See Chapman and Westerfield (1942, pp. 36–49), Hammond (1957, pp. 605–617) and Dewey (1910, pp. 136–143).

[35] The earlier Bank of North America was chartered by the Continental Congress during the Civil war in 1781. It was to serve as a 'national bank' to finance the war and to unify the currency, by issuing paper money based on specie. It had also received a charter from the state of Pennsylvania and continued operations as a state bank after the war. In 1786, it also received a charter from the state of Delaware and in 1787 a new limited charter from Congress. The Bank of North America was later succeeded as a 'national bank' by the First Bank of the United States. See Markham (2002, pp. 71–72, 87–88) and Redlich (1947, pp. 7–8, 20–21) for details on the Bank of North America.

the banks' adherence to their charter, and, last but not least, that they had tried to influence politics. Crucially, the Agrarians' cause was aided by state banks that saw it as an opportunity to dispose of the competition and the regulatory influences from the First and Second Bank of the United States.[36]

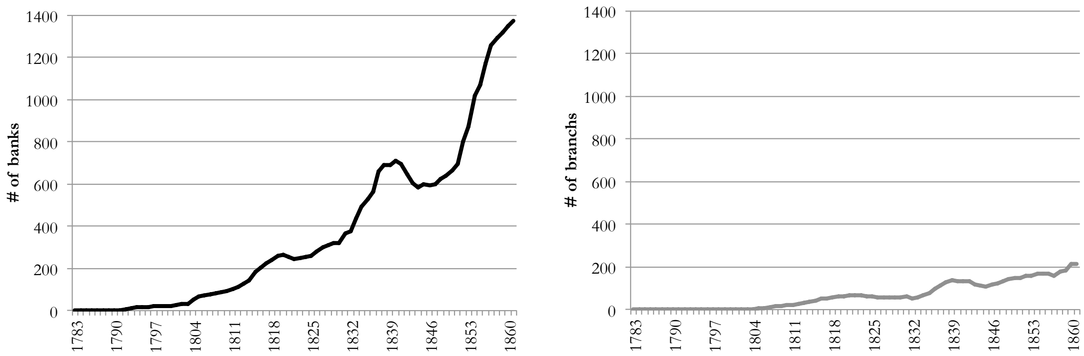
The First and Second Bank of the United States had been successful in furnishing a more uniform national currency and conservative banking practices. After their demise, the United States reverted back to a system with no currency of nation-wide acceptance. Throughout the early 19th century, the number of state banks grew rapidly.[37] And every state bank could (and did) emit their own currency. Hundreds of parallel currencies existed alongside each other, amounting to over 10,000 different kind of banknotes in circulation. Many of the currencies were not convertible 1:1 to each other, and even less so across state boundaries. This made interregional trade more complex with respect to countries with a unified currency. Convertibility of banks' currencies was further hindered by low capital ratios, mismanagement and speculative loans. By the time the Civil War broke out in 1861, banks were relatively unsafe, uncertainty was widespread and the federal government had no control over state banks. Only a handful of states succeeded in building relatively sound banking systems.[38]

[36]See Hildreth (1837, pp. 51–56, 61–63 & 79–88), Holdsworth and Dewey (1910, pp. 9, 12–14, 50–51, 66–71, 83–97, 151–152, 163–175, 254–265) and Markham (2002, pp. 88–90, 126–127, 133–136, 142–147). See Redlich (1947, pp. 96–101) for details on the regulating influence of these 'central banks' on other state banks. See Hammond (1957, 1947, pp. 209–226) for the state bankers' role.

[37]Redlich points out that two particularly strong growth bursts came after the demise of the First and the Second Bank of the United States. Businessmen tried to fill the void these dominating institutions had left. See Redlich (1947, pp. 187) and Redlich (1951, 69–80). For an overview of the growth of incorporated banks see figure 2.1 on page 26.

[38]See Chapman and Westerfield (1942, pp. 49–51), Davis (1910, pp. 12–13, 17–27), Markham (2002, pp. 168–169, 173, 175–180) and West (1977, p. 16). The banking system from the "Wildcat" era (1836 to 1863) was described in the classic Hutchinson (1975, p. 60) textbook on US banking as follows: *"The nation's monetary 'system' was clearly a chaotic, deplorable shambles when the Civil War broke out. Indeed, it is something of a misnomer to call it system at all."* Robertson (1968, p. 31) is sceptical of overly negative assessments. He points out that even though the banking system had many shortcomings, it still enabled rapid economic growth. See Rockoff (1974, 163) for another benign evaluation of the initial free banking era. Gische (1979, p. 25) claims that bank notes from New York banks were generally accepted throughout the country at par, given the stringency of New York state regulations for banks. Data by Jaremski (2010a, pp. 1571, 1582) on state bank failures suggests, that while the decade from 1844–1855 had relatively few failures, they were especially prominent from 1837–1843 and from 1855 until the Civil War. He attributes many failures to the backing of note issues by state bonds, thus every time state bond prices collapsed, so did the banks that had backed their note issue on those state bonds.

FIGURE 2.1: **The number of incorporated banks and bank branches in the United States (1783–1861)**



(a) The number of incorporated banks

(b) The number of bank branches

Sources: Own elaboration based on data from Weber (2006, pp. 449–450). These figures do not include (non-incorporated) private banks.

2.2.2 Introduction of the National Banking System (1860-1905)

Ideas on how to reform the banking sector had abounded in the decades before the American Civil War (1861-1865). A number of these came to fruition in the free banking laws of several states, after the demise of the Second Bank of the United States and the subsequent Panic of 1837. Two other important ideas spawned prior to the Civil War. One was to introduce the free-banking principle on a national scale. The other idea suggested circumventing opposition to a single national bank issuing a national currency by allowing a number of state banks to issue a national currency subject to certain conditions. At first, these proposals did not make much headway. Only towards the 1850 did these ideas gain more prominence.[39]

The American Civil War provided the needed catalyst for reform, not least because the agrarian South of the United States had seceded, and with it the primary opposition to federal government involvement in the banking sector.[40] In his Treasury Report to Congress of December 1861, Treasury Secretary Chase proposed to Congress to pass an Act that would create a unified currency by permitting, or if necessary forcing, existing state banks to issue a national currency based on government bonds and subject to certain

[39] See Davis (1910, pp. 9–12) and Redlich (1951, pp. 99–100) for the various proposals prior to the Civil War.

[40] The Southern states were generally opposed to greater federal government involvement in the economy, besides for matters of war. See Sargent (2012, p. 23) referring to Section III, Chapter 14 of McPherson, James, Battle Cry of Freedom, Oxford University Press, 1988.

regulations.[41] This would finally provide the country with a unified currency again, and it would possibly create a stronger demand for government war bonds. This, in turn, would tie the banks, and thus the country, closer together with the federal government and create a greater economic interest in a victory of the Union. Congress picked up Treasury Secretary Chase's proposal, but modified it substantially in the Currency Act of February 25, 1863. The idea of allowing state banks to issue a national currency was pushed into second tier and eventually discarded completely. Instead, Congress focused on allowing the federal government to charter 'national-banks' throughout the country according to the free-banking principle. Only these national banks would be allowed to issue a national currency. In return, the national banks were required to subject to stringent regulation and supervision by the federal government's Office of the Comptroller of the Currency (OCC). The Currency Act had little impact. Only a handful of national banks were founded in the western regions of the country.[42]

It was quickly realized that the Act had several flaws that made it economically unattractive to either set-up a new national bank or for state banks to convert into national banks.[43] For example, the Act of 1863 lacked a provision that obliged national banks to redeem other national banks' notes at par. Another was that State Banks had to change their name into the format "[First/Second/...] National Bank of [Name of City]". Additionally, some bankers felt that times of war were not an opportune moment to engage in monetary experiments, and it was a certainty that most bankers disliked the federal governments attempt to extend its influence on the banking sector. It was also not certain that the government would survive the war and national banks' survival was intricately linked with the solvency of the government.[44] Furthermore, it was also suggested that the 1863 Act threatened New York's standing as the financial center of the country and thus found no acceptance by the influential New York Banks.[45] Many state legislatures also refused to pass enabling acts that would have allowed banks to convert into national banks more easily. In short, the political and economic incentives were not strong enough

[41] Davis (1910, p. 7) reports that such a system had already been successfully implemented on a state level in New York in 1838. Indeed, much of the legislators inspiration came from banking 'experiments' previously conducted in New York. See also Gische (1979, pp. 25–26, 35) and West (1977, pp. 21–22). Redlich (1951, p. 105) also sees parallels with the English Bank Act of 1844, also known as the Peel Act.

[42] See Davis (1910, pp. 1–93), Hammond (1957, pp. 718–727), and Redlich (1951, pp. 99–108).

[43] See U.S. Department of the Treasury (1863) for the numerous suggestions for improvement.

[44] Indeed, after the American Civil War most state banks in the American south, who were heavily invested in confederate securities, failed as confederate securities became worthless. See Doti and Schweikart (1991, p. 24) and Schweikart (1987, pp. 311–313).

[45] See Gische (1979, p.42–43).

to convince state banks to exchange their charter into a national one. Indeed, the early national banks seem to have been set-up more in a spirit of patriotism rather than entrepreneurship. The National Currency Act of June 3, 1864 mended some of the defects of the previous one, but also introduced a few other detrimental provisions.[46] While national banks were obliged to redeem notes from other national banks at par, capital requirements for national banks were increased and national banks were forbidden from extending real estate loans. As a consequence, growth of national banks was still lower than hoped. The U.S. Congress realized that it had to find a way to make the operation of a national bank more lucrative than that of a state bank. It eventually did so when, in an amendment to the National Currency Act in 1865, Congress levied a tax of 10% on the note issue of state banks. From then on it was no longer profitable for them to issue bank notes. As note issue was an important source of income for many state banks, a wave of conversions into national banks ensued.[47] The first National Currency Act of 1863 and the tax levy of 1865 passed Congress only with the narrowest of majorities. This indicates that legislators were well aware that their measures amounted to a massive infraction into states' rights that could have devastating effects on state banking.[48]

The more recent historical literature has generally interpreted the establishment of the national banking system as an attempt by Congress to raise money for the ongoing Civil War, whereas the older historiography has generally pointed out that it was primarily and attempt to unify the currency and to establish a unified regulatory system. The main argument put forward in favor of the war finance hypothesis was that contemporary policymakers cited it as a motive for backing of the currency with government bonds.[49]

[46] Only later was the 1864 National Currency Act officially renamed into 'National Bank Act'.

[47] See Davis (1910, pp. 94–202), Hammond (1957, pp. 727–739), and Redlich (1951, pp. 108–113). Gische (1979, p. 59) argues that the balance had already tipped in favor of the national banking system before the introduction of the tax, when a number of reputable large New York state banks decided to exchange their charters in the winter of 1864. This broke the opposition of the New York Clearing House association and created nation-wide trust in the system's viability.

[48] See Chapman and Westerfield (1942, p. 61) and Robertson (1968, pp. 43–45, 49, 53–54). For a schematic overview of the regulatory arrangement from 1863 onwards see figure 2.2 on page 31.

[49] War finance is cited as the primary motive for the introduction of the national banking system in Haber (2007, pp. 31–32), Golembe (1967, pp. 1096–1097), Schweikart (1987, p. 311), Sylla (1969, p. 659), Sylla (1999, p. 267), Wall et al. (2011, p. 4) and White (1983, p. 11). Chapman and Westerfield (1942) see the war finance motive at par with the motive to unify the currency. West (1977, p. 18) is agnostic as to the motives. Hammond (1957, pp. 718–738), Million (1894), Redlich (1951) and especially Davis (1910) represent the traditional view that war finance was not a major driver behind this legislation, but that the unification of the currency and the regulatory regime was. It is possible that the more modern literature, which provides relatively little evidence for this claim, was mislead by the influential account of Robertson (1968, pp. 36–54–183). In the main body of his text, he repeatedly stresses that at the time of the inception of the national banking system, the war finance motive was often put forward. He even stated that the tax on the bills was intended to boost the national banking system, rather than to replace

However, there is significant evidence that besides hoping to unify the currency, the introduction of the national banking system was indeed a Congressional attempt to unify regulation by driving the state banking system out of existence. First, if Congress was primarily interested in raising money for the ongoing war effort, there would have been no need to introduce the national banking system. Congress could simply have worked on the basis of the original proposal of Treasury Secretary Chase that foresaw the unification of the currency on the basis of state banks issuing a national currency backed by government bonds. Second, influential policymakers publicly proclaimed that an important aim of the National Currency Act was to absorb the entire state banking system in the national banking system and thus centralizing control over the banking system.[50] And third, if Congress was serious about using the National Currency Act as a major source of income, then it would probably not been enacted as slow as it did. After all, time is of the essence in times of war. Between the first proposal of Treasury Secretary Chase in December of 1861 and the enactment of the first National Currency Act lay well over a year. Indeed, the bill was even temporarily put on hold and greenbacks were issued instead.[51] By the time the revised National Currency Act was passed, almost another year had gone by. During this year, the support to war finance of the first National Currency Act was negligible.[52] And only after the taxation of state banks' note issue took effect in 1865,

the state banking system. Yet, in the conclusion of the book he reverses his prior position and clearly states that *"Congress unquestionably intended that all commercial banks should be chartered by the federal government."*

[50] *"[...] only one system will prevail; it requires no spirit of prophecy to predict which of the two is destined to give way. The losses which the people have sustained by bank failures; the inadequate protection which state legislation, with rare exception, has given to the bill-holders; the fact that the credit of issues of the strongest and best conducted State banks, outside of the States or the section where they exist, is not the result of public confidence in their solvency, but of the influence of bankers and money dealers, who can as easily depress that credit as they can sustain it."* See the Circular Letter of the Treasury Department, Office of the Comptroller of the Currency, Washington, July 14, 1863, reprinted as Appendix II in Redlich (1951, pp. 137–139). See also the furious reaction of the New York Clearing House Association to the Controller's statement reprinted as Appendix III in Redlich (1951, pp. 140–143). It accused the government to *"[...] unnecessarily throwing a firebrand into the state, raising the question of state rights."* and concluded that *"[...] the evil is upon us"*. Similar to the Comptroller, the influential Senator Sherman proclaimed that *"The national banks were intended to supersede the State banks. They cannot exist together; [...] If the State banks have power enough in Congress to prolong their existence beyond the present year, we had better suspend the organization of national banks"*, quoted in Board of Governors of the Federal Reserve System (1932d, p. 3) citing the Congressional Globe, 38th Congress, 2nd Session, February 27, 1865, p. 1139. In Sherman (1895, Chapter XIII), Senator Sherman's autobiography, an entire chapter is dedicated to the "Abolishment of the State Banks". Robertson (1968, p. 183) also points out that the national banking system and the prohibitive tax were introduced against the unanimous opposition of the banks.

[51] See Robertson (1968, pp. 40–41).

[52] By October of 1864, just about \$82 million of government bonds were used by national banks to back their note issue. The total note issue itself was limited to \$300 million in the National Currency Act. Additionally, to my knowledge, there exist no estimates of what proportion of this amount actually represents additional demand bought by the banks to back the currency, rather than bonds they already had held previously. For the figure see U.S. Department of the Treasury (1864, p. 47).

did the national banking system take off – well after the war had been decided. Even if it had taken off in time, the size of the budget deficits incurred dwarfed any prospect of obtaining a significant source of income from the introduction of the bond-backed national currency.[53]

While it is of course tempting to infer that the primary reason for imposing the backing in government bonds of the national currency was just a measure to increase the demand of government bonds, it is just as plausible to assume that at that time it was a necessary condition to ensure that the national currency was trusted and accepted across the vast country. These government notes were issued by numerous banks. If one of those banks failed, it would still be possible to redeem the note that bank had issued with the US treasury. It was a measure that put the federal government's weight behind the currency. Additionally, it allowed the government to control the (paper) money supply, without which the idea of a decentralized national currency would have been much harder to realize.[54] There are many plausible arguments for the establishment of the national banking system, but the evidence for the national banking system having been primarily a measure to finance the war is weak. The war finance motive served mainly as a patriotic sweetener to the public.[55]

If the intention of the government was indeed to unify the currency and to replace the state bank system with a centrally regulated national bank system, why did Congress not simply issue a law prohibiting states from chartering banks or require all state banks to subject themselves to central regulation? The barrier to such action was the American constitution, which did not explicitly grant Congress such power. Congress could not prevent states from chartering banks and neither could it regulate state banks directly unless it was needed for currency matters.[56] Consequently it had to create incentives, such

[53]See Davis (1910, pp. 40–42) and Goldin and Lewis (1975, pp. 303–306) for a brief exposition of the union government budget during the war. The budget deficits for 1862 and 1863 were well over $400.000.000 and $600.000.000, respectively, whereas the National Currency Act limited the bond-backed currency to just $300.000.000.

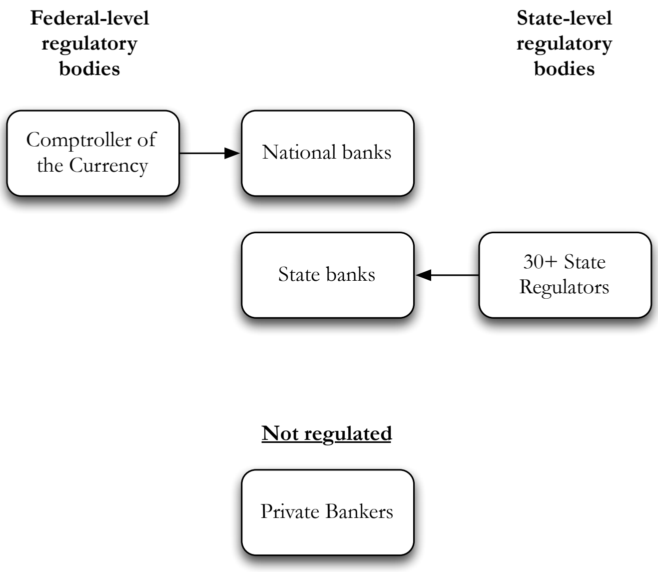
[54]The stabilizing aspect was also expressed by Treasury Secretary Chase and the Comptroller of the Currency. See Redlich (1951, p. 104–105), U.S. Department of the Treasury (1863, p. 58) and U.S. Department of the Treasury (1864, p. 48).

[55]Davis (1910, p. 107–111) reports that war finance arguments were indeed sometimes put forward by contemporary legislators, but that they were primarily aimed at the public.

[56]For an analysis of the constitutional powers of the states and Congress in terms of banking see Hammond (1957, pp. 91–95). This federal conflict in the banking sector regularly causes vigorous disputes. See for example the current debate on federal preemption in the banking sector and its purported role in allowing abusive mortgage practices as discussed in Natter and Wechsler (2012). Note that this particular discussion only considers to what extent state regulations apply to national banks if there is no corresponding federal law, but not the other way around.

that state banks would voluntarily subject themselves to federal regulation by converting their charters into national ones. Congress hoped that the national currency emitting privileges a national bank charter offered, paired with the tax on note emission by state banks would suffice.

FIGURE 2.2: **Schematic overview of the regulatory arrangement in the United States (1863–1912)**



Note that Private Bankers were barred from issuing currency. *Source: Own elaboration.*

And indeed, in 1865 it seemed like the plan would succeed and that the national banking system would replace the state banking system. Large swathes of state banks converted into national banks, subjecting themselves to the federal regulations of the Office of the Comptroller of the Currency. Numerous new national banks were also founded, whereas some state banks closed down altogether. However, growth of the national banking system soon stagnated and the state banking system staged a comeback.[57] This was primarily due to three factors. First, between 1863 and 1870 note issue was limited to $300 million and this limit was already hit by 1867. As a consequence, few new national banks formed until 1870. By the time Congress reacted and abolished the limit, government bond prices had risen sharply and the profitability of national banks' note issue consequently decreased. Second, over time the cashless transfer of money began to spread rapidly. This greatly reduced the need for banks to be able to issue currency as their main source of

[57] See figure 2.3 on page 34 for a rough overview of the evolution of the national and state banking systems in the 19th century.

income. And third, the regulatory institutions of the states did not remain idle to watch their own demise.[58]

National bank regulation tended to be stricter than that of state banks. They had to adhere to stricter capital and reserve requirements. Especially, in more rural areas it often was not economically viable to set up a national bank with the minimum capital requirements specified by the National Bank Act. In addition, national banks were restricted in their portfolio choices as they were required to invest in short-term, self-liquidating loans, which effectively restricted them from engaging in the real estate and securities business. National Bank shareholders were also subject to double liability. In case a national bank had to be shut down, investors not only lost their initial investment, but they were also liable for additional losses up to the par value of their stocks. Last but not least, national banks were not allowed to operate branches.[59] In contrast to that, the regulation of state banks was often aligned with the fiscal interests of the states, rather than being determined by safety concerns.[60] Consequently, state bank regulators reacted to the competition by the national banking system by lowering regulatory requirements. Free banking was introduced in most of the states, permitting anyone to establish a banking corporation, as long as certain conditions were met. Technically, these banks were even allowed to emit their own bank notes, but this was no longer economically attractive given the 10% tax incurred upon their issue. Investment restrictions as well as capital and reserve requirements were lowered well beyond the levels required from national banks. Yet, branching restrictions were largely untouched until the 1900s.[61] The Comptroller of the Currency tried to counteract the resurgence of state banks by lowering regulatory requirements for national banks as well. However, these measures were met by the states with even lower

[58] See Board of Governors of the Federal Reserve System (1932d, p. 4), Hammond (1957, p. 734), Sylla (1969, pp. 659–663) and White (1983, pp. 61–62).

[59] See Board of Governors of the Federal Reserve System (1932d, pp. 7–11), Doti and Schweikart (1991, p. 23–25), Macey and Miller (1992, pp. 2, 36), Redlich (1951, pp. 178–179), Sylla (1969, pp. 559–661) and White (1983, pp. 18–21, 33–35). The national currency acts of 1863 and 1864 did not explicitly prohibit the branching of national banks, but the Comptroller of the Currency interpreted the Act narrowly and refused to authorize the operation of new branches to national banks . Merely banks that had branches and joined the national banking system were allowed to retain these. Remarkably, the branching prohibition found little resistance. Until 1890 there was no political movement to allow for the branching of national banks. See Chapman and Westerfield (1942, pp. 59–60). For an overview of the different regulatory requirements of national and state banks in 1895 and 1909 see (White, 1983, pp. 18–21, 30–31).

[60] See Board of Governors of the Federal Reserve System (1932d, pp. 10–11). Banks often sought methods to stabilize their industry through voluntary local arrangements such as clearinghouse associations. Only towards the end of the 19th century did supervision of state and national regulators become more professional. See Doti and Schweikart (1991, pp. 53–54). For an overview of regulatory practice and method of state banks see Barnett (1911, pp. 144–181).

[61] See White (1982, pp. 34–35).

regulatory limits for state banks. This competition between regulators, allowed banks to engage in regulatory arbitrage – to switch charters depending on which system offered the most suitable scheme.[62]

The national banking system had created a pyramidal scheme of reserve holdings, where required reserves depended on a bank's geographical location. Rural national banks could hold part of their required reserves as deposits with national banks in reserve cities. These banks could in turn hold part of their required reserves as deposits with national banks in central reserve cities.[63] Thus, any sudden changes at the bottom of the pyramid would reverberate in the central reserve city banks. The advantage of holding deposits with other banks was that it paid interest, whereas holding reserves as cash did not. The New York banks, which were the ultimate reserve holders for the national bank system, invested these short term reserves in call loan market that financed margin finance on the stock market. Whenever rural banks would recall their reserves, the New York banks could, in normal times, call in the loan, which could be readily repaid by selling the corresponding securities.[64]

The American Civil War and the initial success of the national banking system had also – unintentionally – wiped out branch banking in much of the United States. The Comptroller of the Currency did not permit national banks to branch, and new state banks were often small and did not develop branches.[65]

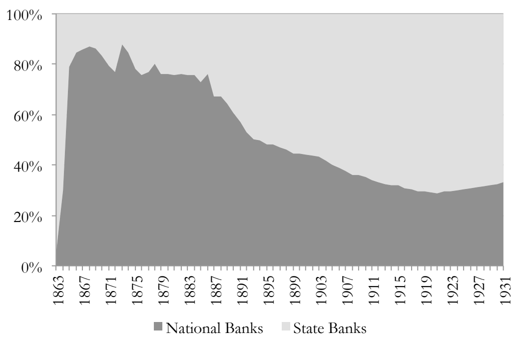
[62]See Board of Governors of the Federal Reserve System (1932d, pp. 11–15), Sylla (1969, p. 664), and White (1983, p. 14–61).

[63]The central reserve cities were New York, Chicago and St. Louis.

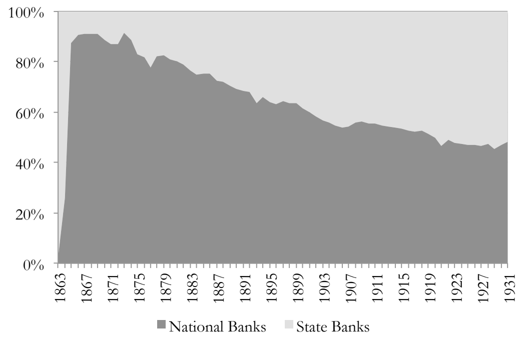
[64]See Sprague (1910, p. 20–24, 83) and Wilson et al. (1990, pp. 88–89), West (1977, pp. 29–32) and White (1983, pp. 27–33). As Laughlin (1912, p. 47) figures show, the pyramidal reserve structure of the national banking system contributed to skewing the capital towards the Eastern States. In general interest rates were significantly higher for more central areas of the United States compared to coastal regions. Jaremski (2010b, p. 14) also finds that a redistribution of capital from rural to urban centers took place, not only because of the reserve scheme, but also because of the high capital requirements of national banks that, paired with the tax on note issue, caused many small state banks to close down. Robertson (1968, p. 51) traces the origins of this reserve scheme to similar correspondence reserve holding schemes that had been the norm in several state banking systems and were consequently copied into the national banking system. Gische (1979, pp. 47, 54) argues that the adoption of this structure was a concession to the New York city banks that preserved New Yorks status as center of American finance.

[65]There is not much known as to why the Comptroller of the Currency restricted branching of national banks as tightly as it did. There was no general movement towards restricting branch banking even after the Civil War, but neither was there a movement advocating the permission of branch banking until the 1890s. Modern explanations why unit banking was widespread in the United States are rather limited. The prohibition of branching of national banks is often interpreted as a historical accident, that was of little relevance to banks and policymakers at the time. Once it became a relevant issue in terms of financial sector stability, supporters of the existing system, i.e. unit bankers and anti-trust advocates fought those attempting to liberalize the system. See Calomiris (2006c, p. 47), Chapman and Westerfield (1942, pp. 59–65) and White (1983, pp. 14—16). A study of the Board of Governors of the Federal Reserve System (1937a, p. 21) suggests that the national banking system might have been regarded by the first Comptroller

FIGURE 2.3: **The evolution of the national and state banking systems compared by the number of banks (a), and by the amount of assets held (b)**



(a) As a proportion of the total number of national and state banks



(b) As a proportion of the total assets of both national and state banks

Sources: Own elaboration based on data from U.S. Department of the Treasury (1932, pp. 3, 5). The figures do not include private banks.

The regulatory race to the bottom consequently cemented a banking system, which was highly fragmented with numerous small and mainly rural banks, with the exception of a few large banks based in New York. Instead of developing a unified banking system with the federal government as the sole regulator, as most countries did, the United States developed a dual banking system that was separated into national and state banks.[66] The cyclical nature of the predominantly agricultural economy, paired with the pyramidal reserve system, led to recurring tightness in the New York money money markets. Crucially, there was no standing mechanism to counter these liquidity shortages, such as a

of the Currency, McCulloch, as indeed a banking system with branches. After all, the structure of the national banking system was similar to that of the Bank of Indiana that had been presided by McCulloch himself. Other less convincing explanations often highlight Americans' general suspicion or even hostility towards concentrations of economic and financial power. See for example Barnett (1911, p. 135–143). These explanations fail to explain the relative ease with which branching was accepted prior to the Civil War and why quite a number of states allowed bank branching after all or did not explicitly prohibit bank branching in the post-bellum period. It has also been argued retroactively that the aim of the National Banking Act was to create *"[...]local institutions that were independent of each other, but under national control and supervision. Nationalization without centralization was the keynote of the law."*. See Board of Governors of the Federal Reserve System (1932b, p. 18), quoting the Solicitor General of the United States in 1911 and citing the Commercial and Financial Chronicle, November 4, 1911, p. 1232; November 25, 1911, p. 1433 and United States Congress, 72nd, 1st Session, Senate Document No. 92, May 10, 1932, p. 3. It would also plausible to speculate that the branching restriction on national banks was a necessity, because of the pyramidal reserve structure. Central reserve city banks naturally benefitted from the reserves of all national banks being effectively deposited with them. If the central reserve city banks were allowed to branch, they would easily outcompete other smaller national banks. Thus the need to restrict the geographic spread of the 'privileged' central reserve city banks. For an overview of the legal status of branching throughout the U.S. States in 1901 see Chapman and Westerfield (1942, pp. 76–77).

[66]Indeed, it might would be more appropriate to speak of a triple banking system, as unincorporated private banks still existed. However, we shall keep with the terminology of the dual banking system as information on private banks is relatively scarce and their relative share declined over time. See figure 2.6(c) on page 42.

central bank.[67] This, paired with the lacking risk diversification of the unit banks, made the banking system highly vulnerable to monetary shocks.[68] Consequently, the banking system was plagued by numerous banking crises.[69]

2.2.3 Introduction of the Federal Reserve System (1906-1917)

Even though there were periodical banking crises, proposals to reform the banking system were relatively scarce after the introduction of the national banking system.[70] Reform proposals intensified towards the end of the 19th century, as a number of weaknesses in the banking system were pointed out. Some argued for the liberalization of branching, others for the introduction of a central bank and a currency based on assets rather than government bonds, but the various proposals did not yield any significant legislative results.[71] The only changes to the national banking system were changes that relaxed regulations for national banks to put them on a slightly more equal competitive footing as the state banks.[72] The reform discussion never really took center-stage until the liquidity crisis of 1906/07.[73]

[67] Banks in reserve or central reserve cities often set up clearinghouse associations to counter this problem. See Redlich (1951, p. 175).

[68] See Kemmerer (1910), Miron (1986, pp. 138–139), Sprague (1910, p. 48) and more recently Hanes and Rhode (2012, p. 35). This traditional interpretation that monetary shocks largely originated in the cyclical agricultural has been challenged by Calomiris (2006a, p. 140) and Wilson et al. (1990, pp. 89–101). They point out that the stock market crashes of 1929 and 1987 occurred even though there was access to a lender of last resort. As an alternative explanation they propose that the crises in the late 19th century were primarily driven by the public's lack of confidence in the stability of the banking sector, and the public withdrew their deposits en masse in anticipation of a recession. See also Wicker (2000).

[69] In the US there were three major banking crises in 1873, 1893 and 1907 and seven minor ones in 1884, 1890, 1896, 1899, 1901, 1903 and 1905 according to a modern reclassification by Jalil (2012). See Sprague (1910) for a contemporary account of some of these crises. Bordo (1985) compared the stability of the Banking Systems in the U.S. with that of the U.K., Germany, France, Canada and Sweden. He finds that the American banking system was much more crisis prone than any of its other major counterparts.

[70] West (1977, pp. 35–41) attributes this to the rather benign course of the crises and that contemporaries believed that the underlying structure of a competitive banking system was desirable and functional. Instead, individual banking practices were to blame. The prohibition of interest payments on reserve deposits was the first major proposal voiced after the crisis of 1873. Although it was generally welcomed, it failed to materialize. See also Sprague (1910, pp. 89–107).

[71] See Chapman and Westerfield (1942, pp. 64–74), Redlich (1951, pp. 207–217) and West (1977, pp. 42–49) for the reform proposals around the turn of the century, and in particular the Baltimore Plan and the Indianapolis Monetary Commission.

[72] The most important piece of legislation was probably the Gold Standard Act of March 14, 1900, which lowered the capital requirements for national banks in small towns and allowed national banks to issue bank notes at par with the government bonds deposited with the Comptroller (previously they had only been allowed up to 90% of the value of their deposited bonds. Its main effect was the founding of several hundred of new small national banks, but hardly any state banks decided to convert. See Willis (1923, pp. 14–17).

[73] See White (1983, p. 63). Chapman and Westerfield (1942, p. 65) point out that reform of the currency was a much more prominent issue than systemic considerations prior to the liquidity crisis of 1906/07.

The effects of the San Francisco Earthquake of 1906 caused a monetary shock in the international financial system via the gold standard that ultimately lead to a widespread breakdown of the convertibility of deposits throughout most of the United States.[74] In contrast to the previous crises, the financial crisis of 1907 was so severe that it generated enough political momentum to create the potential for a major change to the American banking system.[75] The swift ascent of the financial trusts, which were created to evade existing regulation, and which pursued more risky business models that almost brought the system to a collapse, caused a change of heart. The systemic risk associated with the trusts' business model did not go unobserved amongst 'traditional' bankers. From that perspective it is thus unsurprising that it was especially the relatively strictly regulated national banks, which were calling for increased regulation; regulation that would encompass trusts and create a central institution that would be able to act as a reliable lender of last resort.[76] This is probably the key difference with respect to previous crises. Prior to 1907, the banking industry saw no major reason for concern and largely opposed regulatory reform. After 1907, influential parts of the banking industry actively sought greater government involvement to protect their banks from failing due to the actions of unregulated parts of the system.

The U.S. Congress felt compelled to establish two commissions. The National Monetary Commission (NMC) was tasked with investigating the structure of the banking system and its defects, in particular its lack of a central bank. The Money Trust Inquiry, better known as the 'Pujo commission', was created to investigate the extent to which a few financial institutions exerted an undue influence over other financial and industrial corporations.[77] Especially the NMC became an immense exercise.[78] It prepared reports on the

[74]See Friedman and Schwartz (1963, p. 157) and Sprague (1910, pp. 286–290). The earthquake triggered massive gold inflows to the United States, as European insurers indemnified American claimants. As a consequence of the massive gold-outflows, the major European central banks were compelled to increase interest rates. This increase in the international interest rate level caused a short but severe recession and ultimately a banking crisis in the United States. See Odell and Weidenmier (2004) for the transmission mechanism.

[75]It was considered by contemporary scholars to be the *"[...] most extensive and prolonged breakdown of the country's credit mechanism which has occurred since the establishment of the national banking system"*(Andrew, 1908, p. 497). But as Calomiris (2009, pp. 5, 11-13) points out, the scale of bank failures in the second half of the 19th century and the early 20th century was minor compared to what would follow in the 1920s and 1930s.

[76]See Frydman et al. (2012, pp. 7–15), Moen and Tallman (1992, pp. 612-616, 621), Moen and Tallman (1999, pp. 11,18–20), Moen and Tallman (2000) and Sprague (1910, pp. 319–320) for details on the crisis. For the ascent of the financial trusts, see for example Barnett (1911) and Neal (1971).

[77]The claim of undue influence is exactly the same that has often been made in the case of the largest German Universal banks as well.

[78]Over the course of 1909 and 1912, the commission published around 30 comprehensive reports. See National Monetary Commission (1908-1913).

history and the current state of the American financial system. More interesting still, the NMC also conducted extensive studies of foreign banking systems in an effort to identify and 'import' monetary and regulatory best practices to the United States. About half of the documents published by the NMC are concerned with *foreign* banking systems rather than the domestic one. Representatives from the commission travelled to Canada, England, France, Germany, Italy, Scotland, Sweden and Switzerland to study those countries' banking systems at first hand.[79]

The principal defect as outlined by the NMC and contemporary observers was the lack of leadership and the absence of a *lender of last resort.* At best, the banks were the sum of its parts. At worst, the lack of structure brought the system to the brink of collapse over and over again as responsibility was 'shared' rather than centralized. In times of crisis, banks acted rationally on an individual level (by cutting-down on lending), however, this lead to collective irrationality as money markets froze.[80] While the largest New York banks had to some extent tried to fulfil this role, their actions were limited by the fact that they did not have the legal power to emit notes based on gold or commercial paper. The establishment of a central bank was a necessity to buffer these liquidity spikes.[81]

Surely enough, the *atomization* of the banking system and the lack of diversification which resulted from it, was also recognized as a major problem for systemic stability. And indeed, some states had already proceeded on their own to liberalize branching laws for state banks, most notably California. However, it was deemed politically impossible to remove branching restrictions on a national scale. The American public's and the unit banks' opposition towards concentration of (financial) power was considered to be simply too strong. Thus, this problem was to remain untouched at a federal level.[82]

[79] Other countries that were studied but not visited were Austria-Hungary, Holland, Japan, Mexico and Russia. See National Monetary Commission (1912, p. 4).

[80] Any substantial attempt by depositors to convert their holdings into currency would necessarily have to be satisfied by banks' reserves. And as reserves dwindled, so did the loans extended by banks. In a system with literally thousands of unit banks, this could easily lead to a wide-scale domino effect as did during the late 19th and early 20th century.

[81] See Sprague (1913, pp. 17–18) and Vreeland (1912, pp. 9–10).

[82] *"Much may be said in favor of branch banking from an economic standpoint but our people would never accept it Under branch banking in 20 years a few great banks in a few of our great cities would own the banking system of the country. Our people are satisfied with our system of home-owned banks. We do not desire to change it in that respect."* (Vreeland, 1912, p. 9). Chapman and Westerfield (1942, pp. 74–75) point out that the aversion towards bank branching coincided with the Antitrust movement of the outgoing 19th century that saw the establishment of the Federal Trade Commission and the practise of 'trust-busting'. Abolishing branching restrictions would, in the eyes of antitrust advocates, run counter to the policies they were pursuing. For California's liberalization and an overview of other states' policies towards branching in 1910 see Chapman and Westerfield (1942, pp. 87, 89).

The central bank, which was, eventually, established in the United States was based on the tested principles according to which successful European banking systems operated.[83] However, the specifics of the American nation, its regulatory history and tradition, were taken into account, i.e. it was a political compromise. The Federal Reserve System, as created in 1913-1914, was not a central bank in the traditional sense. There was no central decision-making body. It was more of a loose cooperation of special-purpose banks, which could - to some degree - act as lenders of last resort and conduct open market policies. The loose cooperation could break down just as easily as it would form.[84] Apart from its function as a lender of last resort, the Federal Reserve served as yet another regulatory agency. Its aim was, once more, to centralize banking regulation. Again, the government tried to provide state banks incentives to subject join the Federal Reserve System and to subject themselves to regulation by the Federal Reserve, and thus create a more homogenized regulatory regime. At the same time, Congress also somewhat relaxed national banks' regulations in order to put them on a more equal footing with state banks.[85]

While national banks were required to join the Federal Reserve System and subject to its regulations, state and private banks where given the option to join the system if they subjected themselves to the regulations of the Federal Reserve. Essentially, they were given the choice to exchange access to a lender of last resort for increased federal regulation. Consequently, banks could be separated into one of four categories, depending

[83] First drafts for a 'National Reserve Association' seem to have been strongly influenced by the experiences of the German banking system. See West (1977, pp. 70–71) and Willis (1923, p. 528).

[84] See Willis (1934, p. 101). A critical figure in this process was Representative Carter Glass, who in the 1930s would continue to play a leading role in shaping banking regulation in the United States. See also Glass (1927) and Willis (1923, pp. 3–825) for contemporary policymakers' accounts on the origins of the Federal Reserve Act and see West (1977, pp. 52–172) for a historical account.

[85] This aim becomes evident not only from the Act itself, but also from the Congressional Hearings. E.g. U.S. Congress (1913, pp. 44–46, 156, 817, 838–842, 1976–1981, 2057–2059). See also Federal Reserve Board (1915, p. 145) and White (1983, pp. 126–131). In his analysis of the National Reserve Plan that would form the basis for the Federal Reserve Act, Laughlin (1912, pp. 276–277), a supporter of a centralized regulatory system, reported enthusiastically: *"[...] In fact, it is one of the best features of the National Reserve plan that it would tend to unify the state and national banking systems. With a definite pattern afforded by federal legislation, with which the state banks were willing to comply in order that they might be placed upon terms of equality in competing with national banks, it may be expected that progress toward uniformity in banking legislation throughout the country would be much more rapid than ever before. This uniformity would be exceedingly desirable, since it would take away the possibility of evading legal provisions. [...]"* He, and certainly others, believed that state banks that stayed out of the Federal Reserve System would be stigmatized and driven out of existence. Similarly, Benjamin Strong – the first president of the influential New York Federal Reserve Bank, proclaimed in a speech that *"No reform of the banking methods in this country will be complete and satisfactory until it includes all banks."*, quoted in Chandler (1958, p. 80), citing a speech on May 14, 1915, reported in the Financial Age (May 22, 1915). In 1916, Benjamin Strong even advocated asking Congress to take action to force state banks into the Federal Reserve System – but he never did ask. Throughout his mandate, bringing the state banks into the federal reserve system remained one of his main concerns. See Chandler (1958, pp. 80-82). See also White (2011, p. 2).

on the regulations they were subject to: First, the *national banks*. These were regulated by both the Federal Reserve and the Comptroller of the Currency.[86] Second, *state member banks*. These were regulated by the respective state governments and because of the banks' membership in the Federal Reserve System, they were also subject to regulation by the Federal Reserve. Third, *state non-member banks*. These were merely regulated by the respective state governments. Last but not least, there was still the option for non-incorporated *private banks* to avoid regulation altogether.[87]

This second attempt to bring state banks in a centralized system of regulation was ineffective. Less than one hundred state banks opted to join the system at its outset. In order to make the Federal Reserve System more attractive, a 1917 amendment to the Federal Reserve Act allowed state banks joining the system to retain all their charter and statutory powers.[88] This created far-reaching exceptions from federal regulation for state banks, giving them them an important regulatory advantage vis-a-vis national banks. Nevertheless, while some larger state banks opted to join the system, the vast majority of state banks decided to stay outside. The economic benefits from joining the Federal Reserve System did not outweigh its regulatory costs for most state banks. After all, most of them were small rural banks that had little to no use for the re-discount facility of the Federal Reserve System. If they needed a re-discount facility they could always approach larger correspondent banks. Additionally, many state banks viewed the system as an undesirable attempt by the central government to extend its control over the state banking system.[89] Consequently, the desired centralization of regulation did not come about this time either. Instead, the regulatory system became more complex still as the possibilities for regulatory arbitrage had been increased through the introduction of the Federal Reserve System.[90]

[86] Crucially, the OCC was not abolished, even though this possibility was considered by Congress during the deliberations of the Federal Reserve Act. It was also suggested that the OCC be transferred from the jurisdiction of the Treasury to that of the Federal Reserve Board. See for example Harding (1925, p. 6).

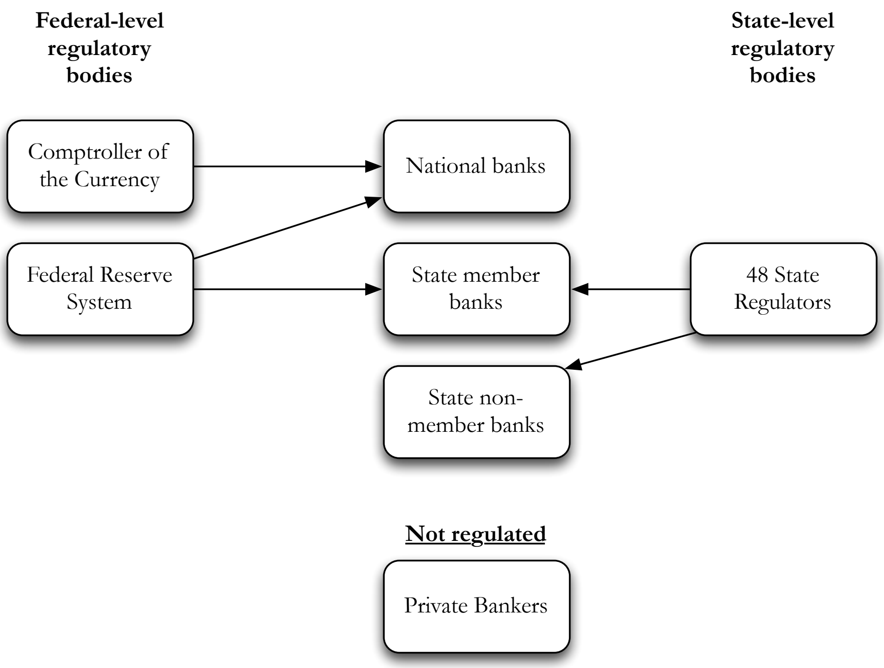
[87] For a schematic overview of the regulatory arrangement in the United States from 1917–1931 see figure 2.4 on page 40.

[88] See Board of Governors of the Federal Reserve System (1932d, p. 25–26, 29) and Wyatt (1932, pp. 239–240).

[89] See Board of Governors of the Federal Reserve System (1915, pp. 178–179) and White (1983, pp. 132–136). Willis (1923, pp. 1185–1187) attributes the temporary increase in state bank membership after 1917 due to state banks hoping to be shielded from financial turmoil caused by the war, which the United States had just joined.

[90] For the evolution of the state and national banking system throughout this period see figure 2.5 on page 42. For the proportion of banks members in the Federal Reserve System see figure 2.6 on page 44. Indeed, White (2011, pp. 2-3, 38–40) argues that the introduction of the Fed as another regulator caused a deterioration in the quality of banking regulation and supervision, as it further spurred the laxity in competition.

FIGURE 2.4: **Schematic overview of the regulatory arrangement in the United States (1917–1932)**



Source: Own elaboration.

The much lesser known Pujo commission was investigating the concentration of financial power, in particular several well-known Wall Street bankers and their practices. In its final report, it called for the strict separation of investment and deposit banking and the prohibition of national banks to exert any direct influence on each other, be it through cross-shareholdings, interlocking directorates or common owners.[91] These suggestions were largely discarded by Congress. The most prominent bankers had withdrawn from influential business positions, in order to pacify the public and the legislators. Merely the prohibition of interlocking directorates found its way into the Clayton Antitrust Act. Even so, the Pujo commission is sometimes credited with providing a powerful counterbalance to the conservative congressional forces that sought to maintain the status quo.[92]

2.2.4 The regulatory discussion in the 1920s (1918–1929)

As the United States moved further away from being an agrarian state towards one based on industry and services, it experienced a short but intense period of economic growth.[93]

[91]See House of Representatives (1913, pp 161–164).
[92]See Simon (1998, pp. 1082-1083) and Willis (1923, pp. 105–115).
[93]See Friedman and Schwartz (1963, pp. 240, 244-245).

At the same time, however, the United States was experiencing a wave of bank failures on an unprecedented scale. Between 1921 and 1929 well over 5000 banks failed. Interestingly, this massive failure wave went about without full-fledged banking crises. These failures could be traced back to a boom and bust in the agricultural sector and the still fragile atomistic structure of the banking sector.[94] The policymakers were well aware of this problem. Also, the question on how to increase state bank membership in the Federal Reserve System had remained firmly on Congress' agenda.[95] Repeated calls were also made for the abolition of the Office of the Comptroller of the Currency and the transfer of its competence to the Federal Reserve Board. Several bills to that effect were introduced in Congress, but without much success.[96] The issue of reforming banking regulation never died, but during the 1920s there was no sense of urgency either.[97]

The main subject of discussion during the mid-1920s was that of branch banking. A few but important states experimented with lifting branching restrictions, in order to encourage the development of larger and more stable banks.[98] A majority of states continued to prohibit branch banking. At the same time, the national banks pressed the Comptroller of the Currency and the Federal Reserve Board for a relaxation of regulatory standards that would allow them to compete better with state banks.[99] And indeed, the Board and Governors and the Comptroller of the Currency began authorizing a few

[94] See Alston, Grove, and Wheelock (1994). Chapman and Westerfield (1942, pp. 23, 109) have called the period from 1920 stretching to 1933 that of the "holocaust of bank failures". For details on the failures of national and state banks see also Board of Governors of the Federal Reserve System (1932a).

[95] See for example U.S. Congress (1926) and Board of Governors of the Federal Reserve System (1932d, pp. 26–28).

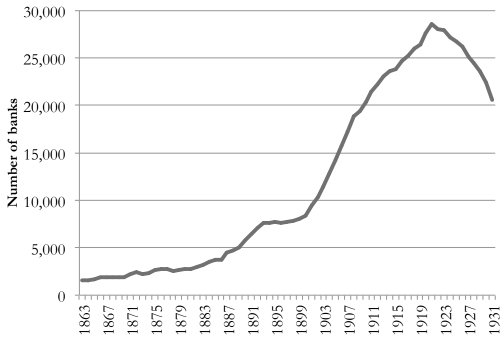
[96] Indeed, there were severe disagreements between the Office of the Comptroller of the Currency and the Federal Reserve Board with respect to regulatory issues. See Harding (1925, pp. 7, 201–214), Robertson (1968, p. 113–115) and White (2011, pp. 35–40).

[97] Macey and Miller (1992, pp. 31, 37, 57–62) argue that there was no sense of urgency, since bank depositors rarely lost large amounts. This, they argue, was due to the double liability bank shareholders, which was mandatory for national bank stockholders, and a widespread practice for state bank stockholders as well.

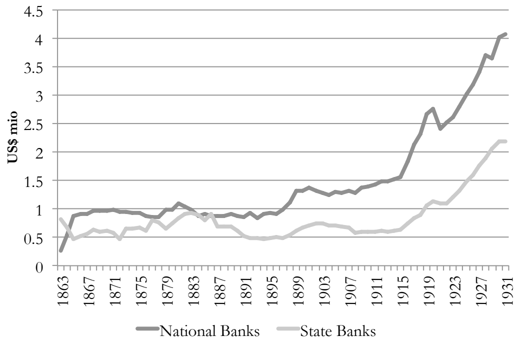
[98] And as Carlson and Mitchener (2009) point out, the removal of branching restrictions did indeed lead to a more efficient and more stable banking system – at least in the case of California, which allowed state-wide branching. Most other states that liberalized branching did so on a city level. See also Doti and Schweikart (1991, pp. 78–85).

[99] The National Banking Act of 1863 was generally interpreted as having barred the establishment of branches for national banks. The only cases of national banks having branches occurred, when national banks took over state banks that did have branches or when these banks would convert to national banks. Those branches were generally allowed to continue operating, even though they were now officially part of a national bank. Similarly there were cases in which state banks with branches were admitted into the Federal Reserve System. Branching regulations for member banks were not uniform in the years following the establishment of the Federal Reserve System and were subject to changing attitudes of both the Office of the Comptroller of the Currency and the Federal Reserve Board. See Board of Governors of the Federal Reserve System (1932c, pp. 117–137), Burns (1974, p. 54) and Federal Reserve Board (1924, pp. 285–286).

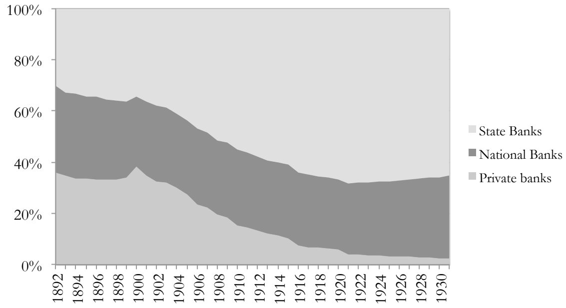
FIGURE 2.5: **The evolution of the banking system in the United States (1863–1931)**



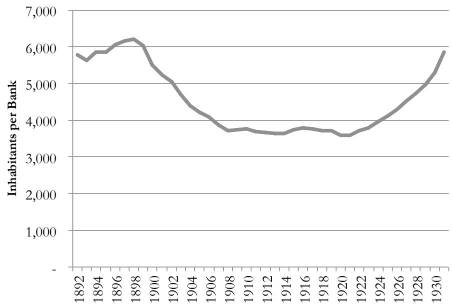
(a) The total number of state and national banks (1863–1931)



(b) The average balance sheet size of national and state banks (1863–1931)



(c) The triple banking system: The number of banks as a % of all banks (1892–1931)



(d) The ratio of inhabitants per bank (1892–1931)

Sources: Own elaboration based on data from Board of Governors of the Federal Reserve System (1932a, p. 115), U.S. Department of Commerce (1949, pp. 25–26) and U.S. Department of the Treasury (1932, pp. 3, 5). The figures (a) and (b) do not include private banks, whereas figures (c) and (d) do. All figures do not include branches.

within-city branches from 1922 onwards.[100] Yet, when a national bank tried to outright establish a new branch in a state that did not allow branching, stating that it was a bank with a national charter and hence state law did not apply, the Supreme Court ruled that the national bank was not explicitly empowered to operate branches and that state law was therefore applicable. The Supreme Court ruling essentially confirmed the practice since the inception of the National Bank Act.[101]

In an effort to put the national banks at par with state banks, the McFadden bill was introduced into Congress in 1924. It had become a necessity, since national banks

[100] Since the inception of the Federal Reserve System, both the Board of Governors and the Comptroller of the Currency urged Congress to pass legislation to allow for at least limited branching of national banks within city or county boundaries. See Chapman and Westerfield (1942, pp. 92–102).

[101] For the decision of the Supreme Court see Federal Reserve Board (1924, pp. 281–286).

started converting into state banks in the 1920s.[102] The McFadden bill was opposed fiercely by the unit state banks who wanted to avoid competition from branch banks that could have spelled the end of the unit bank system. They were supported by their larger correspondent city banks.[103] Similarly, Congresses opinion was on the whole not favorable towards bank branching per se. It is possible that a Congressional majority could have been found that would have voted for an outright ban of branching throughout the United States. Yet, Congress did not possess the necessary constitutional powers to prevent states from allowing their own state chartered banks to branch within state borders. The next best option, to prevent both national banks and state member banks from operating branches, was also considered. But such an option would most certainly have led to the demise of both the national bank system and ultimately the Federal Reserve System in its existing form, as it still depended to a large extend on the compulsory membership of the national banks. If regulations proved too restrictive, national banks were free to exchange their charters for state charters, and state member banks were also free to leave the Federal Reserve system. If such a development would have taken place, it would have amounted to Congress reneging its influence on the banking sector and this was not an option to Congress. The hands of the federal government were tied by the states' regulatory competition, and thus required Congress to pass a law that would put national banks on a more equal footing with state banks.[104]

As a consequence of the branching controversy, the McFadden-Pepper Act was not passed until 1927.[105] The Act amounted to a a slight liberalization of branching restrictions for national and member banks. It allowed them to establish branches within their home city, as long as state laws gave state banks the same right. Additionally, the number of branches was limited depending on the size of the city, and the opening of new branches by national banks was subject to approval by the Comptroller of the Currency. State-wide branching was still prohibited to national and state member banks, even if state banks in

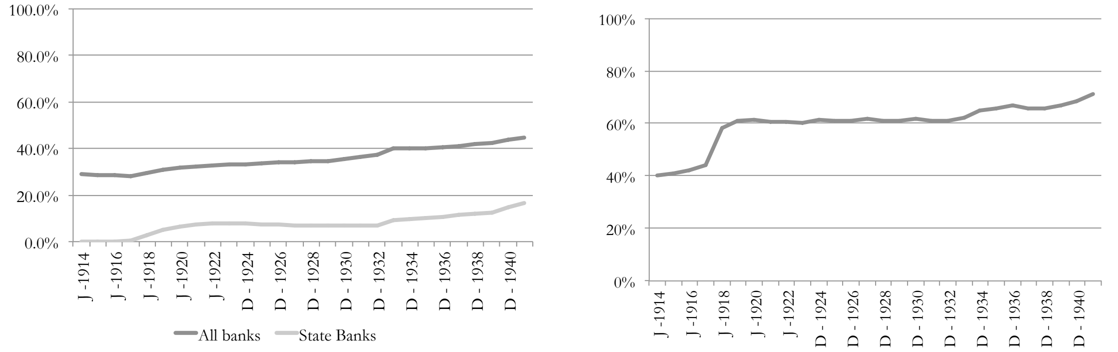
[102]See Board of Governors of the Federal Reserve System (1932d, pp. 26–28), Board of Governors of the Federal Reserve System (1937c, p. 5–7) and Meltzer (2003, p. 216–217).

[103]Interestingly, in California, the state with the most liberal branching laws, a formidable unit banker lobby emerged as well. It was grappling with the effect of the liberalization of branching restrictions in its home state and sought to have it banned or at least restricted again. See Board of Governors of the Federal Reserve System (1932c, pp. 150–151).

[104]For the preferences of political actors with respect to branch banking see Board of Governors of the Federal Reserve System (1932c, pp. 139–141).

[105]The unit bank lobby formed associations for the defence of unit banking and even attempted to include a permanent barrier to an extension of branching in the McFadden-Act in the form of the so-called 'Hull amendments'. This amendment would have turned the bill into a distinctly anti-branching measure; the opposite of what was originally intended.

FIGURE 2.6: **Federal Reserve membership rates (1914–1941)**



(a) The proportion of the **number of banks** that are members of the Federal Reserve System

(b) Federal Reserve member **bank assets** as a proportion of total banks assets

Sources: Own elaboration based on data from Board of Governors of the Federal Reserve System (1943, pp. 6, 16–17, 20–23). All figures do not include branches or unincorporated private banks not reporting to State banking authorities. Banks in US possessions are excluded as well. The letters 'J' and 'D' refer to either year ending in June or December.

the same state were allowed to do so. The Act introduced a number of other important liberalizations on the lending restrictions of national banks. Their passage was largely uncontroversial.[106] The regulatory drive did not end with the McFadden-Pepper Act, and neither did the conversions of national banks into state banks cease completely. Once the Great Depression had set in and the rate of bank failures accelerated, it was clear that a major reform of the regulatory statues for the banking system was on the books.[107]

2.2.5 The Glass-Steagall reforms (1930-1935)

The Great Depression is probably one of the most studied areas in economic history, however, up to this date there is a lively debate as to what exactly caused banks to fail during this time.[108] What stands after decades of debate is the following, however: First, there needs to be a mechanism in any banking system that aids prudent banks in coping

[106]See Board of Governors of the Federal Reserve System (1932c, pp. 141–154) or Chapman and Westerfield (1942, pp. 102–107) for an overview of the Congressional bargaining process and the controversy surrounding the Hull amendment. See U.S. Congress (1927) for the actual McFadden-Pepper Act.

[107]Herbert Hoover even called for banking reform in his annual message to Congress in December of 1929. See Burns (1974, p. 7) and U.S. Congress (1930, pp. 6–9). For an overview of the state and national bank failure rates during the first years of the Great Depression see Board of Governors of the Federal Reserve System (1932a).

[108]Traditionally, there have been two 'camps', the ones arguing that illiquidity, due to depositors panics and the Federal Reserve's inaction, were mainly to blame for most of the bank failures between 1929 and 1933. Friedman and Schwartz (1963) and Wicker (1996) are the most prominent most proponents of this view. The other camp argued that it was insolvency, due to investments and loans going bad, which caused most of the banks to collapse. Calomiris and Mason (2003), Temin (1976) and White (1984) are the most

with adverse liquidity shocks. Second, there also needs to be a regulatory mechanism preventing banks from engaging in lending practices that fail to diversify risk and make them overly sensitive to shocks of the real economy.[109] Contemporary policy-makers were well aware of all this. Thus, Congress went into overdrive and both Houses began a series of extensive hearings[110] on the state of the American Banking System from 1930 onwards, even before major banking panics had set in.[111]

One of the least appreciated aspects in the modern literature of the American attempt to reform its banking regulations in the early 1930s is the fact that leading policymakers[112] were advocating for a complete regulatory overhaul. This overhaul was to replace the current system of over 50 different sets of rules and regulations with a unified commercial banking system under federal supervision. Throughout the Congressional hearings conducted in the early 1930s these opinion were put forward. In most cases it was suggested to unify regulation under the Federal Reserve.[113] In 1932, Senator Carter Glass, chairman of the Subcommittee of the Committee on Banking and Currency of the United States Senate,[114] even requested the Federal Reserve to *"suggest a constitutional method of bringing about the establishment of a unified system of banking under national supervision."* Judicial and legislative precedents had established that states had the right to charter banks. A unified banking system under federal supervision would have to find a way to take away the states' chartering rights. And indeed, the Federal Reserves' general counsel opined that Supreme Court rulings provided Congress with the constitutional power to establish

prominent proponents of this view. Of course, it is a tricky endeavor to separate the two from each other, as they tend to be two sides of the same coin.

[109]These 'lessons' can already be found in the classic Bagehot (1915).

[110]In 1932, the idea of a full-fledged banking commission was unsuccessfully floated. It would have infuriated Senator Glass (amongst others) given the extensive hearings both the House and the Senate had already conducted. See for example an exchange of letters between Guy Emerson and Treasury Secretary Ogden Mills dated July 27,1932 and August 2nd, 1932 in NARA RG 331, Central Files of the Office of the Secretary of Treasury, Correspondence of the Office of the Secretary 1917-1932, Box 84.

[111]See for for example U.S. Congress (1930) and U.S. Congress (1932a).

[112]By this I mean experts of the Federal Reserve, the Comptroller of the Currency and politicians who had been involved the reform of banking regulation for decades, such as Senator Carter.

[113]For example, see Board of Governors of the Federal Reserve System (1932d, pp. 131-134), Board of Governors of the Federal Reserve System (1932e, pp. 43–51), U.S. Congress (1932a, pp. 33, 44) and U.S. Congress (1932c, p. 2). Even President Hoover was not entirely hostile to this idea in his address to Congress in 1931. See President of the United States (1931, p. 10). See also Burns (1974, pp. 11–12, 53) and Kennedy (1973, p. 51).

[114]The chairmen of the relevant Senate and House committees have powerful roles in the American legislative process. Without their consent, pieces of legislature find it difficult to emerge from the (sub)committee. See Berman (1964, p. 212).

a unified commercial banking system under national supervision using a mixture of taxation and prohibition.[115] The Federal Reserve was also strongly in favor of creating such a centralized regulatory system.[116] That the idea of a unified banking system was a powerful one is further highlighted by a resolution of the State Bankers Division of the American Bankers Association, in 1932. In the resolution, the state bankers decried the fact that the idea was having the backing of "powerful interests" and needed to be fought.[117] However, these deliberations were cut short, first, by the upcoming presidential elections of 1932, which led to a political stalemate and later by a wave of bank runs beginning in the fall of 1932.[118]

Even though the United States were rattled by a series of banking crises from 1930 onwards, the federal government would not intervene actively until early 1933. Congress, for its part, had passed a series of legislations aimed at stabilizing the general economic conditions and at improving the operations of the Federal Reserve. But there had been no direct intervention in the banking sector. Until then, it was the state governments trying to combat the various banking crises themselves. It was only with the inauguration of President Roosevelt that policy changed sharply and a nation-wide bank holiday was declared.[119] The first acts passed immediately after the declaration of the bank holiday

[115]The General Council of the Federal Reserve argued that Congress should resort to compulsion, justifying this with three separate lines of reasoning. First, Congress could argue that the competition from state banks represented a danger to the national banking system's stability and survival. Second, since Congress had the power to provide for a national currency it could simply discriminatorily tax the issue of checks by state banks. And third, Congresses power to regulate and protect interstate commerce also applied to the banking sector according to him, as banks could essentially be interpreted as instruments of interstate commerce, whose breakdown had catastrophic consequences on the economy as a whole. The General Council recommended a prohibition of any other than national banks to receive checkable deposits, a prohibitive tax on all checks or similar instruments not drawn or payable at a national bank, as well as the generally prohibition of national banks to interact with state banks. See Wyatt (1932). For a similar opinion see Rodkey (1934). It is uncertain, however, whether the prohibition of state banks to offer checkable deposits would have indeed been proclaimed constitutional and whether it would have done the trick. After all, they still did not take away the right of states to charter financial institutions per se. For example, the ascent of money market funds after the Second World War would probably not have been affected by such a provision. Additionally, Duncan (1999, pp. 221–222) points out that the courts had begun to develop the "competitive balance" doctrine, which referred to the balance between state and federal statutes. It was originally meant as a defensive device for the national banking system, but it turned into a shield for state banks from federal regulation and national bank competition. Scott (1977, p. 42) claims that the doctrine stemmed from an incorrect interpretation of the courts of the intentions behind the original National Bank Act.

[116]See for example a statement read by Governor Meyer on behalf of the Federal Reserve Board to Senator Norbeck in U.S. Congress (1932b, pp. 357–358).

[117]A later report by a less partisan committee of the American Bankers Association would somewhat soften its attacks and instead call for more cooperation amongst regulators. See Board of Governors of the Federal Reserve System (1932d, p. 68). See also Burns (1974, pp. 71–73) and Kennedy (1973, pp. 232–233).

[118]See Willis (1935, p. 718).

[119]For the frantic discussions surrounding the Emergency Banking Act during the first days of Roosevelt's administration see for example McJimsey (2001).

provided the necessary funds to re-capitalize banks through the Reconstruction Finance Corporation (RFC) in return for preferred stock. By the end of the banking holiday, the government had equity interest in half of the countries' banks.[120]

During the first three months of Roosevelt's presidency, Congress acted both swiftly and decisively. In doing so, Congress was benefiting from three years of prior Congressional hearings and debate. The options were clear and it was only a matter of compromising on measures that could be readily implemented and that would restore confidence in the American banking system. This made a major overhaul of the banking system, such as a centralized regulatory agency, an unlikely candidate.[121] Nevertheless, the unification of the banking system under national supervision was an option taken into consideration and advocated by an increasing number of individuals, including the New York State banking authorities.[122] Swift actions in Congress were aided by a significant shift in public opinion. This was of course primarily due to the general banking holiday, but also to some extent to the so-called 'Pecora' Investigation. It was a Congressional inquiry, which had been launched in 1932 to investigate the origins of the Wall Street Crash of 1929. Initially, the commission was unable to reveal much of interest. Only when Ferdinand Pecora took over in early 1933 as chief council did the investigation uncover fraudulent practices amongst Wall Street banks, which outraged the public.[123]

In the summer of 1933, major regulatory reforms, commonly referred to as the Glass-Steagall Reforms, were passed after a series of intense discussions.[124] By then, the situation in the banking sector had already stabilized. Nevertheless, the Act introduced comprehensive changes to the regulatory framework and to the banking structure. In terms of regulation, it introduced stricter limits to investment and it included the possibility of the removal from office of bank directors or other bank officers. The Glass-Steagall Act required the complete separation of investment and deposit banks. Investment banks were

[120]More than $\frac{2}{3}$ of the banks the government had a stake in, were state banks according to Kregel (1997, pp. 262–263).

[121]See Burns (1974, p. 89), Schlesinger (1960, pp. 4–7) and Willis (1935, p. 697).

[122]See McJimsey (2001, Document 14, pp. 78-98), which contains the minutes of a series of meetings in the U.S. Treasury beginning March 5, 1933. For the growing support of a centralized banking system see Burns (1974, pp. 82–84).

[123]For a recent account of the Pecora Commission see Perino (2010). For a more academic account see for example Kennedy (1973, pp. 106–128, 204–205).

[124]See Burns (1974), Calomiris and White (1994), Kennedy (1973) or Preston (1933) for detailed accounts of the discussions taking place in the spring of 1933. See U.S. Congress (1933a) for the Banking Act of 1933.

not allowed to accept any deposits from the general public nor from deposit banks. Interlocking directorates were also explicitly banned. Deposit banks were only allowed to buy investment securities on account of their customers. This was the same idea that had been proposed by the Pujo commission 20 years earlier. This time around, it was Senator Glass who had thrown his weight behind it.[125]

The Act also introduced deposit insurance. Deposit insurance, too, had been an idea with a lengthy albeit largely unsuccessful history. During the 1930s, it had been strongly opposed by the entire league of 'technocrats', as well as the larger banks and President Roosevelt. Essentially, deposit insurance was only a partial kind of remedy for the structural problems caused by the atomistic structure of the banking system. Once depositors knew that their money was federally insured, they had no incentive to 'run' anymore. This strengthened unit banks vis-a-vis larger banks, as safety was no longer a distinguishing feature by which they had to compete with them. The technocrats had preferred to solve the problems resulting from the atomistic structure of the banking system by allowing banks to branch.[126] The lobby for deposit insurance centered around the Chairman of the House Committee on Banking and Currency, Representative Steagall, and faced the resistance of the Chairman of the Senate Subcommittee on Banking and Currency, Senator Glass. Each of them was opposed to the reform plans of the other. However, the unit banker lobby embodied by Representative Steagall successfully linked their call for deposit insurance with the public's cry for the safety of their deposits, and eventually Steagall and Glass settled for a 'tit-for-tat'. They simply passed both measures, deposit insurance and the separation of investment and deposit banks, as they were not in direct conflict with each other. Additionally, Steagall sweetened the deal by agreeing to another provision Senator Glass was trying to include: an interest rate prohibition on

[125]See Burns (1974, p. 25). Macey (1984, pp. 16–21) suggests that Senator Glass must have been supported by the existing pure investment banks, as they were effectively protected from the competition of commercial banks by this measure. However, most modern evaluations of economists see the separation of deposit and insurance banks as a case of misguided public policy. See for example Benston (1990), Kroszner and Rajan (1994, 1997) or White (1986). One important, but often overlooked fact, is that these rules applied only to national banks and member-state banks, but did not apply to non-member state banks, as pointed out by Benston (1990, pp. 9–10). Neither were commercial banks prohibited from underwriting and dealing in securities outside the United States. This allowed some national banks to become key players in the Eurobond market. For an interesting analysis of the initial effects of the separation on the investment banking industry see for example Carosso (1970).

[126]See Calomiris and White (1994, p. 147–152). Macey and Miller (1992, pp. 34, 37–40), Mitchener and Richardson (2013, pp. 23–24) and White (2011, pp. 49–50) point out that the introduction of deposit insurance came hand in hand with the abolition of double liability. They see the abolition as a major cause for banks' increased risk-taking in recent decades.

demand deposits.[127] The existence of deposit insurance paired with branching restrictions largely still in place, effectively meant that the atomistic structure of the banking system would prevail for as long as the states upheld the branching restrictions. Indeed, in its report on the bill preceding the Banking Act of 1933, Senator Glass once more stated that the proposed measures were a temporary fix, rather than a comprehensive reform, and that a way needed to be found to harmonize, i.e. centralize, banking regulation throughout the United States.[128]

Instead of centralizing the regulatory framework of the United States, the introduction of deposit insurance created yet another new regulatory institution: the Federal Deposit Insurance Corporation. Thus, the regulatory framework was to become even more fragmented. All national banks as well as all state banks who were members of the Federal Reserve System were required to join the FDIC. Non-member banks of the state system could apply to join. The regulatory structure of the United States became more complex still. Now banks were either *national banks* (and regulated by the Comptroller of the Currency, the Federal Reserve and the FDIC), *state member banks* (regulated by the Federal Reserve, the FDIC and the respective state of origin), *insured nonmember banks* (regulated by the FDIC and the respective state of origin) or *noninsured nonmember banks* (regulated merely by the respective state of origin).[129] The commercial banks had even more options than ever to engage in regulatory arbitrage.

Interestingly, the Banking Act of 1933 also contained three key provisions that would have given state banks a much greater incentive to either become members of the Federal Reserve System or to convert into national banks altogether. First, after July of 1936, access to the permanent federal deposit insurance fund was to be restricted to member banks of the Federal Reserve System only. State banks that did not subject to regulation by the Federal Reserve would not be able to benefit from deposit insurance from the summer of 1936 onwards.[130] Second, the banking act also repealed a provision that allowed state banks to become members of the Federal Reserve System with only 60% of the capital

[127] Senator Glass wanted this in order to further weaken potential links between investment and deposit banks. See Calomiris and White (1994, pp. 172–175) and Preston (1933, pp. 587–590).

[128] See U.S. Congress (1933b, p. 2). Indeed, quite a number of states liberalized branching restrictions. By the end of the decade, 17 of 49 states allowed at some kind of limited branching, whereas 19 states even allowed state-wide branching. See Chapman and Westerfield (1942, pp. 128–129).

[129] Private banks which wanted to continue receiving deposits were required to subject to regulation by either the federal government's or a state's regulation.

[130] See Section 8 (f) of the Banking Act of 1933. See also Preston (1933, p. 592). Kennedy (1973, pp. 218–221) reports that Senator Glass was able to push this provision past Representative Steagall and that even the Comptroller of the Currency O'Conner lobbied strongly for this provision.

Table 2.1: **Banks' membership rates in either the Federal Reserve and/or the FDIC in 1935**

	Proportion of all banks	**Proportion of all deposits**
Member Commercial Banks	**40.0%**	**69.5%**
National Banks	33.7%	44.8%
State Member Banks	6.3%	24.7%
Insured Non-Member banks	**48.6%**	**12.0%**
Commercial Banks	47.9%	9.9%
Mutual Savings and Other	0.7%	2.1%
Non-Insured Non-Member Banks	**11.4%**	**18.5%**
Commercial Banks	5.7%	1.3%
Mutual Savings	3.2%	16.1%
Other	2.5%	1.2%

Merely 40% of banks, but with 70% of the deposits were members of the Federal Reserve System, and almost 90% of bank joined the FDIC's Deposit Insurance, representing over 80% of all deposits in the country. *Source: Own elaboration based on data from Federal Reserve Board (1937, pp. 782–784).*

that comparable national banks would have to hold.[131] This greatly reduced incentives for national banks to convert to state banks in order to benefit from the lower capital charge incurred by state banks. The third provision clarified that national banks would be allowed to branch in states, where state banks were explicitly allowed to operate branches as well.[132]. Once more, the federal government created strong incentives for state banks to submit to central regulation of the Federal Reserve, if state banks wanted to benefit from the rediscount facility of the Federal Reserve System or deposit insurance. Senator Carter Glass and his supporters were thus trying to implicitly create the incentives necessary for greater centralization of banking regulation, just as the U.S. government had done in 1863–1865 and 1913.[133] However, the provision requiring banks to be members of the Federal Reserve System in order to gain access to the Federal Deposit Insurance was relaxed numerous times in the following years. In the Banking Act of 1935, membership to the Federal Reserve was only made mandatory for banks with deposits over US$1 million, if they wanted to join the deposit insurance. And even that only as of July 1942. Additionally, the Board of Governors was given the possibility to exempt banks from the requirement altogether. In 1939 this key provision was repealed entirely.[134]

[131] See section 17 (b) of the Banking Act of 1933. Exceptions were given merely for particularly small state banks.

[132] See section 5 (b) of the Banking Act of 1933.

[133] Preston (1933, p. 597) claims that these provisions were indeed Senator Carter Glass' intentions.

[134] See Board of Governors of the Federal Reserve System (1936, p. 8) and Board of Directors of the Federal Deposit Insurance Corporation (1959, Section 'Legislation under which the Corporation has operated'). The latter was found in BArch B102/41817.

Although the inception of the FDIC technically brought most state banks under the influence of a federal agency, the American regulatory structure was far from being a centralized system as there was no uniformity in regulatory standards and supervisory responsibility was still diffused.[135] The states were still free to charter banks and to engage in regulatory competition. As part of the regulatory reforms, the federal government had also created the Federal Home Loan Bank (FHLB) system in 1932, which was a system of banks that provided rediscount specifically to mortgage banks. The Federal Home Loan Bank Board (FHLBB) both chartered and regulated federal savings and loan associations (S&L's), which would automatically join the FHLB system. Furthermore, their deposits were insured by the newly established Federal Savings and Loan Insurance Corporation (FSLIC). Again, existing state chartered S&L's could opt to join these systems.[136] The separation of deposit and investment banks also led to the creation of a separate regulatory agency for investment banks – the Securities Exchange Commission (SEC). The SEC indirectly regulated investment banks through their activities in stock exchanges, which were subject to regulation by the SEC. Thus, the government had created a separate regulatory system for the different types of banks. Furthermore, the three main federal regulatory institutions for commercial banks (the Comptroller of the Currency, the Federal Reserve and the FDIC) had severe disagreements with respect to regulatory practice, which hindered effective cooperation.[137] Last but not least, all banks, including national banks and member banks, were generally still subject to regulations by the respective states they were in, if the federal government or its independent regulatory institutions had failed to regulate a certain aspect of the banking business. In those cases, state law could still apply. Sometimes, the federal regulators even specifically relied on the legislation provided by the states for certain regulatory definitions.[138]

From 1936 until 1939, the Federal Reserve launched another attempt to convince the Roosevelt government to attempt the centralization of the commercial banking sector.

[135] Burns (1974, pp. 174–175) sees the introduction of the FDIC as a big success for the federal government, given the degree of opposition it faced in introducing its reforms. For the complexities of the regulatory structure see Board of Governors of the Federal Reserve System (1937b) as well as figures 2.7 and 2.8 on pages 53 and 54. In contemporary accounts, the Department of the Treasury and the RFC were also depicted as additional (temporary) regulatory agencies. While the Treasury had minor licensing responsibilities, the RFC could conduct examinations in banks that it had taken a capital stake in.

[136] See Harriss (1951), Wallace (1938) and Wheelock (2008, pp. 140–145).

[137] See Robertson (1968, p. 134).

[138] See for example Federal Deposit Insurance Corporation (1984, p. 73). It is still the case today that state legislation can have an effect on federally regulated banks, unless the federal government or its regulators pre-empt state law. See for example Natter and Wechsler (2012) or Duncan (1999).

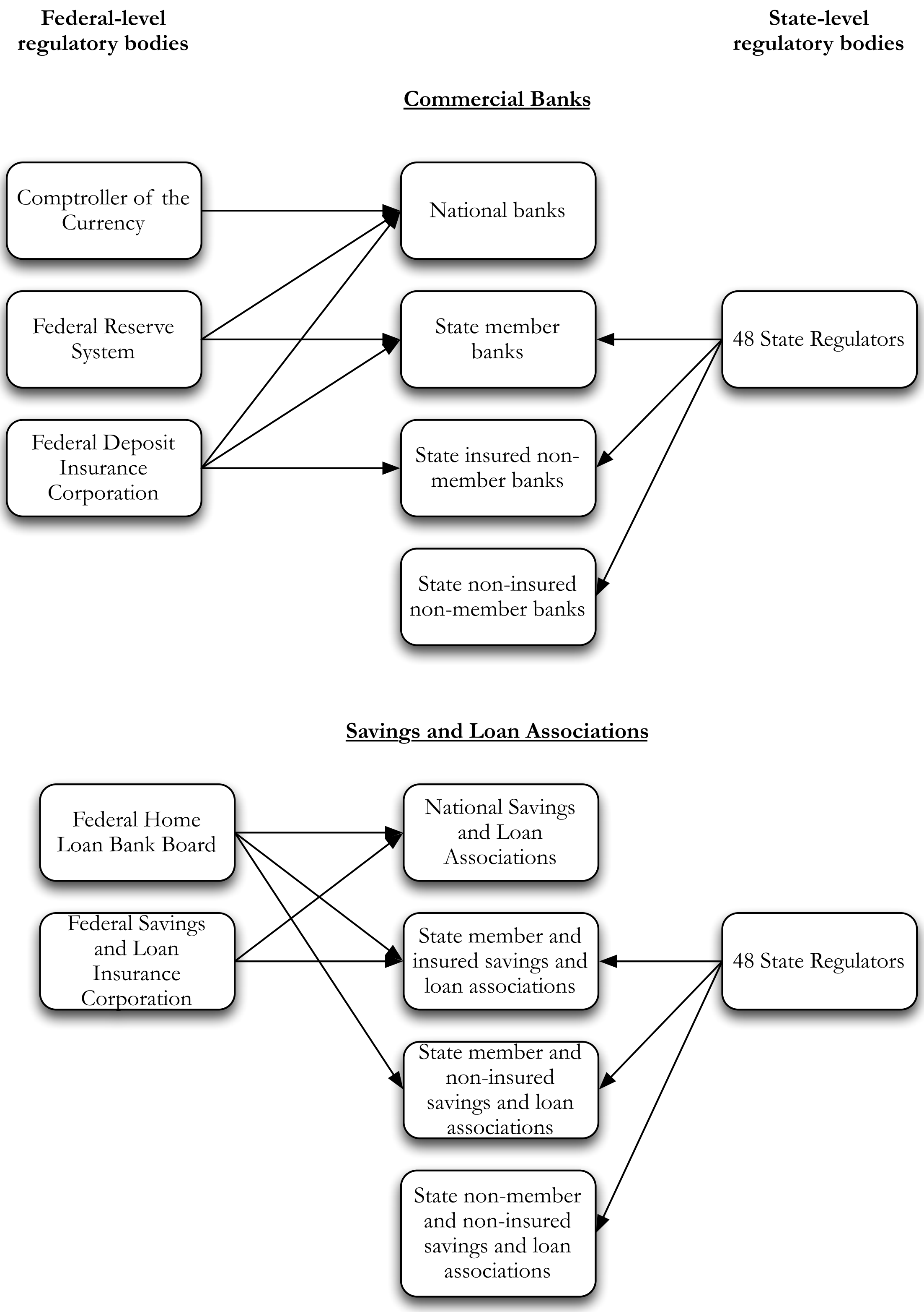
In a series of memoranda, the Federal Reserve laid out the case for the centralization of banking regulation and the possible measure that could be taken by the government to bring about a unified commercial banking system.[139] A number of bills that attempted to unify regulation on the federal level were even introduced in Congress between 1938 and 1939.[140] But the political momentum of the banking crisis of 1933 had already been used up in the Banking Acts of 1933 and 1935, and the Federal Reserve's calls went unanswered.[141]

[139] See Board of Governors of the Federal Reserve System (1936-1938) for the 'Bank Suspension Study' and in particular Board of Governors of the Federal Reserve System (1936) for a memorandum on the 'Unification of the Commercial Banking System'. See also the Annual Report of the Board of Governors of the Federal Reserve System (1939, pp. 1–21), as well as a concrete plan to improve federal banking supervision by the Board of Governors of the Federal Reserve System (1941).

[140] See Hackley (1966b, pp. 800-801).

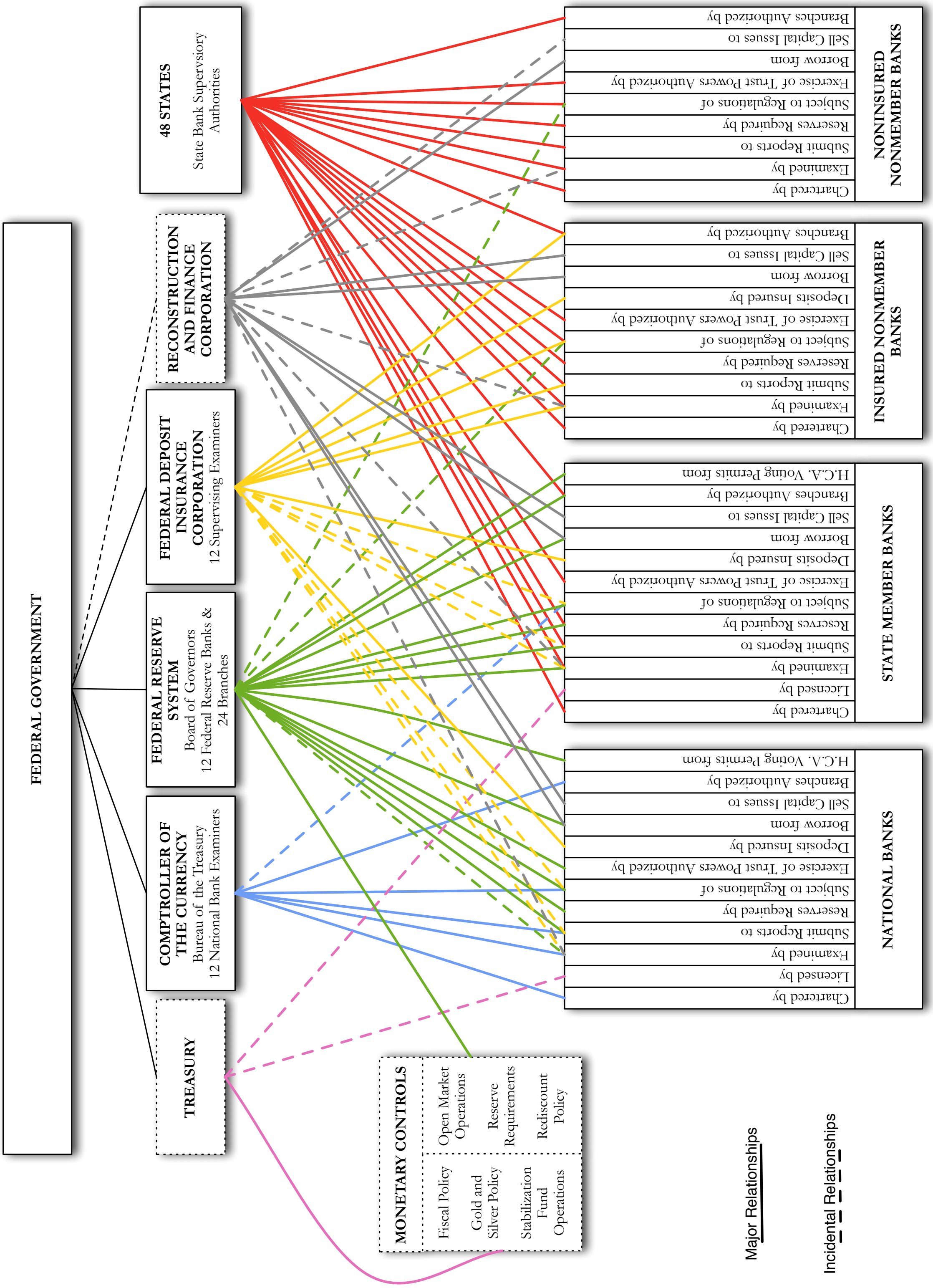
[141] This 'window of opportunity view' is echoed in Calomiris (2006b, p. 76) However, it is not clear from the existing literature, why exactly further regulatory reform did not take place. One suggestion by Chapman and Westerfield (1942, pp. 125–126) is that from 1936 onwards the influential American Bankers Association combated any law that endangered the dual banking system and that threatened to increase the federal government's influence over the banking sector. For a schematic overview of the American regulatory structure in 1935 see figure 2.7 on page 53. For a detailed view of the regulatory responsibilities see figure 2.8 on page 54.

Figure 2.7: **Schematic overview of the regulatory arrangement in the United States in 1938**



Investment banks (both state and private) are not included in this chart since they were not allowed to accept deposits. Investment banks were regulated indirectly, through their activities in stock exchanges, by the SEC. Contemporary accounts sometimes also included the Secretary of the Treasury and the Reconstruction and Finance Company (RFC) as other potential regulators of the commercial banks. See figure 2.8 on page 54. *Source: Own elaboration.*

FIGURE 2.8: **The principal regulatory responsibilities for commercial banks in the United States in 1938**



This overview does not include non-incorporated banks (e.g. savings and loans banks) or investment banks. It does however include the Refinance and Construction Corporation (abolished after World War II) and the US Treasury, which are generally not included in other overviews of the regulatory structure. Note that each federal regulatory agency operated with a number of sub-offices throughout the United States. *Source: Board of Governors of the Federal Reserve System (1939, p. 9) and Board of Governors of the Federal Reserve System (1941, pp. 5–6).*

2.3 Germany

2.3.1 Pre nation-state banking regulations (1815-1870)

The development of a modern German banking system only began towards the middle of the 19th century, when the first corporate banks were founded and when measures were taken to unify the country and the currency.[142] Before the Napoleonic wars, Germany consisted of a loose federation of about 300 individual kingdoms, principalities, duchies and city states, which were formally united under an elected Emperor in the Holy Roman Empire.[143] Many of these had their own currency. Under the Napoleonic occupation, the number of states and kingdoms was drastically reduced. The end of the Napoleonic wars also saw the ascent of the kingdom of Prussia, which was instrumental in bringing about the unification of the numerous German states and kingdoms into a single German nation state. Furthermore, in 1815, the Congress of Vienna established a loose association of 41 German states in a "German Confederation".[144]

In the Confederation the number of currencies circulating simultaneously was reduced to just nine. In 1834, a German customs union was established by some of the member states of the German Confederation, which promptly attempted to standardize the currency amongst its member states, albeit with limited success.[145] Even so, the pace of industrialization increased significantly. As the German territory was still dominated by agriculture, up until the middle of the 19th century the predominant mode of banking was still 'pre-industrial' in nature. Private bankers dominated the scene, which helped to finance governments and to some extent also the expansion of transport networks. Some larger government run banks were set-up, but their primary concern was that of government rather than commercial or industrial finance. In Prussia, so-called 'Landschaften' had been installed in the 18th century already, to facilitate mortgage credit to wealthy

[142] Prior to that it is difficult to speak of a banking system in a modern sense. For an overview of banking in Germany prior to 1806 see Klein (1982).

[143] The central structures of the Holy Roman Empire were weak at best. Ever since the Peace of Westphalia in 1648 they were virtually non-existent anymore. Nevertheless, the last Emperor only stepped down in 1806. Voltaire humorously summarized this arrangement as follows: *"This agglomeration which was called and which still calls itself the Holy Roman Empire was neither holy, nor Roman, nor an empire."*, cited in Knowles (2001, p. 797). For a brief history of the German Reich under a Kaiser see Winkler (2006, pp. 4–46).

[144] Prussia and Austria were the largest and most powerful of the states and dominated the German Confederation politically and economically. See also Kitchen (1978, pp. 9–33) or Winkler (2006, pp. 64–70).

[145] Austria did not join the customs union, leaving Prussia to dominate it.

landowners. They were organized according to the cooperative principle, but excluded poor small scale farmers. During the first half of the 19th century, the public *Sparkassen* or savings bank system developed strongly, primarily as a measure of social policy. The *Sparkassen* were adjunct offices of the municipal administrations. They accepted savings deposits only from the low to middle income strata of society in urban centers. At the outset, the *Sparkassen* did not even offer credit to their depositors. Instead, they invested the deposits in save assets, primarily in mortgages, but also in (municipal and eventually federal) government paper or in some cases in local businesses, and paid the depositors interest. At the outset, the Sparkassen were thus more similar to mortgage banks. Due to decentralized nature of the political framework, the German banking system also adopted a decentralized structure by the middle of the 19th century. Contrary to the banking system in other European countries such as England, Scotland or France, it was a highly localized unit bank system with the added disadvantage that capital markets were not well developed either.[146]

A further contrast to the United States was that incorporated credit banks only began to develop as late as 1848. In large measure, this was due to the dominant Prussian state, which did not look favorably upon the establishment of joint-stock companies in general. Consequently it had established strict chartering requirements. Other German states were even less inclined towards joint-stock companies. After all, industrialization threatened the economic and social standing of the landed aristocracy. The pace of industrialization increased substantially after the German Revolution of 1848, and incorporated banks were founded in increasing numbers as the Prussian state adopted a more liberal stance. The cooperative banking movement established a foothold in Germany after the revolution of 1848 as well. These cooperative banks meant to alleviate the lack of credit in rural areas, for both small scale farmers and manual laborers.[147] At the same time, the division between protectionist Austria and the increasingly liberal Prussia widened. After a prolonged period of diplomatic manoeuvring and shifting Alliances, a series of wars ensued in the 1860s. These culminated in the in the Franco-Prussian War of 1870/71. From this a unified

[146] For the Customs Union see for example Kitchen (1978, pp. 34–61). For the German Banking System up until 1848 see Born (1985, pp. 31–34, 55) and Pohl (1982a). For the development of the *Sparkassen* see also Pohl (1982b, pp. 195–201).

[147] See Born (1985, pp. 31-34), Kitchen (1978, pp. 61–109), Pohl (1982a) and Pohl (1982b, pp. 171–194, 202–210) and Tilly (1999, pp. 135–137). Manâa (2011, p. 98) points out that the prevailing mercantilist thought only deemed the limitation of personal liability acceptable, as long as the corporation was driven by the motive to foster the common good, rather than being driven by the profit motive.

German national state under the sole leadership of Prussia emerged.[148] This state was a federal political system in many respects. However, unlike the United States, the federal legislature had the right to impose regulations for the entire banking sector throughout Germany.[149]

2.3.2 Uninhibited growth (1871-1905)

The spoils of the Franco-Prussian War also included French war reparations, which the French government was able to pay within merely three years. This influx of capital, paired with the creation of a new unified market, fuelled a substantial economic boom that already began in 1867 with the formation of the North German Confederation – the first German nation state in the modern sense, which then evolved into the German Empire. Numerous joint-stock companies, including banks, were founded. The creation of joint-stock companies was made possible not only by the abundance of capital searching for investments in the new nation state. It was also facilitated by new liberal legislation, which introduced the principle of freedom of trade (*Gewerbefreiheit*). This waived the governments' rights to charter joint-stock companies throughout much of Germany.[150]

The boom ended in a major stock market crash, soon termed *Gründercrash* (literally: start-up crash), as the ensuing recession weeded out many of the newly floated companies and reduced their stock to worthless paper. Nevertheless, the boom had paved the way for the wide-spread acceptance of joint-stock banks throughout Germany. The boom had also seen the ascent of specialized mortgage banks. They too were joint-stock companies, but they focused exclusively on agricultural and later on urban mortgage credit. From 1871 to 1875, the currency was unified and the Gold standard formally introduced. In 1875, an act of parliament created a public-private central bank, the *Reichsbank*, that served as the main note issuer, and re-discount facility for banks. The *Reichsbank's* introduction was not universally welcomed, as there were 33 different private note issuing banks prior to its introduction. In a political compromise, these private note-issuing banks were allowed to continue to exist, but their note issue was limited, and it was taxed to a higher degree

[148] See Kitchen (1978, pp. 110–132) and Winkler (2006, pp. 118–191).

[149] For an analysis of the constitutional arrangement see Burhop (2011b, pp. 20–23), and for the constitution itself see Reichsgesetzblatt (1871).

[150] Interestingly, the government was well aware that this liberalization would lead to a boom in cooperations, some of which might not be run by prudent managers. See Manâa (2011, p. 97) and Wandel (1982b, p. 15).

than the note issue of the *Reichsbank*. Also, the other private note issuing banks were only allowed to establish branches within their home state, whereas the *Reichsbank* was allowed to branch nation-wide, through which it accepted deposits by the public. However, these did not yield any interest payments and primarily served for cashless payment services. As a consequence of the newly established *Reichsbank*, almost half of the private note banks reneged their privilege to issue notes within the first year of the *Reichsbank's* existence.[151] The private note banks continued to cause some headaches to the *Reichsbank* until the turn of the century, primarily because they offered better conditions for re-discount. This practice was prohibited by law at the turn of the century at about the same time as the *Reichbank's* notes were officially declared the only legal tender in 1906.[152]

The *Reichsbank* was an institution created by public law, but as part of the compromise it was funded by private capital. This gave the shareholders significant influence over the *Reichsbank's* affairs. As a public institution it was officially under the control of a government Curatorium. However the government rarely got involved in internal *Reichsbank* matters. Instead it delegated most of its responsiblities to the *Reichsbank's* executive body, the directorate. The President and the Vice President were the most important individuals within the organization. Rarely did members of the directorate oppose motions put forward by either of them. The directorate was, however, further supervised by a Central Committee. This was a committee elected by the private shareholders of the *Reichsbank* to represent their interests. By the beginning of the 20$^{\text{th}}$ century, most of the committee members were affiliated in one way or another with the major private banks at the time. The Banking Act of 1875 stipulated that the opinion of this committee had to be heard on a range of issues and in some cases it had veto power. This was for example the case with the extension of credit to the government that went beyond normal business dealings. While the influence of this committee on actual policymaking is debated, there is no doubt that there was a close connection between the major banks and the *Reichsbank* developed towards the end of the 19$^{\text{th}}$ century.[153] Interestingly, the Banking Act of 1875 did not contain any regulatory provisions for other types of banks although the possibility was discussed. It was discarded on the grounds that the legislators were not willing to

[151] See Born (1985, pp. 52–58, 115–119), (Döring, 1933, p. 144), Kitchen (1978, pp. 132–160), Manâa (2011, p. 98), Pohl (1982b, pp. 210–215) and Pohl (1982c, pp. 223–229, 243–251, 305). For the unification of the currency see especially Borchardt (1976, pp. 6–14).

[152] See Döring (1933, pp. 140, 144) and Wandel (1982b).

[153] See Borchardt (1976, p. 16), Feldman (1993, pp. 26–27), Habedank (1981, pp. 15–21) and Reichsgesetzblatt (1875).

abandon the principle of 'freedom of trade' that had been introduced just a few years earlier.[154]

Banking regulation was only discussed after 1891 again. A number of private banking businesses had collapsed amid allegations of fraud. In the subsequent government commission with respect to stock market practices, the issue of bank regulation was not part of the official discussions. Nevertheless, a draft law was proposed by conservative members of the commission that aimed at protecting depositors. It would have regulated the private banking sector and would effectively have amounted to a separation of investment and commercial banks.[155] This draft law was briefly discussed within the commission, but quickly discarded as not being actionable. Eventually, the German parliament merely passed a resolution in which it urged the government to study the feasibility of universal banking regulation, and to prepare a corresponding legislative proposal – which the government never did.[156] And it was with the executive government, where the de-facto power lay during the German Empire. It was nearly impossible for the parliament to impose legislation against the will of the executive. Indeed it was not uncommon for interest groups to bypass parliament and to go straight to the chancellor with their demands.[157]

The German parliament did pass a new corporate law, however, that had a direct effect on the incorporated banks. Already in 1884 the government had already re-introduced specific chartering requirements for the establishment of new incorporated banks in an effort to increase the quality of newly established incorporated banks. The Corporate Act of 1896 introduced additional rules to protect the public from fraudulent corporations. One of these barred new corporations from selling their shares on a stock exchange for one year after after the corporation's establishment. Its shares would have to be held by a bank for that time period. But it was only larger banks, which could afford to conduct such a risky investment. Thus, this specific change in corporate legislation greatly favored larger banks over smaller ones. The law, which had the intention of protecting the public, ended up promoting one part of the banking sector at the expense of the others. This

[154]See Bankenenquete 1908/09 (1910, p. 4), Manâa (2011, pp. 112–113) and Wandel (1982b, p. 19).

[155]The law would have required quarterly balance sheet reporting of minor financial agents (individuals and entities whose primary business was not financial) and monthly balance-sheet reporting of full-fledged financial institutions. Additionally, the draft called for deposit banks to be prohibited from engaging in speculative activities, from acquiring shares in any 'undertaking' or corporation, as well as prohibiting deposit banks from helping in placing bonds of any 'undertaking' or corporation on the capital markets - apart from government paper and well-collateralized securities. This 1896 proposal from Graf Arnim et. al. is reprinted in Bankenenquete 1908/09 (1910, pp. 65–67).

[156]See Bankenenquete 1908/09 (1910, p. 4).

[157]See for example Gall (1995, p. 78) or Feldman (1981, p. 165).

fostered concentration in the banking sector. Concentration tendencies had already been fairly strong in previous years. After all, industrialization had created new sectors such as the mining and steel industry, which were capital intensive and it was only corporative banks, which possessed the necessary financial muscle to cater to these industries, as capital markets were not sufficiently developed.[158] Similiarly, in 1881 already, a tax was passed on the transfer of securities at stock exchanges (the *Reichsstempelgesetz* of 1881). Again, this law benefited larger players, as they could simply conduct transactions internally, without conducting actual (and thus taxed) transactions.[159] After the passage of the Corporate Act of 1896 a number of credit banks began to develop extensive branch networks, to a large extent by taking over competitors and by turning their offices into outright branches. Already in 1881, the largest private and Berlin based banks, began to form a cartel (the *Berliner Stempelvereinigung*). At first it was a tax-saving association, but it soon turned to harmonizing short-term interest rates and commissions.[160]

Towards the beginning of the 20th century, the issue of banking regulation resurfaced in public again. On one hand, this was due to the rapid development of the banking sector and the increasing concentration in the private credit bank segment, and on the other due to some isolated bank failures of private bankers and mortgage banks caused by fraudulent practices. Concrete proposals for both regulation and supervision of large swathes of the banking sector were put forward by academics, in order to protect depositors. But these failed to make much headway in parliament and no action was taken by the government.[161]

By the turn of the century a system with specialized banking types had evolved in Germany. *Cooperative banks* focused on rural working-class customers, the *Sparkassen* on urban working-class and small business customers, *mortgage banks* on urban real estate, regional government banks on agricultural mortgage credit and medium sized companies, while *private credit banks* catered to industry, and *private bankers* acted as brokers and

[158] See Döring (1933, pp. 145–146), Manâa (2011, p. 112), Tilly (1999, pp. 139–141) and Wandel (1982b, pp. 14-16).

[159] See Riesser (1911, pp. 618–623).

[160] See Verhandlungen und Berichte des Unterausschusses für Geld- Kredit und Finanzwesen (V. Unterausschuß) (1930, pp. 25–28) and Hardach (1995b, p. 915–917).

[161] Draft laws by Professor Warschauer proposed the establishment of a federal deposit bank, as well as state deposit banks and they aimed at restricting the maximum amount of deposits investment banks and credit cooperatives could accept. Professor Wagner was the most vocal proponent of the establishment of a supervisory supervisory agency. Another prominent proponent was Dr. Georg Obst. See Bankenenquete 1908/09 (1910, pp. 4–5, 77–78). For a contemporary work on the concentration movement of the largest private credit banks see for example Riesser (1911).

Table 2.2: **Market shares of the different banking groups in Germany (1860–1913)**

Bank Group	**1860**	**1880**	**1900**	**1913**
Sparkassen	12.0%	20.6%	23.3%	24.8%
Cooperative Banks	0.2%	4.4%	4.1%	6.8%
Incorporated Banks	9.2%	10.0%	17.2%	24.2%
Mortgage Banks	16.9%	26.7%	28.5%	22.8%
Private Bankers	35.3%	18.5%	8.6%	4.4%
Private note emitting banks	22.4%	11.6%	6.3%	4.4%
Other banks	4.0%	8.2%	12.0%	12.6%

Source: Burhop (2011b, p. 168).

investment advisers. However, the private bankers and the note emitting banks had already lost much of their market shares during the early years of the new nation state, in particular to the largest private credit banks.[162] Similar to the United States, Germany had thousands of small unit banks, either taking the form of cooperative banks, *Sparkassen* or private bankers.[163]

A major difference with the United States was the fact that large parts of the German banking system were comprised by government-sponsored banks, such as the *Sparkassen* and *Landesbanken*. Technically, the *Sparkassen* were not full-fledged banks, yet. They were adjuncts to municipal or city governments and did not have an independent legal shell.[164] As public institutions, the *Sparkassen* and *Landesbanken* were subject to the directives of the corresponding state and were not allowed to conduct business in other states. However, they were also exempt from corporate taxation and they benefited from implicit government guarantees, giving them an advantage over other private banks.[165]

In Germany, no comprehensive federal regulation existed for any bank type, besides for the mortgage banks. This regulation had been passed in 1899 to harmonize mortgage bank legislation throughout Germany, as some states had begun to pass their own special legislation in this particular field. As of 1900, mortgage banks were restricted in their range of investments and they were subject to federal or state chartering as well as supervision by the states they were located in. Federal norms also existed for private note emitting

[162]See Fohlin (2007, pp. 21–28). See tables 2.2 and 2.3 on pages 61 and 62, respectively, for an overview of the market shares and the number of banks over time.

[163]This is indeed remarkable as both France and the United Kingdom had systems with merely a fraction the amount of banks. Rajan and Ramcharan (2009, p. 40) suggest that countries with a higher number of banks per capita had a less concentrated distribution of farm land.

[164]The *Sparkassen* were only given an independent legal form in 1931. See Reichsgesetzblatt (1931a, Fünfter Teil: Handels- und Wirtschaftspolitik, Kapitel 1, pp. 554–556).

[165]See Hardach (1995b, p. 919) and Speer (1933, p. 179).

TABLE 2.3: **Number of Banks in Germany (1861–1913)**

Bank Group	**1861**	**1885**	**1900**	**1913**
Sparkassen	323–517	1,318	2,685	3,133
Cooperative Banks	300	2,495–2,595	12,140	19,300
Incorporated Banks	na	71	118	160
Mortgage Banks	1	24	39	40
Private Bankers	642	na	1,386	1,221–1,800
Private note emitting banks	29–33	17	7	4
Other banks	na	na	na	236

Source: Own calculations based on data from Deutsche Bundesbank (1976, pp. 38, 56–67). The higher figure for the private banks in 1913 is a guesstimate reported in Ziegler and Wixforth (1994, p. 102).The estimate for the note emitting banks and the private banks in 1913, and the Sparkassen for 1861 is reported in Pohl (1982b, pp. 155, 160, 199), the number of private banks in 1900 is reported in Pohl (1982c, p. 262) and the number of Cooperative Banks in 1861 and 1885 is reported in Guinnane (2002, p. 89). These figures do not include branches, and they do not represent all incorporated banks as small incorporated banks were omitted from the central bank statistics.

banks, because of their special privilege.[166] State and municipal governments oversaw their own banks and sometimes emitted laws that served as guidelines for the operations of the *Sparkassen*. Entry to the banking sector was generally unrestricted and did not require government chartering, besides for mortgage banks. Merely the general norms applying to all corporations applied to incorporated banks. The federal government or the central bank had no say in the public banks' operation and neither did it have any tools to influence the public or the private banks' behavior besides the interest rate. A liberal laissez-faire approach to the banking system was taken, albeit a somewhat myopic one. On the one hand, anyone could enter the sector. On the other hand, the local and state governments engaged directly in the sector. They entered the banking sector as actors under the veil of 'public interest', with the added benefit that it helped to foster their private (fiscal) interests.[167]

Unlike the United States, there were generally no branching restrictions in Germany. Banks could operate throughout the country and diversify risks. At first, only some of the credit banks and the note emitting banks developed branches. Towards the beginning

[166] For the relevant laws see Reichsgesetzblatt (1899) and Reichsgesetzblatt (1875). For an overview of the supervisory structure see BArch R2501/6920, pp. 82–87. For the origins of the mortgage bank regulations see Pohl (1982c, pp. 297–301). Sometimes it is argued that the Cooperatives Act of 1899 also constitutes a regulation of the cooperative banks. However, it is not a specific regulation targeting cooperative banks per se. Rather it is a law establishing a new cooperative type of company. It is thus no more a piece of banking regulation than corporate law is. See Reichsgesetzblatt (1889).

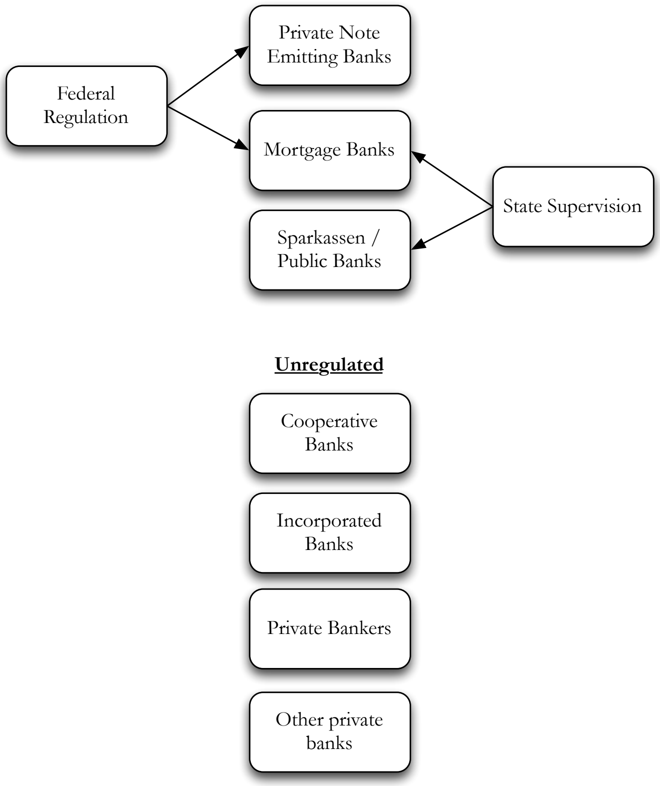
[167] For the fiscal interest of the government in the public banks see Pohl et al. (2005, pp. 55–58). For a schematic overview of the German regulatory arrangement see table 2.4 and figure 2.9 on pages 63 and 63, respectively.

Table 2.4: **The German banking sector and its regulatory arrangement in 1900 by balance sheet size**

Type of regulation	**Balance sheet size**
Federal regulation & state supervision	28%
Federal business restrictions	6%
Government owned	33%
Private and unregulated	33%

The only banks subject to federal regulation (but state supervision) were the mortgage banks. The private note emitting banks were a special case that were loosely regulated, because of their ability to emit currency notes. The *Sparkassen* and the regional government banks were not under any special federal government regulation and all other banks were under no specific regulation whatsoever. *Sources: Own estimate based on data from Burhop (2011b, pp. 168) and Deutsche Bundesbank (1976, p. 67).*

Figure 2.9: **Schematic overview of the regulatory arrangement of the German banking sector (1900–1930)**



Source: Own elaboration.

of the 20th century, large parent organizations evolved for the cooperative banks and the savings banks. These could even out capital needs amongst the associated cooperative banks and, consequently, the entire country. This was a crucial difference with respect to the American unit bank system that had developed after 1863.[168]

Additionally, Germany did have a central bank (the *Reichsbank*), which could help to overcome liquidity shortages, although its ability to help was restricted by its adherence to the gold standard. However, the *Reichsbank's* willingness to act as a lender of last resort developed into a problem for financial stability. Towards the beginning of the 20$^{\text{th}}$ century the major banks increasingly lowered their liquidity and capital provisions and thus became dependent on liquidity support from the *Reichsbank*. Especially at the end of every quarter the liquidity needs of the banks increased, only briefly, but dramatically. Indeed, the degree to which the *Reichsbank* was willing to act as a lender of last resort even surprised foreign commentators.[169] The explanation for the Reichsbank's willingness to act as a lenient lender of last resort, probably lay with the incentives the directors of each Reichsbank branch were confronted with. Their salary was linked to the volume and profitability of the discount business they were conducting. As a consequence their private incentive was to discount freely, with little regard as to systemic stability or the gold coverage ratio.[170] What made matter worse was that the *Reichsbank* thought that by strongly promoting the use of cashless transfers throughout the country it would alleviate the problem of the liquidity spikes. But by doing so it only augmented the banking system's ability to increase the money supply, thus achieving the opposite effect of what it intended in the first place.[171] Unlike in the United States, the stability of the banking system as a whole was never in acute danger up until the turn of the century. There were no major runs and neither did large numbers of banks have to restrict convertibility of deposits. Nevertheless, the adherence of the gold standard, coupled with the rapid rise of cashless transfer and the lowering of safety margins amongst the largest private credit banks, created significant vulnerabilities within the system.

[168] For the evolution of the parent organizations of the cooperative banks see Deumer (1933, pp. 254–256) and for the parent organizations of the *Sparkassen* system that evolved from 1908 onwards see Neumann (1933, pp. 339–341).

[169] See Borchardt (1976, pp. 46–47), Feldman (1993, pp. 29–30) and Habedank (1981, pp. 22–23). For the seasonal variation see also Seeger (1968, pp. 106–109). For the foreign commentators view on the lender of last resort practice of the *Reichsbank* see Borchardt (1976, p. 51).

[170] See Seeger (1968, pp. 111–112).

[171] See Seeger (1968, pp. 110–111) for the *Reichsbank's* thinking in this matter. See also Döring (1933, pp. 142–143) for an overview of the development of the cashless transfers before the First World War.

2.3.3 The first Banking Enquête (1906-1917)

These vulnerabilities of the German banking system came into plain sight when the San Francisco earthquake of 1906, that had ultimately caused a recession and financial crisis in the United States, forced the *Reichsbank* to drastically hike interest rates in order to maintain the gold coverage ratio. Fortunately, this period of financial stress was only relatively brief and it did not even lead to a recession.[172] However, just like in the United States, these turbulences created significant public irritation, as Germany had barely escaped a more serious financial crisis. Richard Koch, the president of the *Reichsbank*, was replaced and a banking commission, a so-called *Enquête*, was established by the German parliament upon the urging of the new *Reichsbank* president Rudolf von Havenstein. Havenstein then also presided over the commission.[173] Whereas previously the main concern of the regulatory discussion was to protect depositors, now the discussion had shifted towards ensuring the stability of the financial system.[174] In large measure, Havenstein was particularly concerned about 'war readiness' of the financial system, i.e. it's ability to withstand large political shocks in the face of an actual war of Germany with her imperial competitors. Thus, the liquidity dependence of the large credit banks' on the *Reichsbank* was his major concern.[175] At the same time Havenstein was confronted with the private interests of the directors of the *Reichsbank* branches, who did not want to reduce overall credit activity in the economy, as this would reduce their personal income.[176]

The core of the commission was dominated by representatives from the banking sector. Additionally, there were representatives from industry, a number of politicians and just two academics. A number of representatives from the state and federal government also attended the hearings, but their involvement was limited.[177] The bank inquiry was given the task to discuss six topics and to provide recommendations on each. Five of these were related to *Reichsbank*. In particular these addressed how to attract more gold, how to prevent another such rapid outflow of gold without the need to raise interest rates to

[172]See Borchardt (1976, p. 30) and Döring (1933, pp. 152–153). It was estimated that 3% of the private Credit banks had failed throughout Germany between 1903 and 1908. See Bankenenquete 1908/09 (1909b, p. 34).
[173]For the replacement of the president of the *Reichsbank in* see Borchardt (1976, p. 47).
[174]See also Bankenenquete 1908/09 (1910, pp. 4–5).
[175]See Habedank (1981, pp. 22–23).
[176]See Seeger (1968, pp. 112).
[177]At least 12 out of 25 of the core members were associated with the banking sector, four were associated with industry, and another eight held political office. Some of these held both political office and a position in banking or industry simultaneously. See Bankenenquete 1908/09 (1909a, pp. III-V) for the composition of the commission.

unacceptable levels, and how to prevent the recurring liquidity needs by the major banks at the end of each quarter. The sixth topic addressed the question of whether there was a need for actual government regulation of banks accepting deposits and if so, what this regulation should look like. Though the question of banking regulation was only one of six topics, it was the one that was dealt with in the most detail. The stenographic records for the first five topics fill 275 pages, whereas the stenographic records for the sixth topic alone, are 192 pages long. The formulation of the topic areas and the corresponding guiding questions, also reflect the commission's primary concern. The credit creation by the banking sector was to be reigned in, in such a way that liquidity needs would no longer spike at the end of each quarter. This was to be achieved by ensuring banks' liquidity and transparency, so that they would no longer resort to the *Reichsbank* as a lender of last resort as a matter of routine.[178]

Many different regulatory ideas were being debated during the inquiry, including the separation of investment and deposit banks, the establishment of a dedicated regulatory oversight agency or even a cap on bankers' wages and bonuses.[179] It was discussed, whether these ideas might be able to improve corporate governance within banks and thus foster the public interest by protecting the depositors of banks. However, depositors' safety was not the main concern of *Reichsbank* President Havenstein. He was almost exclusively concerned about the liquidity of the major banks as, to safeguard overall financial stability and 'war readiness'. Havenstein believed that it would be preferable to come to a gentlemen's agreement with the major banks, under which they would voluntarily increase their liquidity positions, rather than risking outright government legislation. Such government regulation might, after all, go well beyond the required measures and turn into a "Spanish boot", hampering the development of not only the major credit banks, but of all other banks, such as the public and cooperative banks, which had not constituted a threat to

[178]See Bankenenquete 1908/09 (1909a) and Bankenenquete 1908/09 (1909b) for the original stenographic reports and Bankenenquete 1908/09 (1910) for an assembly of the different opinions on the condition of the banking system as well as on the different reform proposals. The *Reichsbank's* compilation of proposals is not only based on the proceedings of the bank inquiry, but it also takes into account the public discussions with respect to banking regulation in the decades prior to the bank inquiry. See National Monetary Commission (1910a) and National Monetary Commission (1911) for the English translation, commissioned by the American National Monetary Commission in 1910/1911. In the following paragraphs, I shall mostly refer to the original German publications as information tends to get lost in the process of translation.

[179]The bankers' counter-argument used back then against limits to bonuses is still in use today: the bonuses were claimed to be crucial in attracting the best and the brightest. If it was not the best and the brightest working in the banks, surely the banking system would suffer serious crises as a result of incompetence (Bankenenquete 1908/09, 1909b, pp. 109–111). A summary of the various regulatory proposals put forward in the decades before and during the Enquête itself can be found in Bankenenquete 1908/09 (1910, pp. 4–62) or alternatively in Riesser (1911, pp. 546–599).

stability until then. Havenstein mentioned the "Spanish boot" only in 1914, but his line of thinking was consistent throughout this period. He prefered *Reichsbank*-led self-regulation over inflexible and unpredictable parliamentary legislation that could have undermined the *Reichsbank's* influence.[180]

Despite the discussion of a number of regulatory measures, the official opinion among the majority of commission members was that there would be no need to regulate. This recommendation by the commission is not surprising given the fact that the majority of commission members were affiliated with either banks or industry. They argued that the problems the German banking system had in the recent past were to some extent due to some moderate excesses, but especially due to a few 'black sheep'. These black sheep could easily be identified and weeded out. After all, it had not come to a breakdown of the financial system and only relatively small banks had failed up until that point. At the same time, the remaining bankers, in particular the large credit banks, promised to significantly increase the liquidity ratios of their banks.[181] Only few members of the enquiry were in favor of introducing regulation and supervision.[182] Opponents argued that government regulation and supervision of the banking sector was considered to be not only a sign of mistrust towards the banks, but also largely ineffective in preventing failures as American and other foreign experiences had supposedly shown. In Jakob Riesser's recommendations to the Enquête, he paraphrased a 1895 report by the U.S. Comptroller of the Currency, in which the Comptroller supposedly acknowledged that violations of the regulations by national banks were generally only revealed after banks had failed. Thus, the regulators depended to a large extent on the honesty and prudence of bankers.[183]

Regulatory measures were rejected unanimously by representatives from all the banking groups, including the Sparkassen and the Credit Cooperatives. Representatives of industry were also largely siding with the banks.[184] Additionally, the major banks pledged

[180] For Havenstein's view on government regulation see Feldman (1993, p. 31), Feldman (1995, p. 132), Habedank (1981, p. 23), Hardach (1995b, p. 918) and Zilch (1980, p. 239).

[181] The notable exception was the the failure of the rather large Leipziger Bank in 1901. But it was an isolated case of mis-investment and not a case systemic instability and the Reichsbank was able to deal with the fallout of this crisis effectively. See Borchardt (1976, p. 51) and The New York Times (1901).

[182] One of the academic members of the Enquête, Adolph Wagner, had argued in favor of increased regulation since the turn of the century. Jacob Riesser, a banker-turned academic, vehemently opposed regulation. The third academic member of the commission, Lexis, was also rather unenthusiastic about the merits of government supervision and regulation. See for example Bankenenquete 1908/09 (1909b, pp. 43–50, 87–90, 97–100, 121–122, 193–210). For Wagner's changing views see for example Riesser (1911, pp. 600–601, 777).

[183] See Bankenenquete 1908/09 (1909b, p. 210).

[184] See Bankenenquete 1908/09 (1910, pp. 5–7).

to cooperate with the *Reichsbank* in order to prevent future crises of the financial sector. The largest private credit banks preemptively agreed to publish their balance sheets bi-monthly, according to a common standard. This could give the *Reichsbank* better and up to date information on the status of the most important banks.[185] At the same time they promised to increase their liquidity ratios. It was a strategic move by the larger banks to signal cooperation with the *Reichsbank* in order to prevent the banking inquiry, and in particular *Reichsbank* President Havenstein, from proposing active government involvement in the sector. Furthermore, the Director of the Deutsche Bank even proposed the creation of a permanent advisory committee to the *Reichsbank* and the federal government to act as a mediator between the banking sector and the government. However this advisory committee was never established.[186] The large credit banks' signal of cooperation worked. The inquiry's chairman concluded the hearings of the banking commission with the words: *"My gentlemen, I hope and wish to all of you, that with us [i.e. in our country] there will be no need for legal measures [...]"*[187] This reflected Havenstein's stance at the time. If somehow possible federal government interference in the banking sector was to be avoided. And in parliament no majority could be found that favored to overrule the findings of the commission either, let alone within the executive government where the true power was.[188] Thus, the banking sector remained largely unregulated. This was in a stark contrast with the federal governments' stance in other industries such as railways, energy and telecommunications, which it also considered vital for 'war-readiness', and were it was much more active.

However, one part of the German banking sector, which saw its range of businesses expand in the wake of the bank inquiry were the public *Sparkassen*. Their competencies were increased as they were allowed to accept cashless deposits and to conduct cashless transfers, granting them increasingly the same rights as other private banks. Without this move, it was feared that the *Sparkassen* customers would migrate to the private credit banks, which offered better terms on the deposits, further increasing the concentration

[185] The mandatory end of year balance sheet statements were unreliable since banks typically engaged in window dressing. See Borchardt (1976, pp. 52–53), Nordhoff (1933a, pp. 245–246), Nordhoff (1933b, p. 481) and Seeger (1968, p. 113).

[186] The banks' agreement to publish their balance sheets was announced on October 12, 1908. See Bankenenquete 1908/09 (1910, pp. 169–173). See also Borchardt (1976, pp. 52–53) and Döring (1933, p. 153). For the proposal to establish a permanent advisory committee see for example Bankenenquete 1908/09 (1909b, pp. 182–183) and Paersch (1933, pp. 33–34).

[187] See Bankenenquete 1908/09 (1909b, p. 192).

[188] See Bankenenquete 1908/09 (1910, p. 7).

tendencies of the banking sector. Additionally, the *Sparkassen* were encouraged to form regional parent organizations, to facilitate cashless transactions and to even out capital and liquidity needs amongst its member banks – similar to the parent organizations previously formed by the Credit-Cooperatives. In part this was encouraged by the *Reichsbank* to achieve its goal of increasing cashless transfers, but it was also meant to provide a counterweight to the large private credit banks. Nevertheless, at that time, the different banking groups were not considered to be in competition with each other. Rather, it was thought of as a system of division of labor up until the first World War.[189]

The discussion with respect to the banking sector did not subside immediately in the aftermath of the banking commission. An increasing number of private credit banks agreed to publish bi-monthly balance sheet statements and in 1910 this practice was turned into law for all private incorporated credit banks, whose stocks were listed on the stock exchange. Previously, it was attempted to have this requirement passed as a voluntary measure by the German stock exchanges, but it was opposed outright by the Berlin stock market association (the *Berliner Börsenausssschuß*). Consequently the *Reichsbank* asked the legislators to act.[190]

The much more pressing issue of increasing the major credit banks liquidity ratios did not advance much after 1909, despite the pledge by the banks' to do so during the Enquête. During the commission most commission members agreed that a liquidity ratio of 10% would be desirable, given that the English banks tended to have liquidity ratios of approximately 15%. Yet in the subsequent years, the major private credit banks hardly increased their liquidity ratios above 5%. The self-regulation that was agreed upon during the banking commission did not work. The strong competition in the banking sector led to a situation where none of the major credit banks, were willing to increase their liquidity holdings as it would affect their profitability. Consequently, *Reichsbank* President Havestein continued to lean on the banks to increase their liquidity ratios, with little success at first.[191]

[189]See Born (1983, pp. 247–248), Hardach (1995b, p. 919, 922, 924) and Speer (1933, p. 179). Note that the *Sparkassen* were only allowed to maintain checkable deposits up to 10% of their total liabilities. See Neumann (1933, p. 336).

[190]See Nordhoff (1933a, p. 246). He makes no mention as to why the Berlin stock market association opposed this measure and why the *Reichsbank* did, after all, call for government intervention.

[191]See Döring (1933, p. 153), Nordhoff (1933a, pp. 246) and Seeger (1968, p. 113).

With the Moroccan Crisis of 1911, the liquidity question became acute once more and Havenstein then began to address the competitive pressures amongst the private credit banks, which he and the banks saw as the main obstacle towards higher liquidity ratios. Havenstein proposed the creation of an cartel, which the major Berlin credit banks were willing to comply with. Even a number of regional banks joined the cartel in the following years. Members within this association harmonized their short term interest rates and other bank charges.[192] An agreement between the *Reichsbank* and the major banks with respect to an increase in the liquidity ratios to 10% was reached at the end of 1912 – and only after Havenstein threatened the banks with the prospect of legislative measures. As part of the agreement, the banks were granted a period of three years during which they should increase the liquidity ratios to their target. Yet, with the outbreak of war, the agreement was abandoned again, leaving it in place for barely $1\frac{1}{2}$ years.[193]

In the weeks before the outbreak of the First World War, Havenstein launched yet another attempt at moral suasion to convince the major credit banks to increase their liquidity holdings to 10% of their assets. Once more Havenstein reiterated that he wanted to avoid government regulation at all cost. He was certain that if he proposed the introduction of a liquidity ratio for banks, proponents of regulation would use this opportunity to attempt to introduce much more far reaching changes, such as the separation of investment and deposit banks or other supervisory mechanisms. But he also pointed out that in both the United States and in the United Kingdom the prescribed or de facto liquidity ratios were significantly higher than in Germany. If liquidity ratios would not improve in Germany, he would have to recommend government legislation. The major credit banks, were largely receptive of Havenstein's message. While some pointed out improvements that had taken place and others highlighted that an immediate liquidity increase was not feasible as long as the public banks and the regional banks did not have to abide by it either, they understood that the *Reichsbank* could no longer stand by without any real

[192] Note that these 'general Agreements of the Associations of privater bankers and banks' (the *allgemeinen Abmachungen für Vereinigungen von Banken und Bankiers (AA.)* were not a strict cartel as the prices varied by region. Nevertheless, the associated banks cooperated with each other in setting the local rates, and the *Berliner Stempelvereinigung* served as a leader for the smaller associations. See Verhandlungen und Berichte des Unterausschusses für Geld- Kredit und Finanzwesen (V. Unterausschuß) (1930, pp. 25–28), Nordhoff (1933a, pp. 258–259), Walb (1933, p. 151) and Zilch (1980, p. 238).

[193] See Döring (1933, p. 153) and Nordhoff (1933a, pp. 253–254).

change happening. Further discussions were prevented by the onset of the war.[194] However, this meeting made it clear that in their differences in interests, the *Reichsbank* and the major Berlin banks had one thing in common, however: their antagonism towards involvement by parliament.[195] And in order to avoid involvement by parliament they had to cooperate – or at least give the impression of cooperation.[196] This close connection, which developed in these and the following years between the *Reichsbank* and the banking sector, and which was to safeguard the stability of the financial system, was later termed 'corporatist regulation'.[197]

2.3.4 Corporatist Regulation (1918-1930)

At the outset of the Weimar Republic, a heated debate took place as to the future structure of the German economy. This took place against the backdrop of socialist ideas that swept across Europe at that time. Both the socialization and nationalization of the banking system was being discussed in the so-called *Socialization Commissions* of 1919 and 1920. However, no recommendation for socialization of the banking system was given.[198] Indeed, the banking system – like much of the economy – remained almost unscathed by these post-war discussions.[199] The only piece of regulation affecting the banks was the establishment of government registration for corporate banking activity. This measure was introduced as an emergency decree in 1920, in an effort by the government to prevent capital flight. It was not motivated out of a need to regulate the operation of the banking sector as such.[200]

An important institutional change took place within the *Reichsbank* due to pressure by the Allies. In order to break with the *Reichsbank's* inflationary past and to regain the public's confidence in the institution, the bank law was amended and the gold standard

[194] The detailed minutes of this meeting are reprinted in Zilch (1980, pp. 237–250). See also Feldman (1995, pp. 132–133) and Habedank (1981, pp. 23–24).
[195] See Feldman (1993, p. 31).
[196] Similarly see Borchardt (1976, p. 53) and Riesser (1911, p. 781).
[197] See Hardach (1995b, p. 918).
[198] See Honold (1956, pp. 46–50). These government commissions consisted of both politicians and experts that were to study the feasibility of socialisation of parts of the German economy. A notable member in these commissions was Joseph Schumpeter. See Winkler (1993, pp. 46–47) for details.
[199] Winkler (1993, p. 46) attributes this to the opposition of the unions to socialization. This in turn was due to an agreement the unions reached with the employers that working hours would be reduced in return for a support of the existing economic structure. This practically forecluded any socialization attempts.
[200] See Reichsgesetzblatt (1920b). For the legislation on preventing capital flight until 1925 see Reichsgesetzblatt (1919, 1920a, 1921, 1922b,c, 1923, 1924b, 1925b).

was re-introduced after the currency was successfully stabilized.[201] Most importantly, the *Reichsbank* was made independent from direct German government influence. No longer was the government officially in charge of executive matters within the central bank. Additionally, the federal government's ability to obtain central bank credit was severely restricted. The governments ability to nominate the executive directors was revoked in the summer of 1924 as well. At the same time, it was attempted to also give the *Reichsbank* more independence vis-a-vis its shareholders. Furthermore, from 1924 until 1930, half of the supervisory board of the *Reichsbank* was composed of foreign representatives. [202]

After the death of the by then discredited President Havenstein in November 1923, Hjalmar Schacht, was installed as the new president of the *Reichsbank* by the German government in the spring of 1924.[203] This was remarkable, since the *Reichsbank* directorate favoured Karl Helfferich, a conservative politician of their kind, who was seen as the 'natural' successor to Havenstein. Schacht was the opposite of Helfferich. He had not studied law like the other directors. Instead, he had studied economics and he represented a new generation of bankers that (at that time) supported the idea of a republic and of international economic cooperation.This made him the preferred candidate for the Allies, the German government and possibly even the banking community. He was consequently first installed as the Currency Commissioner in charge of overseeing the stabilization of the currency, and later as the director of the *Reichsbank* despite the strong opposition of its directorate. In this position Schacht was instrumental in shaping the aforementioned institutional changes to the *Reichsbank*. Even more, he began to restructure the internal

[201] The gold standard had been abandoned at the outbreak of the war. For details on German government finance during and immediately after the war see Feldman (1993) and Haller (1976).

[202] For the relevant legislation see Reichsgesetzblatt (1922a) and Reichsgesetzblatt (1924a).The international supervision of the *Reichsbank* was introduced in accordance with the reparations settlement set out in the Dawes plan to provide a measure of control over German finances, to prevent another hyperinflation and to ensure regular reparation payments. These foreign representatives were removed from the supervisory board in the wake of the Young Plan in 1930. Note that the Central Committee that represented the *Reichsbank's* shareholders continued to exist, yet its powers were limited. See also Born (1967, pp. 28–29), James (1985, pp. 19–25) and Hennig (1930, pp. 13–33, 34). For the pressure of the Allies see especially Reinhardt (2000, pp. 85–132).

[203] Havenstein had been unwilling to put a halt to the government's inflationary finance during, but especially after the war, when the public-sector inflation turned into a private-sector hyperinflation. He believed the hyperinflation could only be stopped, once the Allies were willing to renegotiate the war reparations. See Feldman (1993, p. 833), Habedank (1981, p. 74–80), Holtfrerich (1986, pp. 155–172) and James (1985, pp. 19–20). Note that Schacht could be installed by the government, since the Bank Act amendement of 1922 still allowed the government to nominate the president against the opposition of the Reichsbank's directorate and Central Commission. With the amendement to the Bank Act in the Summer of 1924, the government's ability to nominate Reichsbank personnel was revoked. See the change from Reichsgesetzblatt (1922a, §27) to Reichsgesetzblatt (1924a, §6).

operations of the Reichsbank and its personnel according to his private interest, so that it could serve not merely as a central bank, but as an 'instrument of economic control'.[204]

The "Great Disorder", as the First World War and the subsequent hyperinflationary period was later called, became important for the future development of the banking sector for three main reasons.[205] First, during the hyperinflationary period the large credit banking banks resumed their concentration process and increased the number of branches significantly, covering much of the country. Throughout the inflation period most of the private credit banks remained highly profitable thanks to their speculation in the stock and in currency markets. The numbers employed in the four "D" banks quadrupled between 1913 and 1924. In part it was due to their expansion, but even more so due to the inflationary speculation. Indeed, it came to a boom in new private stock-market banks, whose sole business model consisted in taking advantage of the volatility in the stock markets.[206] Despite the relative success during the inflation years for many of the private credit banks, the capital of the largest credit banks was only about $\frac{1}{3}$ of what it had been back in 1913, once currency had been stabilized and brought back to the pre-war gold parity in 1924. But at least they had a significantly larger branch network to show for it.[207]

The second important development in the German banking sector was with the public banking sector. During the war, the Sparkassen and their parent organizations were increasingly used by the municipal and regional governments as a political tool to foster their private (fiscal) interest. This was nothing new, as prior to the war the Sparkassen were often obliged to invest a limited amount of their deposits in government paper. Their main investements prior to the war was, however, the mortage business.[208] During the

[204]See Feldman (1993, pp. 821–823, 832–835) and Reinhardt (2000, pp. 167–174). See also James (1985, pp. 19–21), especially for the paraphrase.

[205]For a general account of the inflation see Bresciani-Turroni (1937), Holtfrerich (1986), Müller (1933, pp. 190–206) or Pfleiderer (1976). For 'The Great Disorder' see Feldman (1993). See Born (1982, pp. 32–61), Grüger (1933, pp. 32–55) and Speer (1933) for overviews of the effects of the inflation on the German banking system.

[206]The four "D" banks were Deutsche Bank, Diskonto-Gesellschaft, Darmstädter Bank and Dresdner Bank. It is estimated that between 700 to 3000 private banks and credit banks were founded during the inflationary period. It is also estimated that approximately $\frac{1}{4}$ to $\frac{1}{3}$ of these banks closed their doors immediately after the currency stabilization. See Verhandlungen und Berichte des Unterausschusses für Geld- Kredit und Finanzwesen (V. Unterausschuß) (1930, pp. 12–17), Feldman (1993, p. 273), Grüger (1933, pp. 52–55), Hardach (1995b, pp. 924–925) and Bresciani-Turroni (1937, pp. 215–216).

[207]See Verhandlungen und Berichte des Unterausschusses für Geld- Kredit und Finanzwesen (V. Unterausschuß) (1930, p. 6).

[208]For the business model of the Sparkassen prior to the outbreak of the Second World War see especially Pohl et al. (2005, pp. 23–63) or Neumann (1933, pp. 336–337).

war, the need for both state and federal government finance increased enourmously and consequently the public banks were pushed to do their share. At the same time the federal government encouraged the growth of the Sparkassen system and fostered this development with the help of its war propaganda as well.[209] During the inflation the Sparkassen were forced to alter their business model in order to survive. Long-term investments, their main asset class, were no longer profitable. And as the profits of the public banks decreased, so did their ability to support the regional and municipal governments financially. Both the Association of the Sparkassen and the local governments consequently pushed the state governments, who set the general rules for the Sparkassen system, to liberalize the range of businesses the Sparkassen were allowed to conduct. By 1921 a restriction to short term deposits was lifted completely, and soon thereafter the Sparkassen's were liberated in their operations altogether. Some investment restrictions applied, but from the mid 1920s on they could engage in all types of banking activities if they so wished. They were allowed to become universal banks as well. While the expansion of the Sparkassen was ultimately driven by fiscal incentives of the local governments, the official explanation for the expansion of the Sparkassen into other fields of banking was generally touted as being due to the abandonment of the small- and medium scale depositors and creditors by the large credit banks during the inflation. Such a development may well have taken place, but the municipal government's fiscal interest was the main driver of the expansion.[210]

Last but not least, the German people had emerged impoverished and the business sector illiquid from the Great Disorder. On top of that, Germany had to service its war reparations. Consequently, the need for credit was immense. Much of the banks' capital had all but evaporated during the hyperinflation and the subsequent stabilization. The balance sheet size of the banking sector at the end of 1924 was barely 20% of what it had been at the end of 1913. Any source of credit was welcomed by the banks at that time. This included the relatively cheaper foreign credit, irrespective of its inherent dangers in

[209] See Verhandlungen und Berichte des Unterausschusses für Geld- Kredit und Finanzwesen (V. Unterausschuß) (1930, p. 40), Neumann (1933, p. 337), Pohl et al. (2005, pp. 65–66, 75–77).

[210] See Born (1967, pp. 26–28), and Neumann (1933, pp. 337–339). For the liberalization of the Sparkassen see also Pohl et al. (2005, pp. 79–81). The view of the Sparkassen only extending their customer base because of the abandonment of the large credit banks was also given as the official explanation in Verhandlungen und Berichte des Unterausschusses für Geld- Kredit und Finanzwesen (V. Unterausschuß) (1930, p. 41). This was a commission that studied the demand and supply conditions within the economy. The banking sector was one of several sectors analyzed. James (1986, pp. 39–41) also reports that the share of taxation that went to the federal government increased with the new Weimar constitution. Thus this may have been another important driver for the regional governments to encourage the growth of the public banking sector.

a system of fixed exchange rates such as the gold standard. And indeed, by the end of 1925 the banking sectors balance sheet size had already recovered to approximately 35% of its pre-war level.[211] Furthermore, there is significant evidence that German politicians, welcomed the foreign credit as part of a long-term strategy to rid itself of the reparations problem or at least to commercialize the reparations debt.[212] While the *Reichsbank* under Schacht was critical of foreign short-term loans, it encouraged the intake of long-term loans as it saw in it an essential role for the reconstruction of the German economy. The *Reichsbank* tried to brake the intake of short-term foreign credit, but there was not much that it could do other than moral suasion.[213]

Schacht was, however, particularly critical of foreign loans to German governments as he thought that this constituted undesirable competition for the private sector, whom he regarded as more apt to invest the money productively. Consequently he tried to gather political support to do find a way to restrict the government's foreign credit intake. Eventually, it managed to come to an agreement with the German federal and state governments to 'control' the German governments' external borrowing by establishing an Advisory Office for Foreign credit (the *Beratungsstelle für Auslandskredite*), which was to advise on the desirability of the emission of long-term foreign government loans. Short-term foreign loans to governments were only supervised by the Office for foreign Credit at the end of 1930. Even given these nominal restrictions, whatever credit was not directly given to the governments found its way into state and municipal coffers on indirect ways. Given the *Reichsbank's* inability to prevent this development, President Schacht eventually began warning foreign investors publicly of the dangers of giving loans to the German municipal and state governments.[214] Furthermore, borrowing by the private sector was largely unchecked, even though the Economics Ministry (the *Reichswirtschaftsministerium*) attempted to install a similar controlling body as the one for the public sector. However,

[211]See Born (1983, pp. 245–248) and Müller (1933, pp. 198 & 212-214). For the data on the balance sheet sizes see Deutsche Bundesbank (1976, p. 74). See also Bissing (1933).

[212]See Fischer (1933, pp. 519–520), Hardach (1976, pp. 142–143) and Ritschl (2002, p. 125–127).

[213]See Habedank (1981, pp. 116–117), Hardach (1976, pp. 55–56, 60) and Nordhoff (1933a, pp. 254–255).

[214]SeeHardach (1976, pp. 55–57), James (1986, pp. 94–96) and Tewaag (1933, pp. 124–125). The Advisory Office was composed of an equal number of representatives of the German federal government, the states and only one representative of the *Reichsbank*. Thus, the power to limit foreign credit to the government was with the federal and state governments, and not with the *Reichsbank*. Furthermore, the municipalities were not separately represented and were thus often discriminated against, making them more dependent on their 'accessible' source of finance, the Sparkassen.

this measure did not find the support of the *Reichsbank* and as ultimately successfully prevented in cooperation with the main business associations.[215] Consequently, the German economy experienced a boom on the back of borrowed (hot) money, most of which was used for the payment of the reparations or internal consumption, rather than productive investment.[216]

After the First World War, the German territory was reduced significantly in size. Because of this and because of additional growth in the banking sector, the number of banks per capita had grown substantially since the outbreak of the war. If branches are taken into account, the density of banking offices per inhabitants in Germany may well have been almost twice the density in the United States.[217] Consequently, the issue of competition became increasingly important during the 1920s. However, it was no longer just the competition amongst the private credit banks themselves that was a source of concern for the *Reichsbank*. In an increasing measure it was the competition amongst the three main banking groups: the *Sparkassen* on the one side, who aggressively entered new markets, and the credit cooperatives and the private credit banks on the other, who felt threatened by these state sponsored actors.[218] The private sector banks criticized the public banks for their incompetence and fraudulent practices, and that they were invading the private banks' traditional lines of business by abusing their status as public institutions. Indeed, there were reports that the *Sparkassen* aggressively attempted to acquire new customers by directly making reference to the implicit government guarantee, such as by using their forms on letterhead of the local government, or that they distributed savings account booklets for free. Last but not least, the private credit banks pressed for the abolition of the tax exemption of the public banking system. The *Sparkassen* in turn argued that their expansion was a legitimate challenge to the concentrations amongst the private credit banks, i.e. they were an essential counterweight to the great credit banks that threatened to monopolize the banking sector. The public banks were merely fostering

[215]See Hardach (1976, pp. 57–58) for the failed proposal of the Economics Ministry.

[216]Most of this money came from the United States. For an introduction into the credit scheme and for an explanation why foreign creditors were so eager to lend money to Germany despite her large reparation requirements see for example Ritschl (2012) or Tooze (2007, pp. 24–26). For the spend-thrift of the municipal governments see for example Balderston (1993, pp. 250–265), Feldman (1984, pp. 188–189), James (1986, pp. 85–101) or Pohl et al. (2005, p. 95).

[217]See figures 2.11 and 2.6(d) on pages 82 and 42, respectively. If branches are taken into account there was approximately one banking office per 1,927 inhabitants in Germany in 1925. For German population, bank and branch figures in 1925 see Deutsche Bundesbank (1976, pp. 7, 122). See also the overview of the German banking system between 1913 and 1929 in figure 2.10 on page 77.

[218]See for example Walb (1933, pp. 167–173).

the public interest by serving a niche, which had been abandoned by the large credit banks. To make matters more complex still, a number of foreign banks became active in Germany from 1927 onwards, fighting for their share in the market.[219]

FIGURE 2.10: **The key developments of the German banking sector between 1913 and 1929**

	Total Assets (mio. RM)			**No. of Banks**		
Bank type	**1913**	**1925**	**1929**	**1913**	**1925**	**1929**
All banks (excl. Private Bankers)	*66,388*	*22,936*	*60,142*	20,960	22,900	23,452
Large Credit Banks	8,391	6,141	13,765	9	8	6
Provincial Credit Banks	6,266	1,318	1,971	104	67	60
Other Credit Banks	na	na	2,346	na	na	na
Private Bankers	na	na	na	1,221	1,406	1,100
Zentralkassen	684	1,911	1,498	47	43	45
Credit Cooperatives	5,087	1,726	4,600	17,323	19,615	20,260
Mortgage banks	13,871	1,644	7,738	43	47	50
Large Public Banks	2,906	3,305	8,634	13	38	42
Sparkassen	20,802	2,875	12,149	3,133	2,622	2,609
Other banks	8,381	4,016	7,441	na	na	na

(a) Total Assets & Number of Banks

	No. of banking offices		
Bank type	**1913**	**1925**	**1929**
Large Credit Banks	550	1,230	1,220
Provincial and Local Credit Banks	1,335	1,296	1,045
Other Credit Banks	36	182	221
Private Bankers	1,377	1,612	1,270
All Credit Cooperatives (incl. Zentralkassen)	18,544	22,400	21,968
Mortgage banks	na	na	na
Large Govt. Banks	46	294	310
Sparkassen	na	5,145	6,133

(b) Number of banks and full service branches (not including acceptance and payment offices)

Note that the availability of German bank data for the 1920s is patchy and of fair quality. The numbers may not may add up and the definition between the bank types may not be consistent over time. Thus, these tables do not necessarily represent a fully accurate picture of the banking sector. The interested reader is strongly advised to refer to the original data source for details. *Source: Own elaboration based on data extracted from Deutsche Bundesbank (1976, pp. 63, 69–122).*

[219]See Neumann (1933, p. 340) and especially the two memoranda written in February and April of 1926 by the Association of the Credit Banks and Private Bankers (the *Centralverband des Deutschen Bank- und Bankiergewerbes* and the *Sparkassen* Association (the *Deutscher Sparkassen- und Giroverband*), found in BArch R2501/6464, pp. 395–444. For the aggressive methods of the *Sparkassen* see Verhandlungen und Berichte des Unterausschusses für Geld- Kredit und Finanzwesen (V. Unterausschuß) (1930, p. 40–41) and the *Reichsbank* memorandum *Vorarbeiten der Volkswirtschaftlichen und Statistischen Abteilung der Reichsbank vom 4. November 1933: Konkurrenzmethoden der Banken*, found in BArch R2501/6913, pp. 27–36. For the conflict over taxation see Pohl et al. (2005, pp. 93–95) and for the foreign banks entering the German marketplace see especially Balderston (1991, pp. 575–577) and Hardach (1984, p. 214). Hardach (1995b, p. 209) also points out that the *Reichsbank* did to some extend compete with the commercial banks by directly discounting bills of the largest industrial companies.

Ever since the outbreak of the First World War the practice of requiring banks to publish their balance sheet on a bi-monthly basis had been suspended. After the inflation, Schacht urged the banks to re-establish this practice and he asked the government to formally establish this requirement, which it did in early 1925.[220] A few months thereafter, the parliament also passed an Investment and Security and Deposit Bank Act that was meant to protect small-scale depositors and to prevent further growth in the banking sector. It is possible that this law also played an important role in ensuring the foreign creditors' trust in the German banking system.[221] For the first time in German banking history, the German government had created actual restrictions to the creation of new banks. Not all banks were affected in equal measure, however. Not much changed for the public banks, as the set-up of a new one was subject to a permit of the relevant state agencies. New credit cooperatives could also be created, as long as they were subject to a specific audit scheme, and as long they only conducted credit business with members of the credit cooperative. Anyone could also become a private banker as long as he could demonstrate five years of experience in banking. The restriction was binding for the private incorporated banks, however. From now on, new banks required the joint permission of both a relevant state agency and of the Economics ministry. This chartering requirement for private incorporated banks was not just a formality. Both the state and federal government could deny an application if the bank did not meet basic requirements such as sufficient capital or if the proposed management was not considered to be experienced or trustworthy. Additionally, they could deny the issuance of a new charter, if it did not deem it sensible in terms of the general well-being of the economy.[222]

The act required periodic renewal by parliament. It was renewed twice in 1926 and 1927, but was let to expire in 1929 as no consensus could be reached on an amendment to the act. Consequently, entry to the German banking sector was entirely free once more. There were a number of perceived issues with the existing Security and Deposit Bank Act, which had caused a call for revision. One was that it left too many gaps for private bankers and credit cooperatives. Another was that no provision had been made to provide the necessary resources to check each and every application. It seems

[220] See Nordhoff (1933a, p. 248).

[221] For the potential role of this law in international negotiations see the *"Entwurf eines Gesetzes über Depot- und Depositengeschäft*, from 28.04.1930, pp. 6-20, found in BArch R3101/15566.

[222] See Reichsgesetzblatt (1925a).

that during the law's duration the majority of charters requested were merely rubber-stamped. Since Germany had just entered a recession at the end of the 1920s, there was little willingness to increase government bureaucracy amidst a general environment of austerity. Also, the law had become dispensable as a political tool to signal the German banking sectors solidity to foreigners. Furthermore, the private banking sector and the industry pressed the government to lift the restrictions on the private credit banks. At the same time they encouraged the federal government to restrain the expansion of the public bank system. They wanted a provision included, which only allowed for the establishment of new public banks if there was proof that the private banks had failed to provide the necessary banking services.[223] The Economics Ministry seemed willing to accede in part to the demands of the private banking sector and of industry, in part also because it feared American-style regulatory arbitrage. Consequently it pushed for a uniform concession requirements throughout the country. This ran into the opposition of the German states, who wanted to retain their say over the chartering of public banks in their state and they did not want to cede power to a central institution.[224]

It never came to a vote in both chambers of parliament on the same bill. At first this was due to the disagreements between the state and federal governments and later due to the rapidly changing governments as the German economy. It had experienced a sudden stop in foreign credit inflows and entered a deflationary tailspin that destabilized the German government at both the federal and state levels. This also lead to a marked deterioration in the relationship between the German states and the federal government. Even so, the amended law would have meant less, not more, regulation for the banks. With respect to the previous 1925 act, the new proposals would have abolished the need for government consent. Instead new banks could simply take up operations. They would only have had to notify the relevant government authority, which could then object if it found fault with the capital available or the suitability of the individuals.[225]

[223]See for example BArch R3101/15564, Memo by Korsch, *Besprechung betreffend das Depositengesetz im Reichswirtschaftsministerium*, from 03.07.1929. See also BArch R3101/15566, *"Bericht des Arbeitsausschusses zu Beratung des Entwurfs eines Gesetzes über Depot- und Depositengeschäfte*, from 02.07.1930.

[224]See BArch R3101/15566, Statement by the Economics Ministry from 02.07.1930.

[225]See BArch R3101/15566, Motivation of the *"Entwurf eines Gesetzes über Depot- und Depositengeschäft*, from 28.04.1930, as well as the *"Bericht des Arbeitsausschusses zu Beratung des Entwurfs eines Gesetzes über Depot- und Depositengeschäfte* from 02.07.1930. See also BArch R3101/15567, *Entwurf eines Gesetzes über Depot- und Depositengeschäfte*, from 01.06.1931. James (1986, pp. 73–85) reports major fiscal conflicts taking place at the onset of the Great Depression between the states and the federal government. For the political instability see also Born (1967, pp. 39–54) or James (1986, pp. 25–38).

In the second half of the 1920s, the *Reichsbank* acted as a proxy for the government, to reign in the, what it perceived to be, excessive competition in the banking sector.[226] The *Reichsbank* tried to do so using the corporatist method of regulation, i.e. by attempting to come to an agreement between the various banking associations. Ideally, it wanted to bring about the return of the pre-1913 specialization, when each banking group focused on a special segment of the market. This soon proved illusive and the *Reichsbank* subsequently attempted to negotiate voluntary restrictions to competition. In 1928, it brokered a non-binding agreement (the *Wettbewerbsabkommen*) between the major banking associations that restricted advertising practices and created arbitration boards throughout the country to solve conflicts between the banking groups. While the arbitration boards seemed to have worked reasonably well, the competition for clients continued with a similar intensity until the worsening recession forced the banks to reduce their leverage.[227]

Similarly, as of 1924 the *Reichsbank* attempted to persuade the banks to lower their interest rates and to harmonize them throughout the country, in an effort to restrict competition and to improve the transmission of its monetary policy to ultimately support German industry. After the First World War, the *Berliner Stempelvereinigung* continued to act as an association that sought to harmonize short term interest rates amongst its member institutions. Moreover, its interest rate decisions provided the benchmark for another 68–100 other regional private banking associations throughout the country. The major credit banks acted as an enforcer of the interest rates in the smaller associations via their branch network. But even so, long-term interest rate competition was unrestricted. Additionally, both the credit cooperatives and the public banks were not affiliated to these associations, but they tended to have similar harmonization measures amongst their members. The *Reichsbank* attempted to orchestrate a coordinated effort to both harmonize and reduce interest rates across all banking segments. It only succeeded to do so after much pressure in early 1931, when a binding agreement (*Zinsabkommen*) by the major banking associations was announced. This agreement attempted to reduce not only interest rates,

[226] In this context it is interesting to note that the Reichsbank, especially under Schacht, generally acted as if it was part of the German government, and it often attempted to influence government policy. At the same time it never felt the need to comply with the elected government's line and it made sure to safeguard its independence. See Reinhardt (2000, pp. 181–182, 197–199, 229–232).

[227] See Verhandlungen und Berichte des Unterausschusses für Geld- Kredit und Finanzwesen (V. Unterausschuß) (1930, p. 41), Pohl et al. (2005, pp. 97–98), Walb (1933, pp. 151–152) and BArch R2501/6913, *Vorarbeiten der Volkswirtschaftlichen und Statistischen Abteilung der Reichsbank vom 4. November 1933: Konkurrenzmethoden der Banken.*

but also the banks' interest rate marginsen, which made it unpopular with all banking groups as they saw their profitability affected.[228]

By the beginning of the 1930s, neither the *Reichsbank* nor the federal government had obtained any additional tools to regulate or supervise the banking sector.[229] There was no major discernible push by the federal or the state governments to obtain these tools, either. What little restriction to market entry was introduced in 1925 was largely ineffective and was soon abandoned amidst pressure from the private banking associations. Regulation of the banking sector effectively existed only via the moderating influence of the *Reichsbank* that attempted to to so primarily via moral suasion. The threat of increased government regulation was rarely used. If anything it threatened to withold *Reichsbank* funding. Furthermore, in 1929, the *Reichsbank's* charismatic President Schacht had resigned in a public conflict with the German government over the government's fiscal and reparation policy, in which he broke with many of his former Allies. He was replaced by the less charismatic Hans Luther, who quickly developed difficulties with his fellow directors at the Reichsbank, most of which had been handpicked by Schacht and who remained loyal to him.[230] Thus, by the onset of the German financial crisis of 1931, the German banking sector was – in terms of its regulatory structure – either government owned or private and officially unregulated. Merely the mortgage banks were subject to actual regulation and supervision, but their importance had shrunk significantly with respect to the pre-war period, whereas the large credit banks and the public banking system could expand their market share.[231]

2.3.5 Compelled to regulate (1931-1932)

The German Ponzi scheme fuelled by foreign loans came to sudden stop with the onset of the Great Depression. The German economy found itself in a deflationary spiral due to a reparations cum balance of payments crisis, not least due the large amount of

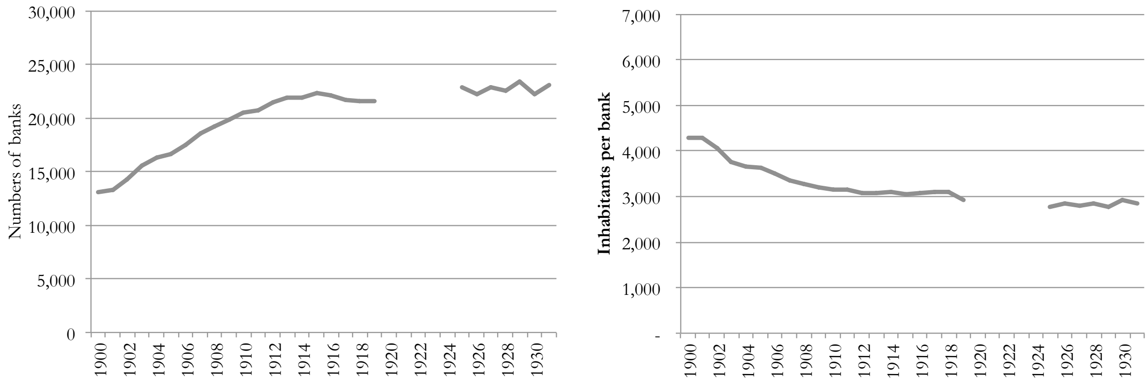
[228] See Verhandlungen und Berichte des Unterausschusses für Geld- Kredit und Finanzwesen (V. Unterausschuß) (1930, pp. 25–28, 175) and Walb (1933, pp. 151). See also BArch R3101/15491, Letter from the Reichsbank to the Ecnomics Ministry, No. I 10349, from 30.09.1930 and BArch R2501/475, Berliner Tagesblatt, article no. 437, from 15.09.1925, *Overtüre zum Bankiertag. Das beherrschende Problem: Die Frage der Zinssenkung.*

[229] The subsequent amendments to the Bank Act of 1924 in 1926 and 1930 contained only provisions which affected the *Reichsbank*. See Reichsgesetzblatt (1924a, 1926, 1930).

[230] See Reinhardt (2000, pp. 197–235).

[231] See figure 2.12 on page 83 for an overview of the proportion of banking assets under federal government control. See figure 2.10 on page 77 for the evolution of the German banking system in the 1920s.

FIGURE 2.11: **Evolution of the German banking Sector from 1900 until 1931**



(a) Total number of banks (b) Number of inhabitants per bank

Sources: Own estimate based on data from Deutsche Bundesbank (1976, pp. 6, 55–67, 74, 112, 121). All figures do not include branches. There is no data available for the hyper-inflationary period following World War I.

short term foreign loans taken in by both the banking sector and the regional and local governments.[232] By early 1931, the German government resorted to passing much of its legislation via emergency decrees.[233] Again, the issue of restricting entry into the banking sector was picked up inside the government. However, the government and the *Reichsbank* were extremely cautious. They feared that introducing any major changes via an emergency decree, would lead to a loss in confidence of foreign creditors and to a full blown run on the German banking system – up until that point there had not yet been a wave of bank failures[234]

No major changes to the regulation of the German banking system were in the pipeline prior to the financial crisis in the summer of 1931. While there were tentative attempts by the *Reichsbank* and the parliament to restrict competition in the banking sector, there was no intent to install a dedicated regulatory system of the banking sector, let alone the intent to create central regulatory and supervisory institutions for the whole country. This changed radically after a nationwide bank-run and the failure of two of the largest banks (the Danat and the Dresdner Bank), when the government had to declare a banking holiday. It found itself compelled to take a major stake in the largest credit banks of the

[232]See Born (1967, pp. 15–19), Hardach (1976, pp. 126–131), Ritschl and Sarferaz (2010) or Schnabel (2004).
[233]Indeed, it is sometimes argued that the Weimar democracy already de-facto disappeared in 1930, and only disappeared de-jure with the rise to power of Hitler. See Bracher (1973, pp. 216–227).
[234]See the minutes of a meeting in the Reichskanzlei from the 30.05.1931, in BArch R3101/15567.

Figure 2.12: **The German banking sector and its regulatory arrangement by balance sheet size in 1930**

Bank type	**Balance sheet size**
Pure Mortgage Banks	10.0%
Sparkassen	20.6%
Govt. Regional Banks/Girozentralen/Landesbanken	14.7%
Other (special) government banks	7.5%
Credit Cooperatives	7.2%
Zentralkassen	2.2%
Private Bankers	5.3%
Large Credit Banks	19.4%
Other banks	13.2%

(a) Percentage of total assets

Type of Regulation	**Balance sheet size**
Federal regulation & state supervision	10%
Government owned	43%
Private and unregulated	47%

(b) Regulatory Responsibility

The federal government's direct influence over the banking sector was minimal in 1930. Virtually all of the government owned banks were in the hands of either the states, municipalities, counties or cities. *Source: Own elaboration based on data from Deutsche Bundesbank (1976, p. 121).*

country in order to prevent an even greater financial disaster. Many of the directors at the credit banks receiving government capital injections were eventually sacked and government caretakers appointed.[235] Furthermore, federal money was used not only for the largest credit banks, but also to prop up the public *Sparkassen* system as well.[236]

From that moment on, the issue of banking regulation was on the top of the agenda, both inside the government and amongst the public. The question was no longer, whether a comprehensive regulatory system would be introduced, but what form it would take.

[235]Nearly all of the directors at Danat Bank and Dresdner Bank were eventually dismissed from their positions and over a third were removed at both Deutsche Bank and Commerzbank. See Born (1967, pp. 170–172) and James (1985, pp. 209-210). Hardach (1984, p. 227) points out that the government subsequently never intervened in day to day bank management, and that from the outset it was the government's intention to merely re-restructure the banks and then to re-privatize them.

[236]It also provided some guarantees and funds to the cooperative banking system. For figures on the extent of the support to the banking system by both the *Reichsbank* and the federal government by 1932, see Hasse (1933, pp. 87–88). The major source of instability in the Sparkassen sector were the *Landesbanken* of the *Rheinprovinz* and the *Provinz Westfalen*, which had been particularly active in lending to municipalities, which in turn failed to repay their loans. See Born (1967, pp. 97–98, 163–164), Pohl et al. (2005, pp. 142–143), BArch R43 I/1450, pp. 213 – 219, *Ministerbesprechung vom 6. Juli 1931, 11 Uhr* and pp. 227–232, *Ministerbesprechung vom 6. Juli 1931, 17 Uhr*. For details on the emergency steps taken by the government during the bank holiday in the Summer of 1931 to stabilize the banking system see Balderston (1991, pp. 596–599), Born (1967, pp. 110–152) and Hasse (1933). An important measure was the introduction of capital controls, and the negotiation of standstill agreements, which effectively took Germany of the gold standard. This in turn increased the scope of the *Reichsbank* to act as a lender of last resort. See also Hardach (1995b, pp. 930-932).

On one hand, the Chancellor Brüning was furious about the large banks that were too big to fail, which had privatized their gains, but now had their losses socialized. On the other hand, he felt that he was unable to justify the rescue of the largest universal banks and the public *Sparkassen* system to its voters, if it did not establish some kind of control mechanism. He consequently put the Economics Ministry in charge of drafting an emergency decree to establish supervision over the banking sector.[237]

A number of discussions on this matter took place in August and September of 1931. The top-level meetings were closed to the public, but a handful of representatives from the private banking sector, agriculture, industry and politics were invited by Chancellor Brüning to act as part of an advisory committee. However he intended the committee to serve as a fig-leaf for parliament, to signal that all the relevant interests had been heard.[238] Several proposals were floated behind closed doors, including the separation of deposit and investment banks, increased regulation by the *Reichsbank*, a temporary regulatory agency or even a dedicated regulatory agency. The separation of investment and deposit banks was discarded relatively quickly, since this was a much more comprehensive reform to the banking structure, than Brüning was prepared to do at the moment. His priority lay on returning the public's trust in the system and to provide a measure of federal government supervision over the banking sector. Moreover, such a move would cause a major political upheaval, in particular from the private banking lobby, something he wanted to avoid.[239]

[237]See the various meetings within the Chancellory in the Summer of 1931, such as BArch R43 I /1450, pp. 423-429, *Sitzung des Wirtschaftsausschusses des Reichskabinetts vom 15. Juli 1931, 12 Uhr*, pp. 557-564, *Sitzung des Wirtschaftsausschusses der Reichsregierung vom 27. Juli 1931*, BArch R43 I/1451, pp. 17-31, *Ministerbesprechung vom 3. August 1931, 16 Uhr* or pp. 419-432, *Sitzung des Wirtschaftsausschusses der Reichsregierung vom 22. August 1931, 10 Uhr*. See also Luther (1964, pp. 228–238).

[238]The committe consisted of: Dr. Schmitz from IG Farben; von Flemming the president of the Agriculture Association in Pomerania; Prof. Stein for the Credit Cooperatives; Reinhart as the Director of the Commerzbank, Robert Pferdmenges as an expert on Industry and Private Bankers; Rudolf Hilferding, Dernburg Adolf Weber as subject experts; and Albert Hackelsberger as a representative from the konservative Zentrumspartei. For Brüning's thoughts on the committee and the composition of the committee (Alfred Weber was only added later), see BArch, R43 I/1451, pp. 325–340, *Ministerbesprechung vom 14. August 1931, 18 Uhr*. Note that the parliament was adjourned during the summer until the 26. of September. See also Born (1967, p. 155–156), who notes that this committee was probably selected so as to represent a majority of the political spectrum represented in parliament (excluding the National Socialist German Worker's Party (NSDAP), commonly known as the Nazi party, and the Communist party), rather than representing the most knowledgable individuals.

[239]See BArch R43 I/1451, pp. 17-31, *Ministerbesprechung vom 3. August 1931, 16 Uhr*, pp. 325–340, *Ministerbesprechung vom 14. August 1931, 18 Uhr*, pp. 397–409, *Sitzung des Wirtschaftsausschusses der Reichsregierung vom 18. August 1931, 15 Uhr*, pp. 419–432, *Sitzung des Wirtschaftsausschusses der Reichsregierung vom 22. August 1931, 10 Uhr*, pp. 511-520, *Sitzung des Wirtschaftsausschusses der Reichsregierung vom 29. August 1931, 10 Uhr*. See also BArch R43 I/2373, pp. 1121–1132, *Besprechung mit Vertretern des Reichsverbands der deutschen Industrie vom 18. September 1931* in which Brüning declares to the industry that he does not want to risk political upheavals. See BArch R2501/1182 pp. 1–200 for newspaper clippings that document the intense public debate that accompanied the governmental discussions.

Interestingly, it was *Reichsbank* president Luther who was of the opinion that a separation of deposit and investment banks was highly desirable and that even the best supervision of banks would not have been able to prevent the banking crisis. It is not clear whether Luther sincerely believed in the separation or whether it was meant to punish the major credit banks. The banks felt betrayed by the *Luther's* adherences to the law and consequently the Gold standard, which had prevented him from acting as a lender of last resort as the gold reserves dwindled. The private banks consequently tried to pressure the government into dismissing Luther at the outset of the crisis – even though the government no longer had the legal power to dismiss the president of the *Reichsbank* since 1924.[240] It is clear however, that Luther wanted to prevent the introduction of an independent supervisory agency as he saw it as a challenge to the *Reichsbank's* political standing. The support of the separation of investment and deposit banking might have been part of his defense.[241] Indeed, Luther was the only high-level official strongly pushing for the serparation of investment and deposit banks. In turn, the *Reichsbank* was criticized by members of the Brüning cabinett and some of the political members of the advisory committee. They suggested that the *Reichsbank's* directorate needed reform. In their view it had become too close to the banks and it had repeatedly undermined the policies of the government in the recent months. Brüning, who had a good working relationship with *Reichsbank* president Luther, acknowledged that it would indeed be desirable to increase the political influence on the *Reichsbank*, but that this would currently not be viable as it would worsen Germany's relationship with its foreign creditors.[242]

The attempts by the representatives of the private banking sector and by the *Reichsbank* to prevent the introduction of a supervisory agency were unsuccessful. After all, this decision had been taken already well before they were invited as act as advisers. Consequently, they changed their strategy and henceforth pushed for the regulatory agency to be as close as possible to the *Reichsbank*. And indeed, the most most controversial arguments developed around which parts of the banking system were to be regulated and who would be in charge of the supervisory agency: whether it should be the *Reichsbank* or the

[240] See BArch R43 I/1451, pp. 397–409, *Sitzung des Wirtschaftsausschusses der Reichsregierung vom 18. August 1931, 15 Uhr*. For the banks' futile attempt to have Luther dismissed see Born (1967, pp. 110–113) and Reinhardt (2000, pp. 255–258).

[241] See also Born (1967, pp. 158–159).

[242] See for example BArch R43 I/1451, pp. 325–340, *Ministerbesprechung vom 14. August 1931, 18 Uhr*, pp. 397–409 and Dernburg's comment in BArch R43 I/1451, pp. 511-520, *Sitzung des Wirtschaftsausschusses der Reichsregierung vom 29. August 1931, 10 Uhr*. See Reinhardt (2000, pp. 235–246) for the working relationship between Brüning and the *Reichsbank*.

central government via a *Bankenamt*. On one hand, the *Reichsbank* was the institution with the most expertise and it would give the regulatory agency the necessary authority, without assuming outright responsibility for the individual actions of banks. This was a lesson policymakers had drawn from Germany's experience with regulating its insurance sector. One of the principal insurance companies, the FAVAG, had failed at the outset of the Great Depression. Although regulation of insurance companies was a centralized arrangement, the failure was attributed to the ineffectiveness of the independent regulator, which lacked sufficient authority and credibility.[243] On the other hand, the *Reichsbank* was also independent of the government and had allegedly counteracted the government's policy on several occasions. Thus, it was feared that if it were given complete control over regulatory matters the government might be excluded from banking policy altogether. And this seemed unacceptable, now that the government had recapitalized major parts of the banking system. Furthermore, the *Reichsbank* could easily find itself in a situation in which it would have to deal with two potentially conflicting policy goals: monetary and financial stability.[244]

Both Chancellor Brüning and acting Economic Minister Trendelenburg saw the main cause of the banking crisis not in some structural defect of the banking system, but they believed it was a problem of corporate governance and hence there was no need for heavy-handed regulation that a full-fledged government-run *Bankenamt* would entail. After all, that only increased the government's responsibility for developments within the banking sector. And that would tie developments in the banking sector directly to the government, unless it could use the *Reichsbank* as a shield. The only structural change in the banking sector policymakers saw as an absolute necessity was with the *Sparkassen*, who were under the direct influence of the respective municipal politicians. Furthermore, despite their disagreements with Luther and the *Reichsbank*, Brüning wanted to minimize future conflict. As a consequence, the Economics Ministry was instructed at the end of August to henceforth prepare the emergency decree, with which banking supervision was supposed to be introduced, in agreement with the *Reichsbank*. This allowed Luther to press for a

[243] See BArch R43 I/1541, pp. 397–409, *Sitzung des Wirtschaftsausschusses der Reichsregierung vom 18. August 1931, 15 Uhr* and the article *"Unter Kuratel. Die Bankenaufsicht"* by Bruno Saekel in the Berliner Tageblatt, Nr. 438 from 17.09.1931, found in BArch R2501/1182, p. 200.

[244] See BArch R43 I/1451, pp. 397–409, *Sitzung des Wirtschaftsausschusses der Reichsregierung vom 18. August 1931, 15 Uhr* and pp. 511-520, *Sitzung des Wirtschaftsausschusses der Reichsregierung vom 29. August 1931, 10 Uhr.*

relatively weak supervisory office and a stronger role of the *Reichsbank*.[245]

During the deliberations, ample use was made of foreign countries' experience with banking regulation, including that of the United States. Without exception, the American experience served as a cautionary tale to the German policymakers on what regulation was realistically able to achieve (and what not) and that a centralized regulatory structure was imperative to avoid regulatory arbitrage. Thus, there was never the question of whether to install a decentralized regulatory regime, in which, for example, the federal government would set the general guidelines and the states would implement it.[246]

The regulatory framework, which was introduced after barely a month of deliberations with the help of emergency decrees, was a compromise universally known to be a temporary stopgap measure. The 'real' reform of the banking sector was only to take place later, once the dust of the financial crisis had settled and the situation could be analyzed properly.[247] Even so, and despite its relatively light touch, it was heavily critized by the association of private banks and private bankers.[248] A centralized two-tiered regulatory oversight for the banking sector was introduced. An oversight agency (the *Aufsichtsamt*), based with the *Reichsbank*, was installed alongside a banking commissioner (the *Bankenkommissar*), which was formally adjunct to the Ministry of the Economy. The oversight agency would set the regulatory policies (such as capital and liquidity ratios) and the banking commissioner was to be in charge of implementing these policies. Almost the entire banking sector was covered by this regulatory arrangement. Merely the *Sparkassen* were exempt from

[245]See BArch R43, I/1451, pp. 511-520, *Sitzung des Wirtschaftsausschusses der Reichsregierung vom 29. August 1931, 10 Uhr*, BArch R43 I/1452, pp. 471–476, *Sitzung des Wirtschaftsausschusses des Reichskabinetts vom 17. September 1931, 10.30 Uhr* and Born (1967, pp. 160–161).

[246]German ministries and the *Reichsbank* had kept a close eye on regulatory developments abroad throughout the 1920s. See for example BArch R3101/15565, folder *Bankenaufsicht in anderen Ländern*, R3101/20155, folder *Bank-, Finanz-, Steuerwesen u.a.m. Amerika (01.01.1931-1932)* or R3101/20156, folder *Bank-, Finanz-, Steuerwesen u.a.m. Amerika (11.3. 1932-6.1.1933)*. In later discussions, Germans continued to analyze the American regulatory experience. See BArch R2/13636, pp. 31ff, *Bericht des Unterausschusses für Bankwesen am 2. Mai 1932*, BArch R2501/6910, pp. 412–472, *Bankfreiheit oder Reglementierung - Vorgänge und Erfahrungen in anderen Ländern* or the article *"Amerikanische und deutsche Kreditbank Reform: Ein Vergleich"*, by Dr. Victor Wrede in Die Bank, Nr 18 from 01.05.1935, found in BArch R2501/1174. Indeed, the American experience seems to have served as a cautionary tale also to their very own neighbours. The framers of the Canadian constitution made sure to clearly separate federal and state powers and to leave matters of banking in the hands of the central government. See Hammond (1957, pp. 737–739).

[247]See BArch R43 I /1450, pp. 557-564, *Sitzung des Wirtschaftsausschusses der Reichsregierung vom 27. Juli 1931*.

[248]See Hardach (1995b, p. 933).

the oversight.[249] Instead, the emergency decrees established specific universal operational rules for all the banks of the *Sparkassen* System (the *Sparkassen* and their parent organizations, the *Girozentralen*). The state governments were required to codify these rules into corresponding state laws. The federal government also decreed that all *Sparkassen* had to be given their own legal entity. Prior to that, they were technically just another branch of of local or municipal governments. While the separate entities were still owned and run by the respective governments, this provision created a stricter separation between the government and the *Sparkassen* and *Girozentralen*, preventing the governments from accessing the banks' funds at will. In a large number of cases, the local *Sparkassen* had served primarily the private interests of the municipal or regional politicians. This was reflected by the fact that some *Sparkassen* had the vast majority of their assets invested in municipal debt, well above the already generous 50% limit.[250]

During the crisis, it had been difficult for both the central government and the *Reichsbank* to obtain up-to-date and accurate data on the health of the banking sector. It proved to be a massive liability throughout the crisis of 1931.[251] This shortcoming was addressed in the regulations. They provided for strict publications rules and gave the newly created regulatory agencies extensive inspection rights and eventually the right to impose liquidity and capital ratios for the sector as a whole. The regulatory regime also tackled two issues that had been of concern in the 1920s. It allowed for the restriction of entry to the banking sector and it also allowed the banking commissioner to impose an interest rate cartel, with uniform and binding interest rates for the entire country.[252] Together, these provisions went a long way towards reducing competitive pressures within the banking system.

[249] Their larger parent organizations were subject to supervision and regulation. Even so, the *Sparkassen* appear to have largely cooperated with the new regulatory institutions to some extent. See Pohl et al. (2005, p. 148). For details as to the nominal state supervisions of the *Sparkassen* see BArch R2501/6920, pp. 76–77, Memorandum on the *Staatsaufsicht über Sparkassen*.

[250] For the emergency decrees establishing the new regulatory institutions see Reichsgesetzblatt (1931a), Reichsgesetzblatt (1931b) and Reichsgesetzblatt (1931c). For the *Sparkassen* reforms see also Ashauer (1982, pp. 285–289), Born (1982, p. 133–135), James (1986, pp. 101–104) and Pohl et al. (2005, pp. 145–150). For a poignant analysis of the new regulatory structure by a contemporary observer see especially *"Briefe eines Bankdirektors and seinen Sohn: Der Reichskommissar für das Bankgewerbe"*, by Argentarius, in Die Bank, Nr. 29 from 26.09.1931, found in BArch R2501/1182.

[251] See Luther (1964, pp. 231-233) and Schäffer (2008, pp. 21–52).

[252] The banking associations were to negotiate a level of universal interest rates, which the banking commissioner could then declare to be universally binding. This was introduced a two months after the first emergency decrees had introduced the new regulatory structure. See Erster Teil Kapitel III, Zweiter Abschnitt, §§ 1-4 of Reichsgesetzblatt (1931c, p. 704).

The tradition of ‘corporatist’ regulation was not entirely discarded by this new regulatory scheme. Quite the opposite, the corporatist tradition was reflected in the new regulatory structure. In a newspaper report, the designated banking commissioner, Friedrich Ernst, explained his future role as that of a mediator between the different types of banks in order to restore the overall stability of the system. He wanted to foster the cooperation between the banks, the government and the *Reichsbank*. Ernst wanted to avoid fixed capital and liquidity regulations. Those should merely serve as a measure of last resort.[253]

Throughout much of 1932, banking regulation was not on the government’s agenda anymore.[254] It was still busy dealing with the fallout from the financial crisis that required further recapitalizations and even the creation of a bad bank. Eventually the central government owned controlling stakes in the Dresdner Bank (91%) and the Commerz- and Privatbank (70%) and a significant share of the Deutsche Bank (35%) and in a number of other private banks.[255] The public mood was extremely hostile towards the banks during 1931-1933 and it was the first and only time in German history that the worker’s unions would call for a complete nationalization of the largest credit banks.[256] Throughout this time period, the Nazi Party was gaining popularity, whose proclaimed aim it was to ‘break the interest-rate-slavery’ by socializing the entire banking system. Other proposals voiced during this time were the break-up and thus the regionalization of the largest credit banks as well as the separation of investment and deposit banks. During these years, the future structure of the German banking system was an unsettled question.[257]

2.3.6 Enter Hjalmar Schacht (1933–1934)

The reorganization of the banking system was only tackled by the German government once the Nazi party had cemented its power in 1933. Given the radical economic changes

[253]See the article in the Berliner Tageblatt, Nr. 464 on 02.10.1931 with the title “Ab 1. Oktober Bankaufsicht”. It can be found in BArch R2501/1183, p. 4. Indeed, the government did not prescribe any capital and liquidity ratios before or during the Second World War. See Bähre (1982, p. 28).

[254]Merely preliminary meetings were held in the Fall of 1932 on a general law specifying chartering requirements from deposit-taking banks. See for example BArch R2501/6502, pp. 333–337, Memo on a meeting in the Economist Ministry from 18.11.1932 on a deposit law.

[255]See Born (1967, p. 176) and Bel (2009, p. 7) for ownership figures. See also BArch R2501/6918 , pp. 63–66, 152–155 for *Reichsbank* loss estimates of the different banking groups.

[256]See Büschgen (1977, p. 27)

[257]One can obtain a good overview of the different proposals in the public (but not necessarily political) sphere through the various press clippings that can be found in BArch R2501/1173. See also the press clippings from BArch R2501/1182. See also Barkai (1988, pp. 27–33) and James (1995, pp. 281–283) for the ideological background of the Nazi party in terms of financial matters.

FIGURE 2.13: **The key developments of the German banking sector in 1930–1938**

	Total Assets (mio. RM)								
Bank type	**1930**	**1931**	**1932**	**1933**	**1934**	**1935**	**1936**	**1937**	**1938**
Large Credit Banks	12,976	9,618	8,803	7,917	7,687	7,590	7,653	8,071	9,012
Provincial Credit Banks	1,913	1,097	970	912	906	942	1,021	na	1,301
Other Credit Banks	3,008	3,040	2,996	3,113	3,646	5,782	5,849	na	7,303
Private Bankers	3,556	na	2,099	na	na	1,739	1,559	1,391	1,260
Zentralkassen	1,466	1,393	1,315	1,232	1,257	1,391	1,446	1,678	2,095
Credit Cooperatives	4,809	4,559	4,284	4,314	4,490	4,784	5,000	5,404	5,988
Mortgage banks	8,674	8,717	8,352	8,153	8,025	8,092	8,145	na	8,473
Large Public Banks	9,803	9,093	8,821	9,487	10,642	10,829	10,579	11,598	12,557
Sparkassen	13,746	13,823	13,756	14,548	16,433	17,473	18,339	20,128	22,471
Other banks	6,854	6,713	6,896	7,347	7,552	8,300	8,145	na	6,695

Note that Other Credit Banks contains the federally owned and rather large Golddiskontbank. Note also that the definition between the bank types may not be consistent over time. These tables may not necessarily represent a fully accurate picture of the banking sector. The interested reader is strongly advised to refer to the original data source for details. *Source: Own elaboration based on data extracted from Deutsche Bundesbank (1976, p. 121).*

advocated by fringes of the Nazi party, it was highly uncertain whether the regulatory reforms set in motion before the Nazi's ascension to power, would be continued.[258] Crucially, Hjalmar Schacht, the former president of the central bank, was re-nominated to be president of the *Reichsbank*. Ever since his resignation as president of the *Reichsbank*, Schacht had developed more extreme political views, coming to favor more authoritarian modes of governing the country.[259] Schacht had first met Hitler in January of 1931. Until 1933 a close working friendship would develop between the two of them. Schacht would serve as Hitler's personal adviser in all matters related to the economy. At the same time, the cooperation with Schacht helped Hitler gain credibility vis-a-vis the international community and the business elite. In particular the private banking community preferred Schacht over Luther as the *Reichsbank* president as they him best able to secure continuity within the banking sector and to protect them from the radical demands regularly emerging from within the NSDAP.[260]

It was thanks to Schacht and his close relationship with Hitler that the initiative in terms of banking regulation came back to the *Reichsbank*. In the late 1920s and during the

[258] See Bähr (2006, p. 41).

[259] See for example Kopper (1995, pp. 24–27, 67) or Luther (1964, pp. 306–307). For more information on Schacht see for example Kopper (2006, pp. 1-3, 195) or Ahamed (2010). On July 30, 1934 Schacht was also assigned the role of acting Economics Minister, which he held until November 1937.

[260] See James (1985, pp. 335–345), Kopper (1995, pp. 67–70, 86), Kopper (2006, pp. 189-191, 195–199, 216) and Reinhardt (2000, pp. 255– 261).

early 1930s, every government policy with respect to the banking sector had been drafted under the auspices of the German Economics Ministry with inputs from the Finance Ministry and the *Reichsbank*. In a political coup, Schacht bypassed both the Finance and Economics Ministries and obtained permission directly from Adolf Hitler to set up a banking commission under the auspices of the *Reichsbank*. Furthermore, Hitler trusted Schacht's advice almost blindly and protected him from the more (in terms of banking reform) extremist backbenchers of the Nazi party, who had become increasingly aggressive in their agitations against the private banking system.[261] By taking the initiative, Schacht wanted to forestall attempts by more extremist wings of the nationalist socialist party to socialize the entire banking system.[262]

The inquiry was announced in the summer of 1933, two years after the financial crisis of 1931. Officially, it was to conduct a thorough analysis of the banking sector and to propose structural changes. However, Schacht and his men from the *Reichsbank* cleverly selected the composition of the members of the banking composition, as well as the experts that were being heard, so that the proponents of a private banking sector were outnumbering its critics. At the same time, he was not subject to direct influence by the (private) banking sector either, allowing him to press for more comprehensive regulation. The committee members were selected such that the *Reichsbank* had a dominating role. Schacht and the *Reichsbank's* vice president Dreyse acted as chairmen of the commission and were thus the agenda setters. A third Reichsbank representative was also on the commission, as well as Friedrich Ernst, the banking commissioner who regularly cooperated with the *Reichsbank*. Both the Economics and the Finance Ministry were represented by sub-secretaries, one of which, Feder, was a well-known NSDAP ideologue who advocated nationalization of the banking sector. Schacht included him and Keppler, the 'special representative to Hitler for Economic matters', in the commission so as to pacify the Nazi party's lower ranks. They were joined by a handful of representatives from industry and agriculture as well as a representative from academia. Unlike the banking commission of 1907/08,

[261] See Hansmeyer and Caesar (1976, pp. 375–376), Kopper (1995, pp. 74–86) and Kopper (2006, pp. 203–205, 216). Indeed, Schacht was able to turn the *Reichsbank* into the main economic policy making body within the Thrid Reich, something he had already attempted during the Weimar Republic, as James (1985, pp. 343–344) points out. Intriguingly, Hitler's pro-business approach was often in direct conflict with the official Nazi Party line, an in particular with some nazi leaders of the old guard and the "rank-and-file of the nazi movement", as Hardach (1984, pp. 228–229) points out. He attributes this to Hitler wanting to rely on cooperation, rather than coercion, of the business elite. Similarly see also Hansmeyer and Caesar (1976, p. 370).

[262] See BArch R2501/6910, pp. 1–16, Memo *Zur Frage der Veranstaltung einer neuen Bankenquete* from 09.06.1933.

no representative of either the private or the public banking sector formed part of the commission, presumably to prevent accusations of regulatory capture by the organized banking interests.[263]

Additionally, most of the experts that were asked to prepare the official preliminary reports came either from the *Reichsbank* or the supervisory office (10), academia (4), the private banking sector (4) or the Prussian Economics Ministry (1).[264] And since the commission took place under the auspices of the *Reichsbank*, all additional support work was carried out by *Reichsbank* staff loyal to Schacht.[265] Schacht also laid down the general (liberal) principles according to which the Enquête was supposed to operate. These principles confirmed the adherence to private ownership and private intitiative, albeit under the guidance of the government. Schacht made clear that he did not intend to introduce major structural changes to the private banking system. Of course he was careful not to make such remarks in public before the commission had taken up its workings.[266]

The major decisions had already been taken before the banking commission even began its work. There would be a tightening of the centralized regulatory regime, but there would be no nationalization of the private banking sector and no break-up of the universal banks either. Indeed, first drafts for two new banking laws were prepared within the *Reichsbank* even *before* the Commission's discussions had begun.[267] According to Schacht, the Enquête was a mere fig leaf in order to give the banks the impression that their concerns have been heard, to neutralize extremist regulatory demands from individuals within the Nazi Party and to prepare the general public for the upcoming changes to the regulatory structure.[268]

[263]See Barkai (1988, p. 197), James (1995, p. 283–285), Kopper (1995, pp. 88–90). See Müller (2003, pp. 116–121) for biographical details on the key commission members.

[264]See Reichsbank (1933a) and Reichsbank (1933b) for the official preliminary reports.

[265]See Müller (2003, p. 136).

[266]In making it's case for the importance of private ownership, the *Reichsbank* carefully collected statements by prominent NSDAP figures that seemed to support these liberal principles. For the principles and the guiding questions see BArch, R2501/6912, pp. 372–382, Protocol of an internal *Reichsbank* meeting on the Banking Commission, dated 21.10.1933, and BArch R2501/6913, pp. 184–186, Memo on the working principles of the Banking Commission, dated 11.11.1933, and Barch R2501/6910, pp.12–15, Annex 2 to the Memo *Zur Frage der Veranstaltung einer neuen Bankenquete*, from 08.06.1933. For the *Reichsbank's* attempt to appear objective by not making public statements in this case see Kopper (1995, p. 97).

[267]See BArch R2501/6912, pp. 383–389, *Entwurf eines Sparkassengesetzes* from 18.10.1933 for a unified *Sparkassen* law, pp. 390–393, for the Memo *Thesen zur Sparkassenfrage*, from 18.10.1933, on the *Sparkassen* issue, and BArch R2501/6913 pp. 141–152, *Vorentwurf zu einem Bankengesetz*, from 19.11.1933, for a draft Credit Act.

[268]See Schacht's remarks in BArch R2501/6915, pp. 81–85, *Sitzungsprotokoll der nichtöffentlichen Sitzung des Bankenqueteausschusses* from 27.11.1933. Similarly see James (1995, p. 284), who reports that Schacht made an equivalent remark to an official at the Bank of England in early October of 1933.

Interestingly only few contemporary observers seem to have seen it as such.[269] Virtually any major change to the banking sector was forestalled by Schacht's actions.

There was one controversial question, however, which Schacht wished to address. It was that of the public banking system. In accordance with the private banking communities long-voiced opinion, the initial *Reichsbank* memos asked the question, whether there was a way to restrict the banking activities of the Sparkassen to their original scope of the time period before the First World War. This issue had become more urgent since the *Sparkassen* had been subject to the ongoing Nazi *Gleichschaltung*, which had replaced many municipal and regional politicians and brought them into line with the NSDAP.[270] These politicians, with the backing of the NSDAP, then instructed the *Sparkassen* to adopt aggressive methods to expand their market share in an effort to increase their income. In some extreme cases the municipal governments gave the order not to transfer any money to accounts that were not held with *Sparkassen*, forcing businesses that dealt with the government to open a *Sparkassen* account. The ideological justification for this behavior was given as the necessary push-back against anonymous private banking capital. By the end of 1933, Schacht had managed to push through an end to these aggressive methods for the time being, but for this he had needed the support of the Economics Ministry. He consequently pushed for the regulatory institutions to obtain the necessary tools to prevent such behavior in the future.[271]

The government commission began on the 6$^{\text{th}}$ of September 1933, first with introductory remarks by Schacht, Keppler and Feder, which were subsequently followed by the presentation of the experts' preliminary reports on the state of the German banking system. Only on the 21$^{\text{st}}$ of November did the official debates and the hearings of additional experts begin. They were organized by banking group, rather than by topic. This ensured that whenever private banks issues were being discussed, not too many supporters of the Sparkassen system were present. The hearings were concluded after a month on the 20$^{\text{th}}$ of December. Nevertheless, the hearings were important as they allowed representatives from all the banking groups and the industry to voice their opinion. In particular for the

[269] An exception was Alfred Lansburgh in his article *Brief eines Bankdirektors an seinen Sohn: Die Banken und die Bank–Enquete*, by Argentarius (pseud.) in Die Bank, Nr. 77 from 22.11.1933, found in BArch R2501/1173, pp. 89–90

[270] For the *Gleichschaltung* of the Sparkassen system see Pohl et al. (2005, pp. 159–171).

[271] See Kopper (1995, pp. 90–92) and Pohl et al. (2005, pp. 150–151). And indeed, throughout the 1930s, the Sparkassen were the banking group that grew the most, to the detriment of the private banking sector. See James (1995, pp. 279–282).

private banking sector it was an important forum in which it could publicly defend itself against the attacks from the NSDAP and other parts of the public, which demanded their nationalization. Most of their hearings were public and closely followed by the press. The importance Schacht attributed to the different points of discussion are reflected by his attendance. Schacht attended and hence chaired most of the sessions that dealt with the private banks, to ensure that any discussion went in the direction he desired, if need be by cutting short any undesirable discussion. However he did not chair any session on the Sparkassen System or the Credit Cooperatives.[272]

Given the composition of the banking commission, the invited experts and the overall *Reichsbank* leadership, it was relatively easy for the private banking sector and the German industry to fend off the nationalization suggestions put forward by Feder and other ideologues. A plan that attracted significant attention in public, and that proposed to break up the Dresdner Bank and the Commerzbank into regional government banks, was also fended off in the banking commission with ease.[273] Indeed, the wealth of testimonies in favor of the private banks, not only from the bankers themselves, but also from medium and large scale industry and other business men, were successful in temporarily silencing the banks' critics during the hearings. The private banks did their share as well, by trying to present themselves as wholly cooperative with the overall aims of the national socialist movement. In the summer of 1933 they even had pre-emtively agreed to collectively lower their interest rates in order to gain the goodwill of the public and the government.[274]

Schacht managed to deflect a good deal of attention away from the private banking system and towards the public banking system. There were just as many working sessions deliberating reform proposals for the public banking sector, as there were for the private banking sector. Thus, proponents of the private banking sector once more used this opportunity to demand that the tax exemption of the *Sparkassen* be lifted.[275] Furthermore,

[272]For the protocols of the month long working sessions of the commission see the folders BArch R2501/6915, 6916 and 6917. For press articles covering the Enquête see for example the folders BArch R5201/1177, 1180. See for example BArch R2501/6916, Protocol of the commission's 2nd working session from 14.11.1933 for Schacht's intend not to let any undue discussion arise in the first place.

[273]For the *Regionalbankenplan* proposed by Kurt von Schröder a private banker, who was rising quickly through the Nazi party ranks see for example the Berliner Tageblatt article Nr. 531, *Großbanken wehren sich gegen die Regionalbanken-Pläne*, from 11.11.1933. Kopper (1995, pp. 94–96) believes that Schröder's motivation for proposing this plan was that these Regional banks would have given him personally significant resources to further his political interests. For Schröder's testimony in front of the commission see BArch R2501/6015, Protocol of the working session from 28.11.1933.

[274]See James (1985, p. 284) for the silencing of the critics and Barkai (1988) for the humble approach of the private bank representatives. See also Hardach (1995b, p. 934).

[275]See BArch R2501/6915, Protocol of the working session from 13.12.1933.

Schacht had determined that most of the hearings and working sessions should not be open to the public. Officially this was to avoid upsetting the population as the commission revealed the flawed workings within the Sparkassen sector. It is much more likely however, that he saw the relative secrecy as the most promising way to eventually impose restrictions on the Sparkassen operations, without triggering the immediate opposition from *Sparkassen* supporters.[276]

One and a half years later, the banking commission ended almost where it began.[277] The actual hearings had taken only about a month. The remainder of the time was divided between the initial preparations for the commission and the drafting of the law. Schacht cleverly delayed the reform process as time was on his side.[278] On one hand, it gave the regime the time to focus on unemployment, which was the much more pressing problem. On the other hand, it also helped to heal the wounds of the public, which had been outright hostile towards the large credit banks. The drafting of the law was largely uncontroversial, as the main direction of thrust had already been determined by Schacht and the subsequent commission. Additionally, Schacht found a way to have Feder and Keppler excluded, the most vocal advocates of a nationalization of the private banking system. Feder had tried to mount public pressure on the commission and on the *Reichsbank*, since he was dissatisfied with their pro private banking stance. With him and Keppler gone, no prominent representatives of the NSDAP were left in the commission. The only major issue that caused some prolonged discussion, was whether the banking commissioner was supposed to be independent from the federal government. Government ministers, who were Nazi party members and who were eventually invited to offer their opinion on a draft version of the Credit Act tried to press for more control of the federal government of the banking commissioner and banking policy in general. When their demands were rejected by Schacht and his men, some of them withdrew from the deliberations in protest.[279]

[276]Indeed, the non-public nature of the hearings of the *Sparkassen*, did alarm many of their representatives. See Kopper (1995, pp. 105–106).

[277]The Economist (1934) remarked that the principles advocated in the final report were not revolutionary. Instead, they reflected standard regulatory principles that had already been adopted in many other countries. Nevertheless, at the time this view was not shared by all outside observers. Dessauer (1935, p. 224) took the opposite view and saw it in line with Nazi policy that tended to *"[...] foster the authoritarian influence of the government."*

[278]Newspapers were reporting that the release of a new law was imminent, just a month after the hearings had ended. Instead it would take almost a year for it to be released. See for example an article in the Deutsche Allgemeine Zeitung, Nr. 11 from the 08.01.1934 found in Bundearchiv R2501/1177, p. 17. For details on the committee's drafting work see Kopper (1995, pp.116–122) and Müller (2003, pp. 129–135).

[279]Schacht excluded Feder by accusing his aide, an consequently him, of leaking internal commission material to the press. See Barkai (1988, p. 197), Hansmeyer and Caesar (1976, pp. 375–377), Hardach (1995b, p. 934), Kopper (1995, pp. 119–122) and Müller (2003, pp. 130–135). James (1995, p. 285)

When the Credit Act of 1934 was proclaimed in December of 1934, it confirmed the regulatory structure that had been introduced in 1931, and it gave the regulatory institutions even more powers. From now on the entire banking sector would fall under a unified federal regulator, including the public *Sparkassen* system and the mortgage banks. This implied that the central government would regulate regional and local government banks. Thus, while the *Reichsbank* was not able to restrict the *Sparkassen* operations to the pre-war level, it was able to force federal control and supervision upon it. At the same time, this meant that the *Sparkassen* had been formally accepted as full-fledged universal banks.[280] No changes were made to the structure of the banking system as such. After all, the German banking system did not have a structural problem. There was no inherent instability, which made it vulnerable during every economic downturn. Rather, the German banking system had, if anything, a corporate governance problem and that could most effectively be tackled by increased government regulation.[281] Not only were publicity requirements strengthened, but from now on banks were required to invest savings deposits more conservatively than other forms of money deposited with them. Limits to investment in certain asset classes were established and minimum liquidity and capital standards could be imposed as well. Furthermore, entry to the sector and even the creation of new branches was only possible with the explicit permission of the regulatory agencies. This allowed them to restrict entrance to the banking sector. The government-sponsored interest rate cartel was also included as an official provision of the Credit Act and so was the restriction to advertising practices that had been agreed upon in 1928.[282]

Given the extensive powers granted to central regulatory authorities by the Credit Act of 1934, the reforms essentially gave the *Reichsbank* (and thus Schacht) the power to control the banking system at her will. While the private banks escaped structural change, they were negatively surprised by the heavy-handedness of the regulations, which

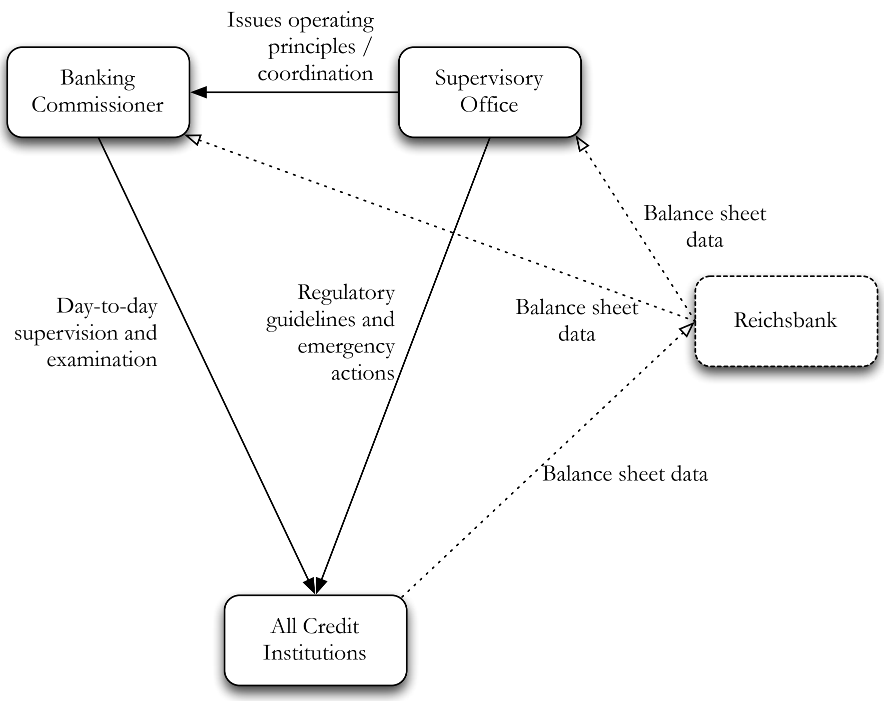
reports that Feder and his ideologues retaliated by attempting to humiliate Schacht and the community of the private bankers. They demanded 'emergency donations' for the party coffers in the form envelopes full of money, that had to be put into physical collecting boxes held by Schacht and the presidents of the major stock exchanges.

[280] Note that the state institutions in charge of regulating the public banks could continue their operations afterwards, as long as they did not counteract federal regulations and supervision.

[281] See also the Kieler speech by Schacht (1934) from January 1934, in which he outlines this view. The Kieler speech also served as the ideological legitimization, as he attempted to link Nazi thinking with the reforms he intended to implement.

[282] See Reichsgesetzblatt (1934). In order to encourage prudent behavior by bank managers, the law also included a provision that retained banker's bonuses even after the bankers' had left the bank. It is likely that this provision found its origins in a similar one existing for *Reichsbank* branch managers. For the *Reichsbank* provision see Döring (1933, p. 147).

Figure 2.14: **Schematic overview of the German regulatory structure as introduced by the Credit Act of 1934**



The Supervisory office was based with the *Reichsbank*, but it also contained members of the government. The Banking Commissioner was an independent agency under the auspices of the Economics Ministry. Banks submitted monthly reports to the *Reichsbank*, which analysed the balance sheet data and made it available to both the Supervisory Office and the Banking Commissioner. The only credit institutions not subject to regulation were special purpose banks, such as the *Reichsbank*, the Golddiskontbank or the German Postal Service and its affiliated institutions. *Source: Own elaboration.*

they feared would affect their profitability.[283] Even though the Reichsbank held significant powers over the banks, it seems like it did not make much use of these specific ones in the pre-war period. Indeed, the government even reprivatized the large credit banks by 1937.[284]

2.4 Conclusion

Why did Germany get a regulatory monopoly for its banking system and why did the United States not? Was it because all major regulatory changes in the United States were designed *to ensure a decentralized banking system*? Was it because Congress unanimously

[283] See also Barkai (1988, pp. 198–199, 203–204). For a schematic overview of the German regulatory structure as introduced by the Credit Act of 1934 see figure 2.14 on page 97.

[284] See Barkai (1988, p. 203), Bel (2009) and Kopper (1995, pp. 199–208).

rejected the idea and never tried to implement it? My research suggests that this was not the case. Indeed it is striking how close the United States was to bringing about a centralized regulatory structure. Ever since the 19th century, Congressional majorities could be found at various times that attempted to bring about a regulatory monopoly. American policymakers thought about centralizing their regulatory system well over a century before their German counterparts, who were only most reluctant to introduce comprehensive regulation of their banking system in the first place. The reason why the United States did not develop a centralized regulatory regime was because of a specific constitutional barrier that granted the individual states the right to charter their own banks. In Germany, a comparable constitutional barrier did not exist ever since it became a nation state in 1870.

At several occasions throughout its history, the American federal government tried to bring about a unified regulatory banking system under national supervision. First, with the establishment of the national banking system (1861–1865), then with the establishment of the Federal Reserve System (1910–1917) and finally with the establishment of the Federal Deposit Insurance (1933–1935). All of these institutional additions were attempts by the federal government to set the incentives in such a way that would compel state banks to subject themselves to federal regulation. In exchange, banks would obtain competitive advantages vis-a-vis banks not submitting to national regulation. The federal government had to take this route, since the constitution prevented it from outright assuming control of banking regulation by prohibiting states to charter banks. The states' right to charter banks is enshrined in the constitution. Consequently, every single one of these attempts failed as they were circumvented either by legislation or financial innovation.

The introduction of the national banking system was specifically designed to replace the state banking system. It was made possible by the special conditions of the Civil War. It had seen the secession of a number of states that were particularly averse towards federal control of the banking sector. The first attempts to introduce a national banking system were only mildly successful. Only after a punitive tax of 10% on states' bank note issue was introduced in 1865, was the national banking system turned from a virtual failure into an astounding success. Almost all of the state banks converted to national banks or ceased operations. However, Congress made a crucial mistake in not realizing that in a fractional-reserve system money could not only be created in a physical form in the form of gold-backed notes, but also in the form of deposits. The state governments did not remain idle either and reacted to the federal competition by loosening the regulatory requirements for state banks. Together with the rapid rise of the cashless transfers, the advantages enjoyed by national banks were erased over time.

A major liquidity crisis in the aftermath of the San Francisco earthquake of 1906 created the necessary conditions for major banking reform. Numerous crucial defects of the banking system were quickly identified, in particular the prohibition of branching, the lack of regulation of certain parts of the banking system as a result of various regulatory agencies, and the lack of a central bank that could act as a lender of last resort. The Federal Reserve was installed not only as a central bank but also as another regulatory institution in an attempt to coax state banks under a central regulatory body. National banks were forced to join the system, whereas state banks were given the option to join. At the outset of the Federal Reserve System, national and state member banks were required to subject to the same federal reserve regulation. However, this provision was loosened a few years later for the state banks as hardly any of them converted into national banks. It was a desperate attempt by the government to boost the Federal Reserve System. Congress had vastly overestimated the attractiveness that access to a lender of last resort would have for small state banks. Even with the looser regulations in place, the vast majority of state banks decided not to join the federal reserve system and not to subject to federal regulation. In loosening entry restrictions for state banks, the federal government bowed to the regulatory competition of the states, rather than solving this problem once and for all. The possibilities for regulatory arbitrage increased further, which was quite the opposite of what was originally intended. For the time being, federal policymakers could not find their way around the constitutional barrier to centralize regulation.

The reforms enacted before the First World War only managed to address part of the structural problems plaguing the banking system. Consequently, reform of the banking sector was very much on the agenda throughout the 1920s. It was fast-tracked with the onset of the Great Depression, when it became clear that the reforms enacted before the First World War were far from sufficient. Therefore, the reforms of the 1930s picked up almost exactly where Congress had stopped in 1913. Top policymakers again correctly identified the key problems besieging their banking systems at the time. They were well aware of the structural problems caused by the atomistic nature of the banking system. It was also known that the banks were playing the regulators against each other in a game of regulatory arbitrage. Banks chose the regulation that was best apt for their particular necessities and that tended to be less regulation. The United States was engulfed in a regulatory race to the bottom and needed to find a way to stop it. The country was suffering from the *wrong* regulations, rather than too little regulation. Government officials were aware of this (on both sides of the Atlantic), and some policymakers were willing to change it, if possible by introducing a unified banking system. But outright assumption of control was out of the question, given the constitutional barrier and the political structure. Interest groups of the unit banks and the state regulators, which had not lost their political power in the course of the crisis lobbied hard for the status quo in which they had quasi monopolies in their respective cities. Indeed, even less far-reaching reforms, which were eventually introduced as the Glass-Steagall Act, found it hard to gain the support of a majority during a period of economic depression and banking instability.

Reform was only possible after a cataclysmic nationwide breakdown of the banking system. The kind of compromises made were those of least resistance by introducing new regulatory institutions. In 1933/34, the Federal Deposit Insurance Corporation and the Securities and Exchange Commission were created. Initially, the plan was to require banks to subject to regulations by the Federal Reserve System if they wanted to accede to the FDIC. It would have been a powerful incentive and could have gone a long way to extend the regulatory hand of the Federal Reserve over much of the American banking system. But this provision was first loosened in the Banking Act of 1935 and later dropped altogether. There was no doubt, however, that many key American policymakers considered a unified banking system superior to the decentralized arrangement that was in place.

Another important obstacle on the path to a regulatory monopoly was the fact that each unsuccessful attempt to build a national framework also left behind 'regulatory ruins. And these were not torn down during subsequent attempts to reform and unify the regulatory framework. Consequently, the 'regulatory ruins' developed into full-fledged political actors with their own agenda. Thus, instead of developing a unified banking sector a most complex web of regulatory and supervisory institutions evolved.

The situation was quite different in Germany. By the turn of the century, Germany's banking system had developed into one with specialized banking groups that each catered to a particular segment of the market. There were no branching restrictions in place ever since the unification of the country and private sector banks were virtually unrestricted in their activities. Merely the mortgage banks and a handful of note-issuing banks were regulated to some extent. As a consequence of the liberal approach to banking regulation, and as a side-effect to stock market regulation, a number of large credit banks emerged, which maintained branches throughout the country. This lead to an equivalent decline with the private bankers. Another crucial difference with the American banking sector was that the local and regional government played an increasingly important role in offering banking services via the *Sparkassen* system. Last but not least, from 1875 onwards Germany had a public-private central bank (the *Reichsbank*) that acted as the government's proxy in banking matters.

The 1907 liquidity crisis triggered a banking commission in Germany as well, as the large credit banks had become reliant on liquidity support from the *Reichsbank*, which in turn endangered the adherence to the gold standard. The commission was meant to find a way to reduce the reliance of banks on liquidity support from the central bank. While the commission also evaluated a number of potential regulatory options, it recommended not to regulate the banking sector. This was hardly surprising considering that the majority of the members were either representatives from the banking circles, or from big industry. Furthermore, the *Reichsbank* President Havenstein, also tried to avoid government intervention at all cost as this would have meant a loss of influence for the *Reichsbank*. The major credit banks agreed to publishing their balance sheets on a bi-monthly basis as a gesture of cooperation. In the aftermath of the banking commission, the *Reichsbank* resorted to 'corporatist regulation' by attempting to influence the banking sectors' behavior through moral suasion. It also encouraged the formation of interest rate cartels. It was also in the aftermath of the banking commission, that the public *Sparkassens'* permissible range of operations was widened. In part this was meant to increase the use of cashless transfers throughout Germany, and in part it was meant to encourage the growth of the public banking sector, in order to provide a counterweight to the largest credit banks. The expansion of banking activities of the *Sparkassen* system was also in the fiscal interest of municipal and regional governments, as it provided them with access to cheap credit.

After the war and during the hyperinflation, the *Sparkassen's* operations were further expanded upon the insistence of the municipal governments, which relied heavily on the public banking sector for their fiscal needs. Not only did the *Sparkassen* benefit from their explicit backing of the repsective governments, but they were also exempt from taxation. Consequently, the increasing competition between the public banking sector and the private banking sector became the most controversial issue that had to be addressed by the *Reichsbank* during the 1920s. It attempted to do so by negotiating first a restriction to competitive practices, and later a general interest rate cartel covering the entire banking sector, not just the private credit banks. It is worth noting that prior to the banking crisis of 1931, the government had no intention to replace the *Reichsbank's* 'corporatist' regulation of the banking sector with a comprehensive regulatory framework. If it were not for the Great Depression, Germany might well have gone the same way as Britain and introduced comprehensive regulation only much later.

In the summer of 1931, the German government found itself forced to recapitalize the largest universal banks as well as the public *Sparkassen* system. From that moment in time, the government's attitude towards federal regulation changed drastically for two main reasons. First, it was taken by surprise by the weaknesses in the countries largest banks (which is understandable, giving the dearth of real-time data available on the banking system at the time), and thus felt betrayed by the large banks. Second, it would not have been able to justify the costly nationalization and recapitalization of large swathes of the banking system in front of voters, without installing comprehensive government oversight in return. Within a month, the German federal government scrambled to evaluate various potential regulatory schemes – behind closed doors. Contrary to the usual modus operandi of the German legislative process, neither the banking sector nor the state governments were given much of a say. Instead, regulatory experiences abroad were analyzed, in particular the American one. The regulatory race to the bottom in the American system convinced the German government not to go the decentralized route. Merely the *Reichsbank* was able to represent the interests of the (private) banking community. And indeed, it tried to prevent the introduction of a comprehensive regulatory regime. As it was unable to do so, it switched its strategy to ensure sufficient *Reichsbank* influence over the eventual regulatory institutions. Barely a month after the crisis, the federal government called into existence a centralized regulatory regime, where most responsibility for banking regulation was ultimately located with the *Reichsbank*. In line with earlier attempts of the *Reichsbank* to establish uniform interest rates throughout the country, it also gave the supervisory authority the power to impose an interest-rate cartel and restrictions to banks' advertising practices, in order to reduce competitive pressures in the banking sector. At no time was a decentral regulatory regime, that would have given regulatory or supervisory powers to the German states, even under discussion in that summer. The regulatory regime introduced in the fall of 1931 was hardly radical. On one hand, it was intended to be a stopgap measure. On the other hand, it was a reflection of the federal governments' 'hands-off' stance that delegated most regulatory responsibility to the *Reichsbank*. Indeed, the 1931 regulations are probably best described as the continuation of the *Reichsbank's* 'corporatist regulation' under the veil of federal supervision.

Matters were even easier for the German government from 1933 onwards, since parliamentary activity had been entirely suspended under Nazi rule. From that point in time, the German government could ram through any of its proposals without much consideration for external interest groups. Other than the publicly owned *Sparkassen*, the banks did not have an influential lobby anymore. Virtually, any structural change seemed possible at this point. The government entity that would take the regulatory initiative was almost guaranteed to leave its mark on the banking sector. If it would not have been for Hjalmar Schacht and his close connection with Adolf Hitler, it is almost certain that some kind structural change would have been imposed on the private banking sector. It was a real possibility that under a different leadership the large universal banks would have been broken up into regional banks or the entire banking sector nationalized. The pressure from the extremists of the Nazi party and the general population was immense. Schacht understood that a separation of deposit and investment banks was largely superfluous, since the German banking system had already developed a 'natural' specialization, with each bank group catering to a certain kind of customer. This specialization from the pre-World War I period was largely carried over into the 1920s and 1930s. Additionally, the banking systems' problems were not structural, but, if anything, managerial and the best way to address these problems is through regulations and supervision. Schacht went through great lengths to defend the private banking sector from the attacks of Nazi ideologues and at the same time he attempted to reign in the expansion of the public banking sector. Instead of undergoing a structural change, the German banking system experienced a solidification of existing structures. At the same time, Schacht expanded the regulatory framework first introduced by the Weimar bureaucracy and thus wrapped a regulatory straitjacket around the entire banking sector, which gave him significant control over the entire system, both public and private.

In Germany, central government policymakers did not face major constitutional headwinds by the German states, when it tried to introduce a regulatory monopoly. This was primarily because, the German states' constitutional powers with respect to chartering banks were weaker than those of states in the United States. Additionally, the German states' bargaining position and that of the largest private banks was further weakened by their reliance on the central government for capital during the banking crisis of 1931. Once the Nazi government came to power in 1933, the only remaining question was whether the banking sector would experience a large-scale nationalization or whether it would remain private, but under the supervision of the government. The ultimate regulatory structure is to a large extent an embodiment of Hjalmar Schacht's personal preference – the acting Economics Minister and President of the Central Bank at the time. Schacht outmaneuvered more radical elements of the Nazi party, as well as more conservative elements within the banking sector. And Schacht's personal preference overlapped to a large extent with the framework that had already been put in place by the Weimar politicians in the aftermath of the Banking Crisis of 1931. As such, the Credit Act of 1934 is not to be considered as a Nazi piece of legislation, but in line with German corporatist tradition of regulating the economy.

Even though they do not form the focus of this study, a few key regulatory developments are worth highlighting. Contrary to the United States, in Germany there was not even a discussion surrounding the ability of banks to branch. Until the introduction of the National Banking Act, branching was uncontroversial in the United States as well. And it is unlikely that branching would subsequently have developed into a controversial issue, would it not have been due to the strong states' right with respect to chartering banks. Similarly, deposit insurance was tried by various states in the United States in the 19th century already, and in the 1930s it was implemented for a wide section of the American banking sector. At first deposit insurance was meant as a tool to protect depositors from the bank failures of the relatively small and unstable American unit banks, which, in large parts of the United States, were not allowed to branch or form larger banking trusts any longer. Later, deposit insurance was used as a key measure to protect the unit banks from competition of larger and presumably more stable banks. In Germany, government mandated deposit protection was not on the agenda throughout the period under consideration. Instead, banks either had branches, or they created parent organizations to even out liquidity needs, or they formed cartels as a measure of restricting competition and thus profit margins, and ultimately banks' safety. Interestingly, both countries also introduced government-sponsored short-term interest-rate cartels in the wake of the Great Depression, in an effort to restrict competition. Universal banking was not really challenged in Germany in the period under consideration either. On the contrary, the Sparkassen and Credit Cooperatives that began as specialized institutions, increasingly expanded their operations. Whenever, the separation of investment and deposit banking was suggested, it was an attack targeted at the largest credit banks that meant to reduce their size, albeit with little success as Antitrust considerations did not nearly play as an important role in the German economy, as in the American one. In the United States, Antitrust considerations were the main drivers for restricting universal banking first via the National Banking Act and later through Glass-Steagall Act. After all, by the 1930s most banks did not have branches and could not have been broken up into regional operations. Therefore, the only option that was left to reduce them in size was to split them up along operational lines.

This chapter highlights the crucial role states rights played in shaping the American regulatory discourse and ultimately the regulatory structure of its banking system. The adverse developments in the American banking sector, due to the regulatory arbitrage between the various regulatory institutions, served as additional impetus for the German central government to install a centralized solution. This implies that the regulatory arrangement of the American banking system was only a second-best solution that was held in place by strong states rights. In the absence of these institutional constraints, no such system would have evolved and persisted. The United States would have eventually adopted a centralized approach to banking regulation like most other countries. Instead, the United States developed most complex set of regulatory and supervisory institutions that continue to plague its banking sector to this day.[285] These findings do not replace existing analyses, but they supplement them. They suggest that when the political economy of the regulation of the American banking sector is discussed, not only should the attention of scholars be focused on the issues of branching restrictions, deposit insurance, and the separation of deposit and investment banks,[286] but also on the issue of the centralization of the regulatory structure. This constitutional conflict was a crucial bargaining chip throughout much of American banking history.

[285]The complexity of America's regulatory system is the subject of an informative article in the The Economist (2012a) on the recently passed Dodd-Frank Act.

[286]These are the standard 'ingredients' found for example in Benston (1990), Calomiris and White (1994, pp. 170–176), Calomiris (2006b, pp. 75–76) or White (1983, p. 39). Sometimes the interest rate caps introduced during the Great Depression ('Regulation Q') are also included as in Calomiris (2010).

Chapter 3

The long (re-)birth of the German Credit Act of 1961

3.1 Introduction

In the aftermath of the Second World War, the Allies forced substantial institutional changes on the West-German banking system (henceforth just Germany).[1] Under the leadership of the U.S. military government, the Allies decentralized the largest commercial banks, the central bank and the regulatory structure. In particular, the Allies changed the structure of regulation from a centralized one to a decentralized one. In a major break with German administrative tradition, they also transferred the competency in terms of Credit and Money (and thus banking regulation) from the Ministry of Economics to the Ministry of Finance. Yet, by the beginning of the 1960s most of these institutional changes were reversed by the Germans.

While there exist accounts for the changes to the central bank and to the structure of the large commercial banks[2], the literature is sorely missing a more detailed account of German banking regulation after the Second World War. Moreover, the existing literature treats the changes to the supervisory institutions largely as a by-product, whose reversal

[1]In what would later be East Germany, even more radical changes to the banking system took place, but they are not the topic of this chapter.

[2]See for example Horstmann (1991) and Horstmann (1985) for the Allied changes to structure of the great universal banks. See Dickhaus (1998) and Wandel (1980) for the establishment of a new central bank by the Allies, the Bank deutscher Länder, and see Häuser (1998), Hentschel (1988a,b) and Marsh (1992) for the origins of the *Bundesbank*, which largely reversed the changes introduced to the central bank structure by the Allies.

was a mere formality.[3] Indeed, the 1961 Credit Act constitutes in most respects a re-birth of the Credit Act of 1934.[4] But why did Germany pass almost exactly the same Credit Act twice, within a 30 year period? Was it really just a matter of returning to the historical path, once the Allied influence had waned?

This chapter seeks to provide a more detailed account of the origins of the German Credit Act of 1961 by drawing on the relevant government files.[5] The archival evidence suggests that the Credit Act of 1961 was the product of an intense federal conflict. It needs to be interpreted as the minimum consensus for a coalition that sought to re-centralize banking regulation and which needed a parliamentary supermajority to break the German states' objection.

The chapter will proceed as follows. The next section sets out the regulatory framework in place before the Second World War. followed by a section describing the changes made by the Allies up until 1948. Then the first drafts of a new Credit Act are presented, which were produced under the auspices of the Central Bank and the Finance Ministry. This is followed by a description of the work under the auspices of the Economics Ministry, and a failed recentralization attempt. A Credit Act draft was introduced into to parliament in 1959 and passed after two years of parliamentary struggle in the summer of 1961.

3.2 The regulatory framework prior to 1945

A comprehensive regulatory framework for the German banking system was first introduced during the Great Depression. It was introduced in the form of emergency decrees in the aftermath of a severe financial crisis in 1931. These regulations were later expanded and codified during Nazi rule in the Credit Act of 1934.[6]

[3] See for example Ahrens (2007), Ambrosius (1998), Büschgen (1982), Holtfrerich (1995), Wolf (1998b) and Wolf (1998a) for their treatment of the German regulatory system after the Second World War. The contemporary dissertation of Honold (1956, pp. 74–86) analyzes the state of banking regulation primarily from a legal perspective, but he does not address the political economy of a new credit act. Hardach (1995a, p. 292) sees a major liberalization taking place after the Second World War, but he, too, provides no details as to the Credit Act's origins. Please note that the dissertation on the Credit Act of 1961 by legal historian Ritter von Georg (2013) was prepared simultaneously and independently from this one.

[4] The Credit Act of 1934 constitutes the origin of comprehensive banking regulation by the central government in Germany. In section 3.2 on page 107, I summarize its main contents.

[5] Of particular relevance are the files of the Economics Ministry (the *Bundeswirtschaftsministerium*), the Finance Ministry (the *Bundesfinanzministerium*) and the Chancellery (the *Bundeskanzleramt*).

[6] On events that lead to the regulatory regime in 1931–34 see Born (1967), Kopper (1995) and Müller (2003). For a long term view on the origins of German banking regulation see Chapter 2 of this dissertation.

The regulatory framework had a centralized structure. Only two institutions were involved in the oversight of the entire banking sector.[7] One was an oversight agency (the *Aufsichtsamt*), which was based with the central bank (the *Reichsbank*). Most of its members were holders of political office, but de facto power lay with the President of the *Reichsbank*. The oversight agency was in charge of determining the regulatory policies to pursue. The other regulatory institution was the office of the banking commissioner (the *Reichskommissar*), whose task it was to execute the policies decided upon by the oversight agency. The *Reichskommissar* was a central government agency adjunct to the Economics Ministry. Banks were required to hand in their balance sheets on a monthly basis to the *Reichsbank*, which would then pass on relevant information to the oversight agency or the banking commissioner.[8]

The regulations set out in the Credit Act of 1934 provided for strict publications rules and gave the regulatory agencies extensive inspection rights. They also enabled the regulatory agencies to establish liquidity and capital standards.[9] The banking commissioner was allowed to impose an interest rate cartel and to restrict advertising practices. Also, entry to the banking sector could be restricted on the mere basis of 'economic necessity', i.e. almost at will. These two policies went a long way towards neutralizing competition in the banking sector. Additionally, banks were required to adhere to a set of investment restrictions, aimed at reducing both maturity mismatches and lacking diversification in banks' portfolios.[10] The states' governments did not have any regulatory functions or powers. The only powers regional or local governments wielded was over the banks they were operating.[11]

Important changes to the organization of the regulatory institutions were made in 1939 and in 1944. The changes in 1939 eliminated the central banks' oversight agency and thus eliminated much of the central bank's influence on regulation and supervision. Instead, these powers were transferred directly to the Economics Ministry, giving the central government more control over regulatory matters. Indeed, the wording of the 1939 amendment was so open that, in theory, it allowed the Economic Ministry to dictate specific

[7] The only financial institutions exempt from supervision and regulation were a few special purpose banks.

[8] See Reichsgesetzblatt (1934).

[9] However, the law did not impose a minimum liquidity or capital ratio. These norms needed to be filled with life via a decree by the oversight agency.

[10] See Reichsgesetzblatt (1934).

[11] This was still a significant amount of influence over the banking sector, considering that about a third of the banking sector was government-run in the 1930s.

Table 3.1: **The German banking system in 1935**

Bank Group	**% of assets**
Public Savings Bank System[a]	**42.3%**
Incorporated Private Banks[b]	**21.4%**
Mortgage Banks[c]	**12.1%**
Cooperative Banking System[d]	**9.2%**
Private Bankers	**2.6%**
Other[e]	**12.4%**

[a]Includes the *Girozentralen* and other public *Landesbanken* and *Staatsbanken*.
[b]Includes the Berliner Großbanken, the Provinzbanken and the Spezial- und Hausbanken.
[c]Includes pure mortgage banks, mixed mortgage banks and the *Landschaften*.
[d]Includes all Kreditgenossenschaften and Zentralkassen.
[e]The most important banks in this category are government ones with specific functions such as the Golddiskontbank.

Source: Own calculations based on data from Deutsche Bundesbank (1976, p. 121).

business policies to individual banks.[12] The banking commissioner was also renamed into the supervisory agency (the *Reichsaufsichtsamt*). In 1944, the central bank regained some regulatory powers, as the supervisory agency was dissolved. Most of the agency's functions were transferred to the Economics Ministry, but some of these functions went to the central bank directorate.[13]

3.3 Allied regulatory changes (1945-1948)

After the Second World War, the Credit Act of 1934 was still the basic guideline for the regulatory framework of the banking system in Germany.[14] However, three things made regulatory matters problematic. First, as mentioned above, the Credit Act had been amended several times during Nazi rule.[15] Second, with the end of World War II the Allied occupying forces had assumed supreme command. Consequently, all the central government bodies ceased to exist, including the centralized regulatory bodies.[16] And third, new laws or proclamations regarding banking regulation were passed by either the Allies or the states' legislatures (on behalf of the Allies). Most importantly, military laws transferred the competency for money and credit (and thus banking regulation) from the

[12]See for example the blanket clause in §30 of Reichsgesetzblatt (1939a).
[13]For details see Reichsgesetzblatt (1939a), Reichsgesetzblatt (1939b) and Reichsgesetzblatt (1944). For an overview of all the ordinances passed between 1934 and 1945 with respect to banking regulation see Hofmann (1949, pp. 179-370) and Koch and Roeder (1938).
[14](West-)Germany was considered the legal successor of the Third Reich and the Weimar Republic. Hence, the majority of the laws still applied. See for example Stolleis (2008).
[15]Important changes were made in 1939 and 1944. See section 3.2 on page 107 for the changes.
[16]Technically, the Reichsbank still existed, but its central operations were shut down.

TABLE 3.2: **The German regulatory structure before World War II**

	1934	**1939**	**1944**
Supervisory Office	Regulatory guidelines and emergency actions	Dissolved	Dissolved
Banking Commissioner	Policy implementation	Policy implementation	Dissolved
Central Bank	Balance sheet analysis	Balance sheet analysis	Balance sheet analysis and policy implementation[a]
Economics Minister	-	Regulatory guidelines; emergency actions[b]	Regulatory guidelines and implementation.

[a]The central bank directorate could exempt banks from a wide range of regulations. For key aspects approval by the Economics Minister was necessary. See Reichsgesetzblatt (1944) in combination with Reichsgesetzblatt (1939b).

[b]Addionally, the Economic minister had the power to directly prescribe banks how to manage their business. See §30 of Reichsgesetzblatt (1939a).

Source: Own elaboration based on the relevant legislation: Reichsgesetzblatt (1934), Reichsgesetzblatt (1939a), Reichsgesetzblatt (1939b), Reichsgesetzblatt (1940) and Reichsgesetzblatt (1944).

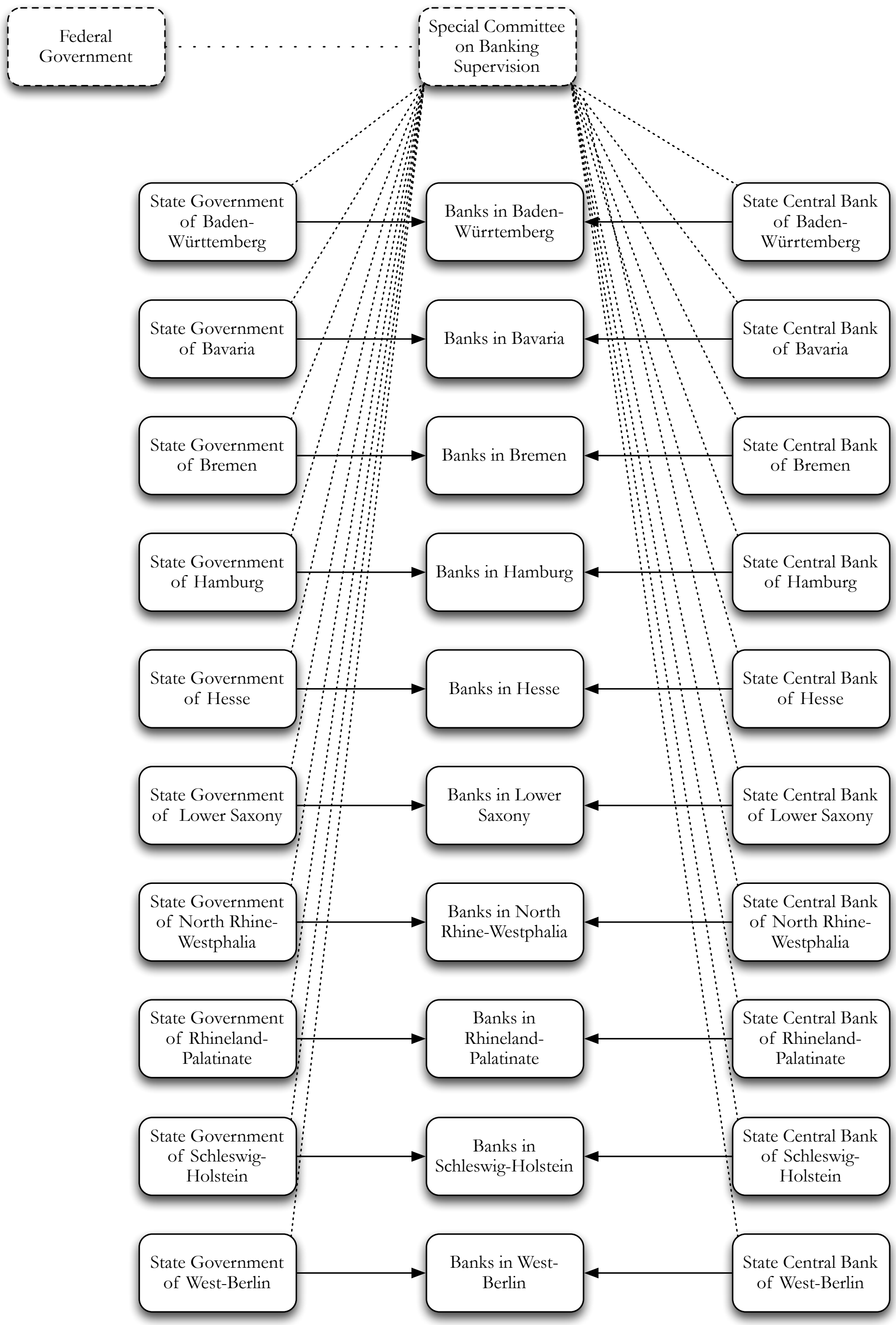
auspices of the non-existing central Economics Ministry and the Reichsbank to the Finance Ministries and central banks of the various states.[17] Thus, the Allies decentralized the regulatory institutions of the German banking system and they broke with German administrative tradition by instigating a transfer of competences.[18] These factors created a situation of legal uncertainty, where banking regulation was not uniformly applied throughout the states. Apart from different day-to-day operations, the Credit Act contained blank provisions for capital and liquidity ratios (amongst others). These needed to be filled out by the regulatory institutions. In theory, each state's supervisory institution could set different capital and liquidity ratios.[19]

[17]See BArch B102/23052, Letter from Fischer to Kattenstroth from 31.01.1950. For an overview of the laws, decrees and ordinances see table 3.3 on page 112. Generally, the finance ministries were assigned the qualitative aspects and the state central banks the quantitative or statistical aspects of regulation and supervision. For a chronological overview of the changes see Honold (1956, pp. 75–76). It was also the finance ministries who were now responsible to uphold and enforce interest rate restrictions. See Ambrosius (1998, p. 164).

[18]For the intentions of the Allies see Horstmann (1991).

[19]The Allies expected each German state to pass laws to regulate the banking sector. An attempt was made by the *Länderrat* of the U.S. zone, which forwarded a draft on 04.11.1947 to the American military government. It was meant to amend the existing law to clarify the regulatory and supervisory competences. The draft was withheld by the American military government, because of the impending introduction of a central bank. See OMGUS (1949a, Art. II, Law Nr. 57 (revised)) and BArch B126/12141, Memo "Bank Deutscher Länder und Bankenaufsicht" by Lubowski from 03.06.1948

FIGURE 3.1: **Schematic overview of the regulatory arrangement in West-Germany (1948–1961)**



Banking regulation was restricted to the state level. The special committee of banking supervision was a consultative body only that was meant to aid to harmonize regulatory and supervisory practice. It could not issue binding resolutions. Officials from the Federal government participated in its meetings merely in an advisory function. Note that the number of state boundaries changed throughout this period. This chart assumes state boundaries as existing in 1952. *Source: Own elaboration.*

Table 3.3: **Laws that formed the basis for banking regulation in Germany after the Second World War**

Credit Act	Credit Act from 25.09.1939		
	Credit Act in its amended form from 18.09.1944		
Regulatory Decentralization			
	U.S. zone:		
		Bavaria	Law Nr. 54 from 27.09.1946
		Bremen	Senate Ordinance from 21.02.1947
		Hesse	Military Decree Nr. 4 from 20.10.1945
		Württ.-Baden	Law Nr. 50 from 12.03.1946
	U.K. zone:		Military Decrees Nr. 18 & Nr. 133
	F zone:		Military Decree Nr. 208
		Baden	Ordinance from 12.03.1946
		Rheinland-Pfalz	Finance Ministry Ordinance from 13.01.1949
		Württ.-Hohenzollern	Ordinance from 12.03.1946
BdL Laws			
	U.S. zone:		Military Law Nr. 60 (revised)
	U.K. zone:		Military Ordinance Nr. 129
	F zone:		Military Decree Nr. 155a
State Central Bank Act			
	U.S. zone:		Military Law Nr. 66
	U.K. zone:		Military Ordinance Nr. 132
	F zone:		Military Decree Nr. 209
2nd Currency Act			
	U.S. zone:		Military Law Nr. 62
	U.K. zone:		Military Ordinance Nr. 62
	F zone:		Military Decree Nr. 159
Bank Decentralization Laws			
	U.S. zone:		Military Law Nr. 57 (revised)
	U.K. zone:		Military Ordinance Nr. 133
	F zone:		Military Decree Nr. 208
Decartelization Laws			
	U.S. zone:		Military Law Nr. 56
	U.K. zone:		Military Ordinance Nr. 78
	F zone:		–

Sources: Honold (1956, pp. 75–76) and BArch B102/41900, Statement of grounds for a Draft Credit Act from 30.05.1949 and from 30.09.1951.

First unofficial German proposals for a reform of the Credit Act of 1934 were made as early as 1946.[20] But it was only in the spring of 1948, that the Americans began pushing the German authorities towards drafting a new Credit Act for the whole of Germany that would replace the numerous laws and directives that constituted the basis for German banking regulation.[21] When the Americans pressed the Germans for a new Credit Act, they initially wanted to see two important structural features to be implemented. First,

[20] One of the first proposals stemmed from the former Commissioner of the banking sector, Friedrich Ernst. See BArch B102/23052, Letter from Fischer to Kattenstroth from 31.01.1950.

[21] See BArch B102/4190, Minutes from the meetings of the Special Committee on Banking Regulation on 21.05.1948, 12.10.1948 and 16.11.1948.

they wanted banking regulation to maintain its decentralized structure, with the states being the main regulators. Second, they wanted the central bank to focus exclusively on monetary policy and to have no influence over supervisory matters. The Americans explicitly wanted the Germans to adopt a two-tier regulatory framework, where the state governments would be in charge of qualitative regulatory matters and the state central banks in charge of quantitative matters.[22]

3.4 First drafts (1948-1953)

Work on a new Credit Act began by the end of 1948 under the auspices of the Bank deutscher Länder (henceforth just 'BdL') – the new central bank that had been founded earlier that year. After all, the BdL was the only German institution covering the three western zones at that time. In this process, the BdL cooperated with the Special Committee on Banking Supervision (the *Sonderausschuß Bankenaufsicht*).[23] It was an informal body created to harmonize regulatory practices throughout the German states, by bringing together the relevant regulatory agencies of all states. Given its informal character, any decisions taken by this body were non-binding.[24]

Over a period of two years, a preliminary Credit Act draft was prepared. During the deliberations, the Credit Act of 1934 (in its amended 1939 form) was used as the basis for discussion.[25] This first official draft was drawn up by the central bank in association with the various state regulatory agencies. While the representatives from the Federal Finance Ministry attended the discussions as of the fall of 1949, the federal government did not get actively involved. Additionally, neither the public nor the banks were given access to these discussions. This attracted sharp criticism from the banking sector, both for the lack of practical experience and the contents of the draft. Influential representatives of the banking sector complained to Economics Minister Ludwig Erhard that

> *'[...]a bureaucracy without leadership celebrates orgies'*

[22] See BArch B102 / 41900, Section A of the Statement of grounds for a Draft Credit Act from 30.05.1949.

[23] As of the fall of 1949, the BdL-led Commission was joined by experts from the central government's Finance Ministry.

[24] For the minutes of the meetings of the Special Committee on Banking Supervision see BArch B126/7401, 12141, 12142, 12143, and 26185.

[25] See for example BArch B102/41901, Appendix to the Statement of grounds for a draft Credit Act from 30.09.1951.

and that

> *'if one glanced at the current draft one could get the impression that the entire banking sector is in the hands of criminals or, alternatively, that the sector is about to be subjected to softening-up barrage in preparation for an all-out attack, leading to socialization.'*[26]

The draft was not quite as extreme as these representatives from the banking sector made it sound like.[27] However, in line with American demands, the draft foresaw the continued decentralization of banking regulation, which was seen by these private bankers as a most undesirable feature. Additionally, the Credit Act draft changed the scope of some norms in order for them to be compatible with the new constitution (the *Grundgesetz*).[28] Nevertheless, a working group of the associations private banks prepared its own draft law and presented it to the federal government. However it was of little impact.[29] What made matters even more complex, was the fact that several political issues, that potentially would have a significant effect on a new credit act, were still pending.

First, with the help of military laws (decrees) the Allies had decentralized the German banking sector by introducing barriers to interstate branching and by breaking up the three largest banks into 30 state-level banks. This decentralization would, eventually, have to be codified by a democratically legitimized law. The Allies wanted to see this

[26]The German original is as follows: *"[...] die Bürokratie, die keine Führung hat, feiert sonst Orgien"* and *"Wenn man den Text überfliegt, könnte man zu dem Ergebnis kommen, daß die gesamte Kreditwirtschaft nur von Verbrechern geleitet wird, oder aber, daß sie in ihrem Gesamtumfange langsam für die Sozialisierung sturmreif gemacht werden soll."* See BArch B102/41902, Letters from Pferdmenges to Erhard and from Rath to Pferdmenges from 21.04.1950 and 19.04.1950, respectively. See also BArch B136/1216, Letter from Scheliha to Rust from 24.03.1950. Similar complaints were made by other banking associations as well. See for example BArch 126/1216, p. 24, Letter of the Working Group of the Mortgage Banks from 24.03.1950.

[27]Even so, representatives of the private banking associations prepared a draft, which they forwarded to the government. This draft was found little attention within the Finance Ministry. For the draft see BArch B102/41899.

[28]See BArch B102/41901, Statements of grounds of the Draft of a Federal Credit Act from 30.09.1951.

[29]The draft law of the working group can be found in B102/41899. In the same folder, see also the letter from Henckel to von Rauschenplat from 19.12.1950, in which he acknowledges the receipt of the draft, but at the same time urges the private banks to remain patient with their demands for a centralized regulatory regime. He pointed out that the states were currently dominating the drafting process, but the federal government would soon take over the initiative.

codification to happen under their control, before full legislative autonomy would be returned to Germany.[30] Some kind of reversal of the decentralization – which the German private banks vigorously lobbied for – was nevertheless a possibility. Second, the transfer of competence for money and credit from the Economics to the Finance Ministry by the Allies was considered a preliminary measure. Settling this issue had an impact on which Ministry would eventually be in charge of regulating the banking sector. Third, an Antitrust Act, subject to Allied approval, had to be passed by the German parliament as well. The pre-war Credit Act allowed for a government-enforced cartelized banking sector. If the future Antitrust Act were to be as restrictive as the American Antitrust Act, many key provisions in the Credit Act might be incompatible with the Antitrust Act. Similarly, the interpretation of the constitutional clause of economic freedom ('Gewerbefreiheit'), potentially affected a clause limiting entry to the banking sector. Last but not least, the BdL was a provisional central bank. It was founded before the Federal Republic of Germany had been and article 88 of the German constitution stated that a new Central Bank Act needed to be passed.[31] Depending on the structure of the central bank and the norms provided in the corresponding Act, the regulatory framework might be affected. It was certainly a possibility that none of the issues at hand would change much from the American imposed status quo. But the general expectation was that in the near future there would be some substantial change in either of these areas.[32] Irrespective of these uncertainties, a first draft for a new Credit Act was officially presented to the central government in the fall of 1951.[33]

At this time, however, the German Economics and Finance Ministries were engaged in a fierce struggle for competence over money and credit matters. This struggle had its origins well before the founding of the Federal Republic of Germany[34] and broke out in the open at the end of 1949, when the Minister of Economy Ludwig Erhard openly demanded to transfer the competence for money and credit from the Finance back to the Economics

[30] The founding of the Federal Republic of Germany in 1949 and the declaration of the Occupation Statute and the signing of the subsequent Petersberg Accords, limited legislative autonomy had been returned to the Germans. Autonomy would be expanded even further when the Occupation Statute was revised in the spring of 1951. Nevertheless the Allies formally retained veto powers in what they considered important legislative aspects such as in the field of decartelization and deconcentration.

[31] See Bundesgesetzblatt (1949, Artikel 88).

[32] See for example Adler (1949) for the notion that change was in the air.

[33] The draft had no official character as the BdL was not in a position to introduce official legislative drafts. In its statement of grounds, the draftees also stated that a new Credit Act should only be enacted, once both a Central Bank Act and a Branch Restriction Act had been passed. See BArch B102/41901, Statements of grounds of the Draft of a Federal Credit Act from 30.09.1951.

[34] See BArch B102/23051, Memorandum by Dr. Martini from 14.09.1948.

Ministry – in line with German bureaucratic tradition.[35] Eventually, the bureaucratic tradition was restored both on a federal and on a state level. However, the struggle was only resolved in the spring of 1952 and the transition period would prove to be a long one.[36]

Even though the decision to reinstate the Economics Ministry's competence in terms of money and credit was taken in the spring of 1952, formal transition would only occur in the summer of 1952. And even then the Federal Ministry of Economics needed several months to bring its newly founded division VI for money and credit up to speed. Skilled and experienced bureaucrats were in short supply. The Economics Ministry went through significant efforts in order to identify individuals that had worked either in the Economics Ministry's former division for money and credit or within the regulatory institutions, prior to the Second World War.[37] Eventually, the ministry was able to enlist the services of a handful of experienced bureaucrats, including those of of Dr. Heinrich Schreihage and Heinz Kalkstein. Both of whom had not only worked within the regulatory institutions before the Second World War, but also with the BdL after the Second World War. While at the BdL, both men were involved in the first draft of a new Credit Act.[38] Within the Economics Ministry, Kalkstein became the head of Department 5, in charge of matters relating to the savings banks and other public banks. Schreihage was assigned the position of the head of Department 3, for general questions relating to the banking system. It was to be a one-man department. This made Schreihage the sole advisor for matters relating to the Credit Act at first. Every matter with respect to the Credit Act had to be run by him.[39] There was also a considerable change in personnel with the state supervisory institutions, as the changes at the federal level were mirrored at the state level. Thus,

[35] See BArch B102/23051, *"Kabinettsvorlage zur Geschäftsverteilung auf dem Gebiete der Wirtschaftspolitik"* from 24.11.1949.

[36] At one point during this struggle, Erhard implicitly flirted with resignation if he were not given the competence over money and credit. See BArch B102/23052, Letter from Erhard to Adenauer from 23.09.1950. See Löffler (2002, pp. 368–391) for an in-depth discussion of the struggle for competence and BArch B102/23051, 23052, 23054, 23055 and 23056 for the original files.

[37] As a matter of fact, the Ministry's headhunting drive already began well before it could be certain that the competences for Money and Credit would be transferred, albeit with little success. Only when competence was transferred, could it persuade targeted individuals to join the Ministry of Economics. See BArch B102/42911, correspondence with Fischer from 23.02.1950, 25.02.1950, 27.02.1950, 17.03.1950, 06.04.1950, 11.04.1950 and 19.06.1951

[38] For detailed biographies of Kalkstein and Schreihage see BArch B126/16984, I7038, cited in Löffler (2002, FN 126 on pp. 399–400). Both had previously declined offers to join the Economics Ministry, since it did not have the competence over money and credit. See also BArch B102/42911, Letters from Fischer on 27.02.1950 and 17.03.1950.

[39] For the composition of Schreihage's department and its responsibilities see BArch B102/23080, Undated questionnaire, Division VI, Department 3.

supervision of the banks was transferred from the states' finance ministries to the states' economics ministries. As a consequence, many senior state regulators left the regulatory field altogether, since they were presumably anticipating a recentralization of all regulatory and supervisory powers with the federal government in the near future.[40]

Another intriguing aspect of the transfer of competence is that parts of the press speculated openly about whether the regulation of banks might be minimized or even scrapped altogether. After all, the press argued, the free market doctrine carried significant weight within the Economics Ministry, as the Ministry was led by Ludwig Erhard and by Alfred Müller-Armack, two prominent sympathizers of free market ideas of the time. And in a free market the banking system needed little to no supervision.[41]

Work on a new Credit Act effectively stalled between 1951 and 1953. The Allies did not provide any new impulses for the Germans to restart work on the Credit Act. Even more, there is evidence that Americans began to acknowledge that their policy of decentralizing banking supervision had adverse effects, and they were more than happy for Germans to return closer to their old more centralized model. The current decentralized system had led to political appointments in the supervisory agencies, rather than appointments based on knowledge and skill. [42] Instead, all the attention in terms of banking policy on both the German and the Allied side was concentrated on the roll-back of branching restrictions and the separation of the large credit banks, previously imposed by the Allies. Most of German politicians and businessmen were indignant to accept the branching restrictions and the separation of the largest credit banks imposed by the Allies. Similarly, a complete restoration of pre-World War II conditions was unacceptable to the Americans, as they considered the break-up of the three large credit banks as a stellar achievement in terms of the decentralization of financial power. Eventually, a partial roll-back was agreed upon in the spring of 1952.[43] From then on, the Allies left banking matters entirely in the hands

[40]See BArch B102/41902, Memo from 26.08.1952, which warns of a collapse of the states' supervisory institutions, caused by an exodus of experienced supervisors.

[41]See BArch B102/41886, Memo by Schreihage from 15.02.1954. Alfred Müller-Armack was the head of the influential policy division, the *Grundsatzabteilung*.

[42]See Memo by Warner to Lowell and Pumphrey from 09.02.1950 and Memo from Klopstock to Pumphrey from 02.02.1950 in NARA, RG 466, Decartelization and Deconcentration Division, Subject Files, 1948-55, folder 'Banking Deconcentration 1950' box 1. State regulators also failed to enforce the interest rate restrictions, leading to unofficial, or 'grey', deposit rates. See Franke (1999, p. 257).

[43]See the minutes of the negotiations between the Allied High Commission and the German Government (FIN/FED/M(50-51)), for example in NARA, Record Group 84, Germany, Berlin Mission, AK Secretariat, Classified Files 1945-1990, box 107. As part of the negotiations with the Allies over the partial lifting on branching restrictions, the German government had promised not to modify branching restrictions within the next three years. Additionally, it would try to implement a few other measures the Allies wanted to

of the Germans.

Also, it must be kept in mind, that the turn of the decade was an economically and politically highly uncertain period. Important policy decisions were being debated that were to define the parameters for the future German economic and political structure. The so-called *Wirtschaftswunder* (economic miracle)[44] had to overcome numerous hurdles, such as the Korea Crisis, the reintegration of Germany into the international economic system or the settlement of claims with interwar debtors and compensation for Jewish victims during the war. Only afterwards could the 'economic miracle' begin to unfold. Some measure of normality returned to the German political and economic scene only in 1953, when the legislative period came to an end.[45]

Thus, by the end of the first legislative period in 1953, Germany had not come closer to passing a new Credit Act, despite the Allies' initial wishes to do so. Only a draft Credit Act had been prepared by a group of experts, without any involvement of the banks or the public. It essentially incorporated the status quo (and thus Allied demands) into the existing German framework of banking regulation. However, this draft was of little impact, as the Finance and the Economics Ministry fought a bitter and prolonged struggle for competence. At the same time the Allies and Germans wrangled over the liberalization of branching restrictions and the passage of an American-style Antitrust Act. This was flanked by an array of crucial political and economic developments, that put the drafting of a new Credit Act firmly in the back seat. Officially, the banking sector was 'regulated' after all – the quality of which was another (controversial) question altogether. However, the transfer of competence from the Finance to the Economics Ministry and the subsequent headhunting activities for 'experienced' personnel set important precedents for future work on a Credit Act.

transplant to Germany, such as a tighter restriction of proxy voting and the introduction of registered shares. See the Letter from Adenauer to the Allied High Commission from 27.03.1952 in NARA Record Group 466, Records of the US Representative to the HICOM Law Committee, Box 2. For the act that partially lifted the branching restrictions see Bundesgesetzblatt (1952). See also Horstmann (1991, pp. 219–286).

[44]See Ritschl (2005) for the economic miracle that was not.

[45]See Tooze (2011) for an account of this time period and all the challenges that German policymakers needed to tackle simultaneously.

3.5 Internal Disagreements within the Economics Ministry (1954-1956)

After the general election in the fall of 1953, work on a 'new' Credit Act was taken up in earnest by Schreihage again. By 1953, Allied influence in terms of banking regulation was minimal. It was clear that the Allies would return full legislative sovereignty to Germany soon.[46] Already earlier, the Americans had made it known to the German authorities, that they would not oppose a recentralization of supervisory institutions. Schreihage undertook a fresh start to the Credit Act, now that he was essentially free of Allied restrictions. Instead of using the BdL draft of 1951, Schreihage went back to the drawing board, using the proceedings of the German banking commission from 1934 and the Credit Act of 1934 (in its 1939 form) as his starting point.[47]

Over the next few years, Schreihage would be in regular contact with the Federal Association of the Private Banks (*Bundesverband des Privaten Bankgewerbes*). This was not because of Schreihage's sudden affinity with the private banking sector. It was because Minister of the Economy, Ludwig Erhard, had a slightly more integrative approach than his fellow Finance Minister, Schäffer, when it came to business associations.[48] And it was also because the private banking sector was able to enlist the services of Friedrich Ernst, the former Commissioner for the Banking Sector, who was probably the most respected German expert in terms of Banking Regulation at the time. In mid-1954, the Federal Association of the Private Banks created a special Credit Act Commission (*Kommission für die Neufassung des Kreditwesengesetzes*) under the chairmanship of Ernst. Its task was to study the current regulatory framework and propose changes that were to be implemented in a new Credit Act, in an effort to influence the decision making process within the Economics Ministry.[49] After the second meeting of the Credit Act Commission, Ernst

[46]The three Allies and Germany had signed the *Deutschlandvertrag* on the 26.05.1952, which gave Germany full legislative autonomy, once it entered into force on the 5th of May 1955.

[47]See BArch B102/41899, Thank you note from Schreihage to the Economics Minister of Lower Saxony from 11.10.1954 as well as an opinion piece by Schreihage (1961) in which he acknowledges the Credit Act of 1934 as the starting point.

[48]At one point Adenauer even criticizes the Economics Ministry for being too close to the banks, for being too passive and not political enough. See Löffler (2002, p. 389). This statement of Adenauer's is somewhat ironic, since one of his main advisors in economic matters was the banker Robert Pferdmenges, the head of the of the private credit bank association in the 1950s. See for example Die Zeit (1953).

[49]See BArch B102/41893, Minutes of the first meeting of the commission for the new Credit Act draft from 12.07.1954.

invited Schreihage to take part in the commission's meetings.[50] And indeed, Schreihage would become a regular attendee throughout the period from 1954 until 1958.[51]

In the first meetings, the old Credit Act was discussed in minutiae detail; paragraph per paragraph. The merit and demerit of every norm was laid out. In the later years, Schreihage would sometimes present and discuss changes to the Ministry's unofficial draft with the committee. Ernst, and thus the private banks, could be certain to have Schreihage's attention. The key points the private credit banks' association wanted the new Credit Act to reflect, were already decided upon in the first two meetings of the commission. Schreihage was not present at these meetings, but the minutes of the meeting were forwarded to him a few weeks after they had taken place. Ernst also had a personal conversation with Schreihage outlining the private credit banks' position. The commission supported a return to a unified regulatory structure and it was also in favor for a continued restriction to competition. It wanted the state sponsored interest rate cartel, the restrictions to entry, and the restrictions to advertising practices to be upheld. Furthermore, the commission criticized the expansion of the public banking sector and wanted the federal regulator to be given the power to limit the scope of activities the *Sparkassen* were allowed to engage in. The competitive threat from the public banking sector is also the primary reason that the private credit banks wanted a continued restriction to competition.[52]

The private banks, were not the only institution Schreihage discussed regulatory matters with. He also traveled to the central bank on a regular basis.[53] The Federation of the Savings Banks also created a corresponding Credit Act Panel (*Arbeitsausschuss KWG des Deutschen Sparkassen und Giroverbandes e.V.*). Schreihage attended several of these meetings as well, but they only began in late 1955 and they did not take place with the same frequency as the private credit banks' commission.[54] Thus, the private credit banks had a significant first mover advantage over the savings banks. On top of that, the private credit banks had the former banking commissioner Ernst on their side, giving them a much better position to influence Schreihage and consequently the Economics Ministry. It was

[50]See BArch B102/41893, Memo VI 3 - 15483/54 by Schreihage from 22.09.1954.

[51]See the various minutes of the meetings of the commission in BArch B102/41893, 41894, 41895 and 41896. Meetings took place roughly on a monthly basis.

[52]See BArch B102/41893, Minutes of the first meeting of the commission for the new Credit Act draft from 12.07.1954, and BArch B102/41893, Memo VI 3 - 15483/54 by Schreihage from 22.09.1954.

[53]On many occasions he would combine a visit to the Commission of the private banks with a visit to the central bank directorate, as both were located in Frankfurt am Main.

[54]See the memos of Schreihage and the minutes of the meetings of the Credit Act Panel in BArch B102/41898.

also no secret that the Economics Ministry favored private over public initiative and thus would be more likely to attend to the private banking sector's demands than to the public banking sector's. The savings banks were aware of their strategic disadvantage vis-a-vis the private banking sector. Nevertheless they decided to press for important regulatory concessions. Ideally, they wanted the *Sparkassen* to be exempt from federal supervision altogether, but they were aware that this was unacceptable to the Economics Ministry. As a second best alternative, they hoped for the *Sparkassen* to be exempt key regulatory norms, such as capital and liquidity requirements. After all, because of their statutes the *Sparkassen* did not have any capital (only reserves), but they had the financial guarantee of the respective local government. They wanted this financial backing by the government to be recognized in the Credit Act. Of course, exempting them from these norms would give them important competitive advantages over private sector banks.[55]

The credit cooperatives, too, had set up a Special Committee on Banking Supervision (*Sonderausschuss Bankenaufsicht*). However there is little evidence to suggest that Schreihage regularly attended their meetings or that minutes of those meetings were sent to him.[56] Thus, this indicates that the private credit banks were the banking group in Germany that had the best opportunities to influence the regulatory decision making process within the Economics Ministry. Another important aspect of the initial drafting process is that it took place without any major influence from the German federal states. Even though Schreihage attended the meetings of the states' Special Committee on Banking Supervision[57] as an official representative from the Federal Economics Ministry, he would only report on the latest developments. Rarely did engaging discussions ensue about the future structure of the regulatory system.[58]

The Economics Ministry's contact with the banking associations at such an early stage in the drafting process was certainly unusual, but it was not exceptional. In the case of the Antitrust Act, Erhard and his Ministry had even more intense contact with the

[55]See BArch B102/41898, Minutes of the Credit Act Panel meeting from 23.11.1955 and memo of the Federation of Savings Banks from 14.11.1955, AZ 7205. For Erhard's position on protecting the private sector from the public sector see for example a remark made in connection with the Antiturst Act in BArch B126/701, Letter by Erhard to subsecretary of the Chancellery, from 26.04.1952. In this letter he stresses that he wants has no intention to pass an Antitrust Act that favors the public sector at the expense of the private sector, and that he believes in fair competition between the public and private enterprises.

[56]The only mention of Schreihage traveling to take part in one of the credit cooperatives' meeting I could find is in BArch B102/41898, Memo by Schreihage from 28.09.1957.

[57]This committee had been formed in 1948 to harmonize regulatory practices between the states. See section 3.4 on page 113.

[58]See for example the minutes of the meetings of the Committee in BArch B126/ 7401.

Association of the German Industry (BDI) in 1954 and 1955. In these meetings, Erhard came to a actual agreements with the BDI on the fundamental principles of the Antitrust Act. However, he then repeatedly ignored the agreements and did not incorporate them in his ministry's subsequent drafts.[59] Furthermore, the meetings with the representatives of the banking sector had no official character.

From 1954 until 1956, the progress on a new Credit Act was slow, however, and eventually came to a standstill. No official draft was released for public scrutiny before 1957. Many key issues were subject to excruciating discussions within the Economics Ministry. This was due to fundamental disagreements within the Ministry's Division 1 (Policy) and Division 6 (Money and Credit). Division 1 was led by Alfred Müller-Armack, a prominent Economist of that time, who shared Ludwig Erhard's conviction for free markets rather than cartels. Division 6 was the division Schreihage was in, where a number of officials from the pre-war regulatory institutions worked, and who were in regular contact with the banking associations. Major disagreements between Division 1 and Division 6 were about to what extent the banking sector should be subjected to competitive pressures.[60]

Division 1 argued that the banking sector should be treated no different than other sectors as it was not inherently different from other sectors of the economy. Contrary to that Division 6 argued that the banking sector constituted indeed a special case and that this was also reflected in the draft for an Antitrust Act, which stated that the banking sector was not susceptible to automatic regulation through competition.[61] While competition was generally welcomed by Division 6, it argued that a restriction of competition in the banking sector was necessary in order to avoid a competitive race to the bottom that would destabilize the banking sector. In particular a fierce competition between the largest private credit banks and the savings bank system was feared. Furthermore it argued, the

[59] See Hüttenberger (1976, pp. 300–304), who also reports that Erhard had only grudgingly begun discussions with the BDI in the first place, possibly because he was ordered by Adenauer to engage in them. See also BArch B126/702, which contains numerous memos and minutes on the discussions between the Economics Ministry and the BDI, which document that the positions between the two sides were diametrically opposed.

[60] Division 1 originally even went as far as claiming that the Credit Act originated from National Socialist thought and for that reason alone it should be largely discarded. See BArch B102/41886, p. 1 of the Minutes of a meeting between Divisions 1 and 6 that took place on the 28.06.1955, from the 01.07.1955 (VI A 3 - 13 372/55).

[61] Interestingly, Müller-Armack countered this claim by saying that the inclusion of such a remark in the Antitrust Act's draft must have been a "mistake", which would most certainly be corrected. See Barch B102/41886, Minutes of a meeting between Divisions 1 and 6 that took place on the 28.06.1955, from the 01.07.1955 (VI A 3 - 13 372/55).

ongoing expansion of the public banking sector, which enjoyed substantial competitive advantages over the private sector banks. Division 6 was willing to shield the private banking sector from the public banking sector by restriction competition. As a result the divisions disagreed over the government's ability to limit entry to the banking sector, over whether the practice of a government-enforced interest cartel and the restrictions to competitive practices should be upheld, over whether the government should be able interfere in core decisions of the banks, such as imposing strict capital and liquidity ratios, and whether there was a clear enough division between banking supervision and monetary policy. The only fundamental issue they agreed on was that if there was to be regulation of the banking sector, it should be at the federal level.[62]

A most interesting aspect of the Division 1's struggle for less regulation and more competitive pressure in the banking system, was a proposal to abolish most of the regulatory restrictions limiting competition and instead to introduce deposit insurance as a measure of neutralizing competitive advantages. Paired with an effective Antitrust Act, it should remove fears of either monopolies or cut-throat-competition, Müller-Armack argued.[63] The two divisions were unable to resolve their key disagreements over the restrictions to competition in the banking sector, until the end of 1957.[64]

Also, during this period, the ministry was working intensively on a new Antitrust Act and on a new Central Bank Act. Both these laws were considered a priority over the Credit Act. However, work on them took much longer than originally anticipated.[65] As long as these two laws were not passed, the government was hesitant to put forward a new Credit Act. After all, there was considerable interaction between these acts. The future structure of the central bank influenced the possibilities for cooperation between the regulatory agencies. The stringency of the Antitrust Act restricted the options for government intervention in the banking sector. If, for example, the Antitrust Act banned all cartels, a government-enforced interest rate cartel in the banking sector, as it had been the norm since 1931, would not be permissible.

[62] See BArch B102/41886, Memo by Schreihage to the head of Division 1 from 11.05.1955 (VI A 3 - 13 205/55).

[63] See BArch B102/41886, Page five of the minutes of a meeting between Divisions 1 and 6 on the 28.06.1955 from the 01.07.1955 (VI A 3 - 13 372/55).

[64] See BArch B102/41887, Letter from Müller-Armack to Division VI from 09.12.1957.

[65] See Hüttenberger (1976) and Murach-Brand (2004) for accounts of the origins of the German Antitrust Act of 1957.

Overall, the mid-1950s were characterized by two developments: First, a regular exchange of opinions between the Economics Ministry and the private credit banks' association (and to a lesser extent with the savings bank system). And second, fundamental disagreements within the Economics Ministry on whether to re-establish the old cartelized regulatory system, or whether to loosen the grip on the banking system and thus allowing for more competitive pressures. Work on a new Credit Act was only third in line during this period, behind a new Central Bank Act and a new Antitrust Act, which further helps to explain the slow progress. It is in 1955 that Germany regained unrestricted legislative sovereignty, thus freeing itself completely from Allied influence. In terms of banking regulation, the Allied grip had already loosened considerably by the beginning of the 1950s and ceased with the codification of regional branching restrictions into a democratic law in 1952.

3.6 A failed centralization attempt (1957)

In order to make at least some progress before the end of the legislative period in 1957, a decision was taken in November of 1956 to press through the one regulatory aspect that the entire Economics Ministry, all the federal Government Ministries and the lower house of parliament (the *Bundestag*) could agree on: The (re-)centralization of banking supervision.[66] An important rationale for pushing ahead with the re-centralization of regulatory supervision, was the fact that the parliament lifted branching restrictions on banks entirely at the end of 1956.[67] It was certain that the largest commercial banks, which had been decentralized by the Allies in 1948 and who had been allowed to partially re-centralize in 1953, would merge in 1957 and thus re-establish national operations. Both the Economics Ministry and the *Bundestag's* Committee for Money and Credit argued that nationally operating banks could only be supervised efficiently by a national supervisory agency.[68]

A brief draft of five paragraphs was drawn up that would create a single Federal Supvervisory Office for the Banking Sector (a *Bundesaufsichtsamt für das Kreditwesen*) in

[66] The *Bundestag*'s Committee for Money and Credit (also known as the 'Scharnberg Committee') was strongly in favor of a recentralization. See for example BArch B102/23342, Confidential Memo from Henckel to Erhard and Westrick from 30.11.1956 and Letter from Scharenberg to Erhard from 26.11.1956.

[67] For the law scrapping branching restrictions entirely see Bundesgesetzblatt (1956).

[68] See BArch B102/23342, Confidential Memo from Henckel to Erhard and Westrick from 30.11.1956, and Cabinet proposal by Erhard that includes a draft bill from 20.12.1956.

anticipation of a comprehensive new Credit Act, which was to follow a few years later. The draft would essentially reinstate the Credit Act of 1934 in its amended form of 1939[69] When the draft was made public, it amounted to a surprise move by the central government.[70]

It was public knowledge that the German states (represented in the upper house of parliament the *Bundesrat*) would oppose any law that attempted to take their regulatory privileges away from them. However, the central bank, the BdL, also voiced its strong opposition towards the pre-emptive measure. It argued that the Credit Act should be passed as a whole, and not in a piecemeal manner. Also, the decision of whether the regulation of the entire banking system should be centralized or decentralized, did, in the eyes of the BdL, depend on whether the future central bank would have a central or decentral structure. Consequently, the central government should wait until the passage of the Central Bank Act before taking any regulatory measures. The central bank also disagreed with the notion that a centralized regulatory system was needed to supervise the large credit banks, which were operating throughout the country. Quite the contrary, it argued that a decentralized system would be better able to supervise a banking system that had become more complex since the 1930s. Another major critique was the proposed re-enactment of the Credit Act of 1934 with the 1939 amendment. The 1939 amendment robbed the central bank of most of its influence over regulatory affairs. Instead, the BdL argued, parliament should reenact the Credit Act of 1934 in its 1944 version. The amendment of 1944 had reinstated the central bank's influence, without burdening it with day-to-day supervisory tasks.[71] Additionally, the headquarters of the proposed federal regulatory agency was supposed to be in Bonn, the seat of the government, instead of Frankfurt, where the BdL and the majority of the large banks had their headquarters. The BdL objected to this as it would hinder cooperation between the two regulatory institutions. In sum, the BdL painted a bleak picture of a federal regulatory agency that was without any support from the BdL expertise, in case the proposed bill was enacted.[72] Under the surface however, matters within the BdL looked a bit different. It

[69] A negligible amendment from 1940 was also included. For the first draft including its rationale see BArch B102/23342, Cabinet proposal by Erhard that includes a draft bill from 20.12.1956.

[70] It deemed the time as strategically advantageous. See BArch B102/23342, Draft for a Cabinet level memo from 05.01.1957, for the meeting on the 09.01.1957.

[71] For the pre-war regulatory and supervisory responsibilities see table 3.2 on page 110.

[72] See BArch B102/23342, Minutes of the 234th meeting of the board of the central bank from 9.-10.01.1957; the report of Schreihage's business trip to Frankfurt from 16.01.1957 and the letter of the BdL directorate to Erhard from 25.01.1957 as well as B102/23344, Letter from Pfleiderer to Dermitzel from 04.05.1957.

was the board of the central bank, whose members were the presidents of the state central banks and naturally closer to the states' interests, who objected strongly to the proposed centralization. The directorate of the BdL, however, supported the proposed bill, but it was overruled by the central bank board.[73]

Despite the severe criticisms from *Bundesrat* and BdL, the federal government went ahead and introduced the corresponding bill to parliament. The official statement of objection by the *Bundesrat* followed along similar lines as the argumentation of the BdL. Additionally, it brought onto the field constitutional concerns that would arise if the government passed this bill.[74] Even though it was impossible to obtain the support of the *Bundesrat* on this matter, the Economics Ministry was confident that it could pass the bill with a two-thirds majority in the *Bundestag*.[75] For the remainder of the legislative period a bickering over the seat of the future Federal Supervsiory Office took place. At first, it was a struggle between Bonn and Frankfurt, and eventually the possibility of basing the supervisory office in Berlin was thrown in the ring as well. It was a highly political decision that needed to be taken at that time.[76] However no compromise could be reached before the end of the legislative period that would have secured the necessary two-thirds majority.

What further hindered last minute legislative re-centralization of the regulatory institutions was the fact that two other crucial bills were also making its way through parliament hoping to make a spot landing: the Antitrust bill and the Central Bank bill. These had priority over supervisory matters. Whatever political capital was left during this legislative period was spent on their passage.[77] Throughout the drafting process, the Antitrust Act changed almost radically, from a virtual copy of the strict American Antitrust legislation that prohibited all cartels, as Erhard originally wanted it, to one that

[73]See BArch B102/23343, Memo by Henckel for Erhard and Westrick from 08.02.1957.

[74]Amongst them concerns that the reinstated 1934 Credit Act in its amended form of 1939 would contain provisions that were incompatible with the current federal constitution. For details see the bill and the official statements of the central government and the *Bundesrat* in "Deutscher Bundestag, 2. Wahlperiode, 1953, Drucksache 3264, Bonn, den 8. März 1957 (6 – 55101 – 1215/57 V) found in BArch B102/23342.

[75]See BArch B102/23343, Memo by Henckel for Erhard and Westrick from 08.02.1957.

[76]Government bureaucracies tended to be significantly smaller than they are now. The federal supervisory office would eventually employ around 74 people (including secretaries and janitors). Today's supervisory agency, the Federal Financial Supervisory Authority (BaFin) employs over 2000 individuals. The agency is now also in charge of the supervision of the stock market and the insurance sector. Even when taking that into consideration it amounts to an increase in personnel by a factor of almost 10. For today's personnel figure see Federal Financial Supervisory Authority (BaFin) (2011) for the 1962 figure see BArch B136/1218, newspaper article *"Bankenaufsicht nimmt Arbeit auf"* from 30.12.1961, in the Industrierkurier.

[77]See BArch B102/41898, Schreihage's remarks in the minutes of the Sparkassen's Credit Act Panel meeting from 22.06.1957.

had numerous exceptions more akin to Antitrust legislation in other European countries, as German industry and parts of the German government, sought. In particular representatives of the states, as well as a number of cabinet minister's sought exemptions for government-run companies. Initially, Ludwig Erhard could count on considerable support from within the Christian Social Union (CSU), the Christian Democratic Union (CDU), the Free Democratic Party (FDP), the Allied High Commission (AHC), as well as from small and medium sized businesses, which sought protection from large competitors.[78] However, in the early years Erhard was unable to forge a compromise between the German side and the AHC, which was reluctant to compromise on the strict, American-inspired, interpretation of Antitrust. As the process dragged on, the influence of the AHC decreased. At the same rate as the AHC withdrew from German politics, the influence of the BDI increased. Moreover, several sectors of the economy experienced significant bouts of (re-)concentration, such as the banking sector, driving the small and medium sized businesses to the side of those generally supporting cartelization, and with them substantial parts of the CDU and CSU.[79] The Antitrust Act which was eventually passed in the summer of 1957 contained a general ban on cartels. However, it included a number of sectors, which were exempted from this ban, in particular those with a strong government participation. The banking sector was one of them.[80] There is little doubt that this was included at the behest of much of the public and private banking sector, which wanted to have a continued restriction to competition.[81] This exemption in the Antitrust Act opened the way for the German government to include provisions for a government sponsored interest rate cartel in the future Credit Act.[82]

[78] The American High Commissioner thought that the German Antitrust Act could have important economic implications for the rest of Europe, too. See BArch B126/702, Letter from Erhard to Adenauer, from 01.08.1954. See also BArch B126/700, Memo about a draft Antitrust Act, from 20.10.1950

[79] See Hüttenberger (1976, pp. 293–307).

[80] Indeed, in a meeting between Schreihage and the Association of the German Industry's (BDI) Money Credit and Currency Committee, it was remarked that the industry was "jealous" of banking sector's extensive exemptions from the Antitrust Act. After all, any dedicated supervisory office for the banking sector would naturally be closer to the sectors interests than a general Antitrust authority could ever be to industry. See B102/41887, minutes of the meeting of the Money, Credit and Currency Committee of the BDI on the 10.12.1957, from the 19.12.1957.

[81] An important argument in favor of the feasibility to exempt the banking sector that was brought forward early on, was that the banks were already subject to special supervision, which made sure that no socially adverse developments took place in the sector. See for example BArch B136/701, Letter from Schäffer to Erhard, from 18.03.1952, as well as Deutscher Bundestag (1975, p. 17).

[82] Other areas that were exempted from the general ban on cartels are transportation, agriculture and forestry, banking and insurance, intellectual property rights, as well as the public utilities for electricity, gas and water. For the exemption of the banking sector from the general bans on cartels in the Antitrust Act see Bundesgesetzblatt (1957a, §102) and Deutscher Bundestag (1975, pp. 16–28). Note that the exemption of the banking sector was only included in the drafts only relatively late in the legislative process, since Erhard had tried to block this.

The Central Bank Act (*Bundesbankgesetz*) had an equally lengthy history, albeit with a more successful outcome for Erhard. It was primarily a struggle between the supporters of a centralized one-tier organizational structure, such as Erhard, and those that wanted to maintain the decentralized two-tier structure, such as the BdL itself and the German states. The Central Bank Act transformed the BdL into the *Bundesbank*, whose structure was now that of a one-tier central bank. The state central banks lost power-vis-a-vis the central bank directorate, but maintained limited functional independence from the center. This shift in power within the central bank translated into a change in the central banks' stance towards the possible recentralization of banking regulation.[83]

An alliance between the *Bundestag* and the Economics Ministry tried to re-centralize the regulatory institutions through the back door in 1957. It encountered stiff resistance from the states and from the BdL. On top of that, the *Bundestag* engulfed itself in a fruitless debate over the seat of the proposed regulatory agency. Given the already stretched capabilities of the German parliament with the passage of two major acts, just before the end of the legislative period, the centralization attempt failed. It never came to a vote as the necessary two-thirds majority could not be rallied. Nevertheless, both the successful passage of the Bundesbank Act and the Antitrust Act meant that a new Credit Act was next in line. Its passage would finally have the undivided attention of all the parties involved. Additionally, the two enacted laws finally set important parameters that would eventually allow the German federal government to reinstate the old regulatory system, if it wished to do so.

3.7 Labor and (re-)birth (1958-1961)

The central government put the Credit Act on top of its agenda after the elections in the fall of 1957. It also forced the Ministry of Economics wrangling Divisions I and VI to settle their disputes. And indeed, by the end of 1957 an agreement was reached. Competition in the banking sector was to remain restricted. No additional competitive pressures were to be introduced for the time being. There is no evidence as to why Division VI prevailed, even though Economic Minister Erhard must have sympathized with the ideas put forward by Division I. They were similar to his intellectual thinking to give market forces a greater

[83] For the Central Bank Act see Bundesgesetzblatt (1957b). For the origins of the Bundesbank Act see Hentschel (1988a,b) or the next chapter of this thesis.

role in the economy. The most likely explanation, judging by the subsequent strategy by the Economics Ministry, is a decision by Erhard, as he realized that he could not gather the necessary $\frac{2}{3}$ majority in the *Bundestag* to recentralize banking regulation, if the bill contained the free-market provisions that Division I advocated for. Also, the Antitrust Act that had just been passed and it served as an important precedent by exempting the banking sector from the general ban on cartels. If the Credit Act did not contain restrictions to competition, why exempt the banking sector in the first place from the Antitrust Act?[84] By the beginning of 1958, the first official draft for a new Credit Act was finally made public.[85]

The banking associations and all other central government ministries were once more given the opportunity to provide their inputs. Only that this time, the feedback would not take place in the intimate setting of a closed meeting, but in public.[86] It is little surprising that the private banks had few objections, and neither did the credit cooperatives. In its official statement the association representing the private credit banks largely praised the draft's conception. It especially praised the adherence to restricted competition within the banking sector. Indeed, the association argued for a permanent interest rate cartel – the draft only allowed for an interest rate cartel if it was 'economically necessary', which the private credit banks was too weak a formulation. The association also demanded a prohibition of the practice of 'revolving loans', in which short term loans from institutional investors were taken in and lent out on a long-term basis to finance investment projects. The revolving-loan practice was not subject to regulation, as the brokers did not accept deposits by the public. Moreover, the brokers began to turn into competition for the major credit banks.[87] Furthermore, in the draft the government had included a provision that restricted the usage of savings accounts to natural persona and charitable institutions only. Savings accounts were a vehicle meant to facilitate saving of the ordinary population and as such attracted a higher interest than comparable term deposits. The vast majority of these savings deposits were held with *Sparkassen*. As businesses and corporations began to invest their excess funds in these savings deposits with the *Sparkassen*, the private credit banks wanted to restrict this practice. Officially, this was meant to prevent volatile

[84]For the continuing disagreements between the Divisions I and VI, and the need for a Ministerial decision see BArch B102/41887, Müller-Armack to Abteilung VI from 09.12.1957.

[85]For the first official draft see BArch B102/41889, *"1. Referentenentwurf"* from 18.01.1958.

[86]For the different banking groups' statements on the first official draft see BArch B126/7413, B102/41895 and B102/41927.

[87]More on these revolving loans will follow, as they became a major point of discussion in parliament.

institutional funds from 'abusing' this 'privileged' type of account. Unofficially, it was of course a move to protect the private credit banks from the public banking system, and in particular it helped the private credit banks to retain their traditional clientele by the way of law.[88] The attempts by the private credit banks to protect themselves from the public banking system were founded in the public banking system's relatively strong performance in the mid to late 1950s that had arise because of a number of structural advantages. The government actively encouraged its citizens to deposit their spare money in savings accounts, which were the traditional domain of the *Sparkassen*. Furthermore, the development of an increasingly wealthy, while at the same time financially conservative middle class, greatly benefitted the *Sparkassen* as well. After all, these were traditionally customers of the *Sparkassen* and the credit cooperatives, rather than the private credit banks. An additional competitive advantage for the *Sparkassen* system came through the near universal adoption to transfer the pay cheque electronically in the 1950s. The *Sparkassen* and Credit Cooperative with their countrywide bank network and thus cost-effective payment systems benefitted greatly from this development, not least because many new customers were forced to open bank accounts, if they wanted to receive their pay cheque.[89]

The association representing the public banks raised strong objections however. They criticized continued, extensive regulatory provisions, which they deemed to be a form of direct (federal) government planning. The government's draft prescribed concrete minimum capital and liquidity ratios. The *Sparkassen* objected to these, because these ratios neither addressed the specificities of the *Sparkassen* system[90] and because such a system lacked flexibility to adjust to changing circumstances. They demanded that no concrete minimum capital or liquidity ratios should be specified in the law itself, as it was the case with the existing legislation. In a similar vein went a further critique. A ruling by the Federal Administrative Court in 1957 had already sunk the original provision that allowed the government to restrict both the establishment of banks on the basis of economic necessity

[88]See BArch B102/41895, *Stellungnahme des Bundesverbandes des Privaten Bankgewerbes (E.V.) zum Referenten-Entwurf des Bundeswirtschaftsministeriums für ein Kreditwesengesetz.*

[89]See Pohl et al. (2005, pp. 266-308). For an overview of the development of the different banking groups in the German banking system after the Second World War see figure 3.2 on page 132. Alternatively, see also Wolf (1998a, pp. 127–148).

[90]Because of their legal statutes, the *Sparkassen* did not have shareholder capital, they only had retained earnings and the backing of the government. Also, the *Sparkassen* held most of their liquidity reserves with the *Girozentralen* or *Landesbanken* and the government's draft only wanted to consider cash equivalents, such as reserves with the central bank, but not reserves held with other banks for the calculation of liquidity ratios.

as unconstitutional, as it collided with the constitutional clause that guaranteed anyone to choose its 'freedom of trade'.[91] As a consequence of this a flurry of new branches were established by banks. Now, the draft suggested that the government should retain the right to restrict new branches, though not new banks, once more. The association considered this provision as obsolete, and it argued that competitive pressure could effectively regulate the amount of branches in the country. Furthermore, the public banks' association objected to restricting savings deposits to natural personas and charitable institutions. The savings account was the most popular and most important source of funds, and they certainly did not want an artificial restriction to it. In this they were supported by the BDI.[92] While the association of the public banks continued to favor certain restrictions to competition, it was slowly abandoning this position. The public banks' strong performance in the 1950s made them aware of their competitive advantages with respect to the private credit banks. They now saw an opportunity to expand their market share at their expense and consequently toned down their demands for restrictions to competition.[93]

Junior-level deliberations amongst the different ministries and the Bundesbank (*Ressortbesprechungen*) to work out the details of the individual paragraphs began in February of 1958. The Economics Ministry installed three working groups. One for matters relating to entry restrictions, another for liquidity and capital ratios and another related to information disclosure. The proposed centralized structure of the regulatory system was not put up for fundamental discussion, however, and neither was the inclusion of the central bank in regulatory matters. The working group on the entry restrictions was made obsolete, when the ruling of the Federal Administrative Court on entry restrictions was made public.[94] The court's ruling had made it clear, that no rule restricting entry or the establishment of branches, would survive a constitutional challenge. Also, the working group on the liquidity and capital ratios had decided, at the urging of both the Bundesbank and the banking sector associations not to prescribe minimum capital and liquidity ratios

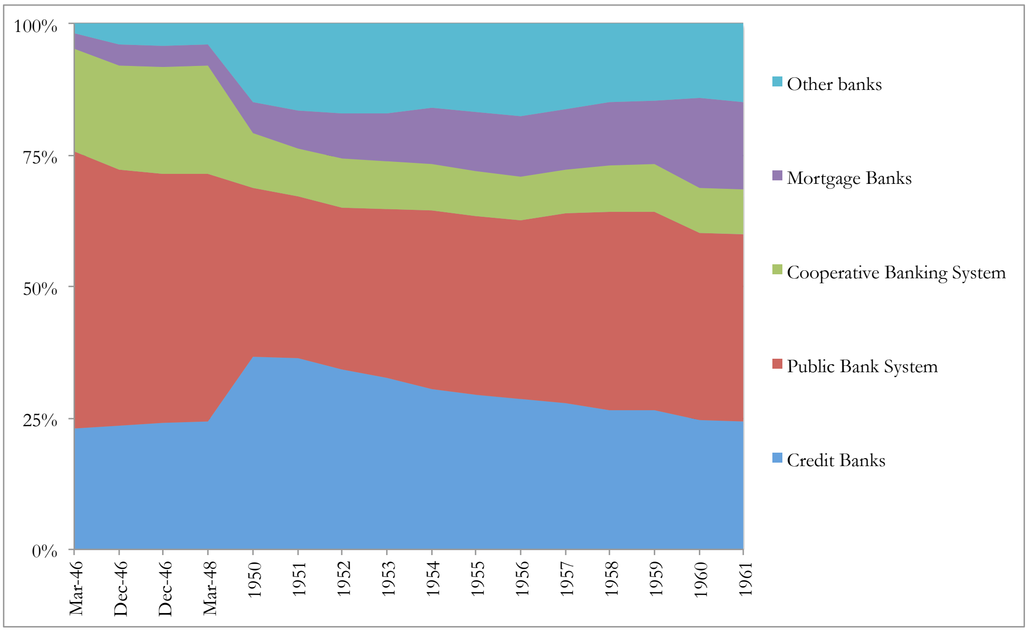
[91] For the ruling of the Federal Administrative Court see Bundesverwaltungsgericht (1958) and for the relevant clause in the constitution see Bundesgesetzblatt (1949, Art. 12, (1)). See also Pohl et al. (2005, pp. 302–303).

[92] For the official statement of the public banks' association see BArch B102/41895, *Stellungnahme des Deutschen Sparkassen- und Giroverbandes e.V. zum Referenten-Entwurf eines Gesetzes für das Kreditwesen.* For a summary of other associations' viewpoint see for example BArch B102/41927, Memo by Schreihage, from 06.03.1958, about a meeting with the various banking associations on the draft of a new Credit Act (VI A 3 - 5660/58). For the BDI's position on the savings account controversy see BArch B102/41930, Letter from the BDI to Schreihage, from 02.02.1959.

[93] See Pohl et al. (2005, pp. 305–308).

[94] See Bundesverwaltungsgericht (1958) for the ruling.

FIGURE 3.2: **Market shares of the banking groups in Germany by balance sheet size (1947–1961)**



Note that the break in the time series is probably due to the currency reform in 1948. The Public Bank System includes the Landesbanken and the Sparkassen, the Cooperative Banking System contains the Credit Cooperatives and the Zentralkassen. There is no data available for 1949. *Source: Own elaboration based on data from Deutsche Bundesbank (1976, pp. 126–127) for the time period from 1946–1948. For the time period form 1950 to 1961 the Bundesbank time series OU0308, OU0749, OU0824, OU0874, OU0924, OU1024, OU1074, OU1124, OU1174, OU1224, OU9319, OU1424, OU7672, OU7647 have been used (year end data).*

in the law, but to leave them blank. Of all the banking associations, merely the private credit bank association had sought them. A general agreement was reached by the working groups by the end of October of 1958. The was merely one issue that remained somewhat controversial. It was the restriction of savings deposits to natural persona only, which was supported not only by all the private sector banks, but also by the Bundesbank. The Interior Ministry objected to this provision on behalf of the German States and the public banking sector, but it was not successful in having the provision removed in subsequent high-level discussions.[95]

By March of 1958, the government bill was introduced to parliament, where it encountered immediate resistance by the *Bundesrat* (i.e. the German states).[96] There was little

[95]See BArch B102/41904, various minutes and memos of the intragovernmental deliberations in 1958. See especially the Memo by Schreihage, from 29.10.1958, which outlines the outstanding points of agreement.

[96]The *Bundesrat* even debated a state-sponsored competing piece of legislation that would have transferred some regulatory responsibilities to the federal level. See BArch B136/1216, p. 84–89, 165–168 &

disagreement about the actual material regulations, such as the credit institutions covered by the Credit Act, the provisions regarding capital and liquidity ratios, or the restrictions to competition. Once again, the key issue was the structure of the regulatory system that caused the dissent. The states were not prepared to accept the proposed centralization of the regulatory structure.[97] The most they were willing to accept was a central regulatory agency for the largest credit banks and for banks operating in more than two states. The likely reason, why the states did not want to give up their regulatory privileges stems from the fact that the close contact with the banks allowed them to support their own pet projects.[98] It was clear to Schreihage and his men that it would be impossible to obtain the support of the states, as long as the draft foresaw the centralization of banking regulation. The passage of the bill was bound to end in a head-on confrontation between the central government and the federal states.[99] In doing so, the federal government could build on the overwhelming support of the Bundestag. This was all it needed to pass the Credit Act, as the field of banking supervision was one of competing competences between the states and the central government. The central government could assume responsibility for the field if there were reasons that made it indispensable for the central government to assume control. However, unless it had the support of the *Bundesrat*, the central government would need a supermajority in the *Bundestag* to overrule the *Bundesrat's* objection.[100] Importantly, the Economics Ministry was also able to secure the political support of the Bundesbank. After all, the opposition of its predecessor, the BdL, had helped to stop the government's attempt to bring about the regulatory centralization in 1957.[101]

On the Credit Act's way through parliament, two other issues were vigorously debated. The *Bundesrat*, the *Bundestag*, and the *Bundesbank* suggested to include some form of

179, regarding the *"Entwurf eines Gesetzes über Zinsen, Gebühren und Wettbewerb im Kreditgewerbe"* from 29.04.1958

[97]See for example BArch B102/41907, Letter by von Hofe to Westrick from 18.03.1959, BArch B102/41907, report by Veit from 20.03.1959 and the newspaper article *"Ist eine zentrale Bankenaufsicht Notwendig?"*, by Hermann Veit from 16.12.1958 in the Frankfurter Allgemeine Zeitung.

[98]See BArch B102/41907, Memo by Schreihage from 16.02.1959, and Memo by Warner to Lowell and Pumphrey from 09.02.1950 in NARA, RG 466, Decartelization and Deconcentration Division, Subject Files, 1948-55, folder 'Banking Deconcentration 1950' box 1. By 1960, 55% of all government loans were provided by the public banking sector. See Pohl et al. (2005, p. 277).

[99]See for example BArch B102/41889, Memo from 28.10.1958 (A 3 - 6122/58).

[100]The *Bundesrat* was unanimously opposed in this case, thus the government needed the Bundestag to overrule the *Bundesrat* with a supermajority. See Bundesgesetzblatt (1949, Art. 72, 74 and 77).

[101]Initially, the state central bank presidents demanded the establishment of a central regulatory agency with a decentral substructure. Such a structure would have required the explicit approval of the states. This demand was soon dropped, however. See for example B102/41889, Blessing to Erhard from 15.10.1958

deposit insurance. The Economic Ministry studied the possibility in detail.[102] However, it eventually blocked all efforts to introduce deposit insurance as part of this Credit Act. It argued that deposit insurance was not viable in Germany. The German banking sector was politically dominated by three large banking groups. Neither of which had an interest in deposit insurance.[103] The Savings banks, as public institutions, had the implicit backing of the local and regional governments. The Credit Cooperatives had devised their own scheme to insure the deposits of their customers. Furthermore, the largest commercial banks were so large, that if one of them were to fail, any deposit insurance scheme would not suffice to contain the damage. Instead government intervention would be needed as they were too big to let fail. Both the government and the large commercial banks were aware of this. Thus, the only banking group interested in any kind of deposit insurance would be the smaller private banks. Additionally, the government sponsored interest rate cartel secured banks' margins, decreased competitive pressures and therefore reduced the probability of collapse. Thus, deposit insurance was no immediate necessity it was argued. And even if deposit insurance were to be introduced after all, an important issue would have to be tackled at the same time: that of equal competitive starting positions. The savings bank system had the advantage of implicit government guarantees. It was certain, that any attempt to privatize the savings bank system would lead to major opposition and thus delay the Credit Act indefinitely. Thus, for the time being, not dealing with the issue of deposit insurance, was the preferred strategy for the Economics Ministry.[104] The Ministry proposed to study the issue in more detail once the Credit Act had been passed.[105]

The other hotly debated issue was that of 'revolving loans'. This was a practice championed by finance broker Rudolf Münemann. He used revolving short term loans from institutional investors and lent them out on a long-term basis. The *Bundesbank*, the

[102]See BArch B102/41817, Letter by Erhard to Niederhalt from 26.09.1958. Indeed, at the time the American System of Deposit insurance was studied within the Economics Ministry. See for example BArch B102/41817, Memo by Schork from 25.09.1958 or the Annual Report of the FDIC in 1958.

[103]For the market shares of banking groups in Germany see figure 3.2 on page 132.

[104]See BArch B102/41817, Letter by Westrick to Schedl from 08.03.1961 (VI A 3 - 4107/61), Handwritten draft Memo from 15.09.1960, and Letter from Dürre to the head of Division VI from 04.01.1956. See also BArch B102/41915, BT Drucksache 2563, 3. Wahlperiode from 01.03.1961, in which the *Bundestag* encourages the government to study whether certain parts of the banking sector are at a competitive disadvantage with respect to others, and how it would be possible to reduce competitive inequalities, such as by introducing deposit insurance.

[105]Eventually Erhard even had to tell the *Bundesbank* off its public support for deposit insurance in order not to jeopardize the passage of the Credit Act. See BArch B102/41817, Memo from 18.09.1959, outlining the *Bundesbank's* position. See also the Letter from Erhard to Blessing from 14.03.1961, asking to cease its support for deposit insurance.

Private Banks and the Finance Committee of the *Bundestag* wanted to see such a practice specifically regulated in the Credit Act. They were concerned about the inherent maturity mismatch of such a scheme and feared that as revolving credit became more 'popular' it would jeopardize the stability of the entire financial system. The Economics Ministry and the *Bundestag* Committee on Economics were against including special provisions in the Credit Act. After all, all the parties engaged in such practices were professionals, and it was presumed that they understood the risks they were taking. More importantly, the Ministry wanted to avoid being seen as passing a "lex Münemann". Once more, the Economics Ministry stood firm and no special provision was included in the Credit Act.[106]

As the legislative period drew to a close, and after over two years of discussions in parliament, the government pressed for the enactment of the law. Just as with the previous failed attempt to recentralize regulatory supervision, a major political wrangling ensued over the eventual seat of the central regulatory agency. Once more the potential host-cities of Frankfurt, Bonn and Berlin were discussed. This discussion almost derailed the project. In order to ensure that the Credit Act could still be passed during the current legislative period, the ruling party, the CDU, agreed to have the future supervisory agency to be based in Berlin.[107]

The *Bundestag* passed the Credit Act with an overwhelming majority. Once again, the *Bundesrat* then did everything in its powers to delay the legislative process. It called upon the conciliation committee. The committee presented a compromise, which did not have a chance to be accepted by the *Bundestag*, as it proposed the continued decentralization of the banking supervision.[108] The proposal was rejected by the *Bundestag*. The *Bundesrat*, for its part, rejected the Credit Act, as it had been passed by the *Bundestag*. The *Bundestag* in turn, overruled the *Bundesrat* with almost unanimity[109] and the Credit

[106]See BArch B136/1217, Memo for the Cabinett Meeting from 02.12.1960 (6 - 55101 - 4643/60), and Memo for the Cabinet Meeting from 13.01.1961 (6 - 55101 - 5092/61). See also BArch B102/41905, Memo of a departmental meeting from 24.08.1960.

[107]See BArch B102/41915, Draft letter of Henckel to Merkatz from 04.03.1961, and Memo regarding the Credit Act Draft from 14.03.1961. This actually created a vigorous protest by the Soviet Union, even before the Credit Act was passed, as it did not consider West-Berlin to be part of the Federal Republic of Germany. See BArch B102/41915, Letter by von Hofe to the Minister and the Sub-Secretary from 10.05.1961 (VI A 3 - 4253/61II) and as an appendix to the letter the translation of the Soviet protest from 15.04.1961.

[108]See BArch B102/41915, Memo by von Hofe from 30.05.1961 (VI A 3 - 4298/61).

[109]There were 350 delegates in favor and 31 against the Credit Act, with two absensions. See BArch B102/49334, Monthly report by the *Bundesbank* for the month of August 1961.

TABLE 3.4: **Conceptual overview of the different interest groups**

	Centralized Regulation	**Decentralized Regulation**
'Free' Competition	Division 1[a]	
Restricted competition	*Bundestag*[b],Division 6[c], Private banks, Credit Cooperatives, *Bundesbank*	*Bundesrat*[d], *BdL*[e], Savings Banks[f], (Finance Ministry)[g]

[a]This is the position by the Division led by Müller-Armack. They were most likely supported by Economics Minister Ludwig Erhard.

[b]Some elements of the Bundestag actually favored increased competitive pressures in the banking sector.

[c]This was the division in the Economics Ministry that was officially in charge of drafting the new Credit Act. This division cooperated closely with the banking associations.

[d]The upper house of parliament, in which the states are represented

[e]The BdL was restructured into the *Bundesbank* in the Summer of 1957.

[f]The public banks were initially in favor of restricting competition, however with increasing success in the late 1950s they began to shift towards a loosening of the restrictions to competition.

[g]The Finance Ministry did not have a strong opinion on this matter and seemed to accept the status quo.

Note: The positions shown here are conceptual in nature. The actual positions are not necessarily as clear cut and indeed more nuanced. *Source: Own elaboration.*

Act was finally passed, just before the end of the legislative period.[110]

Three months later, several of the German states decided to challenge the Credit Act in the constitutional court.[111] While this created a somewhat uncomfortable situation for the government, it did not deter it from going ahead from setting up the new central supervisory office.[112] And indeed, the states' challenge was dismissed after a round of oral hearings.[113]

The Credit Act that was passed in 1961 was essentially the younger brother of the pre World War II Credit Act of 1934. Even the constitutional court remarked the similarity

[110]It would only enter into force on January 1st of 1962, which was meant to give the government time to set up the new central supervisory agency. For the Credit Act see Bundesgesetzblatt (1961).

[111]The states argued that the federal government had violated a number of norms that prevented it from establishing a centralized regulatory regime without the explicit approval of the states. In particular the states challenged that there was a pressing need to centralize regulation. Without a pressing need the government needed the explicit approval of the states. The states also argued that the dual regulatory structure also required approval by the *Bundesrat*. Last but not least, the states argued that the confrontational nature of the federal government violated the unwritten constitutional principle of the 'loyalty to the federation' (*Bundestreue*). This requires all parts of a federation to cooperate with mutual respect. For details see the ruling of the Bundesverfassungsericht from 24.07.1962, BVerGE 14, 197 - Kreditwesen. See also the most critical norms in Bundesgesetzblatt (1949, Art 87, III; Art 84 I, and Art. 72 II).

[112]The Economics Ministry was convinced it would win the case. The only problems it could foresee was the possibility of an interim injunction that would prevent the government from setting up the regulatory agency for the duration of the case. See for example BArch B102/49331, Confidential letter to Henckel from 07.10.1961. For the discussions within the federal government see also B102/49331–49334 and B136/1218, pp. 141–143, 146.

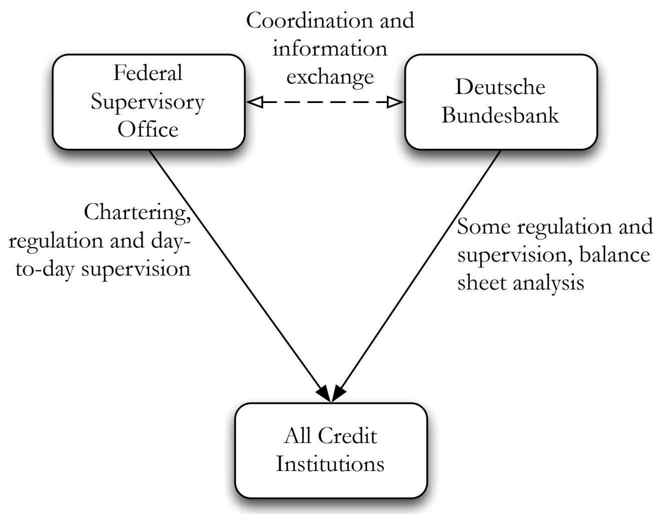
[113]Bundesverfassungsericht, ruling from 24.07.1962, 2 BvF 4, 5/61, 1, 2/62 (BVerfGE 14, 197 - Kreditwesen).

of the two laws in its ruling on the constitutionality.[114] Not many significant provisions changed. Probably the most significant change was one the Americans had previously also advocated. The central bank was to leave matters of 'qualitative' regulation of the banking sector to the government's Federal Supervisory Office; the central bank's supervisory office from 1934 (the 'Aufsichtsamt', which had been abolished in 1939) was not re-established. Instead, the central bank focused almost entirely on monetary policy. The federal supervisory office, was almost entirely in charge of 'qualitative' norms and regulation. Another indirect 'victim' of American influence were the restrictions to enter the banking sector that were based on the vague concept of 'economic need'. These kinds of restrictions collided with the constitutional right to choose ones freedom of trade and were consequently dropped.[115] A major addendum was a banking crisis manual, which described the steps the government could take in case of a systemic crisis. This was introduced to give the government the flexibility to act in times of crisis. In the 1934 Credit Act, such a provision had not been a necessity, as the Weimar constitution already provided for the necessary emergency powers. Other than that, the Credit Acts were de facto the same.[116]

After the first official draft of the Credit Act had been made public in 1958, a number of suggestions for improvement were made. Amongst these were the introduction of deposit insurance and specific regulation for revolving credit businesses. What is remarkable, however, is that while the changes made to the draft were numerous, they did not change either the regulation or the regulatory structure in a significant way. Thus, the original character stood firm and the Economics Ministry made sure it would. It had to, because any major liberalization to the regulations would in turn thwart the supermajority that was needed to recentralize the regulatory structure, the primary objective of this piece of legislation. Any prolonged public discussion would also thwart its probability of passage and so it almost did. While standing firm, the Ministry could count on the support of much of the private banking sector, which sought the restriction to competition as a necessary shield from the competition of the public banking sector. The Economics Ministry was further aided by the fact that the *Bundestag* also wanted to see the Credit Act pass once and for all before the end of the legislative period; even more than it wanted to see the inclusion of deposit insurance or other amendments. The German states

[114] See Bundesverfassungsgericht, ruling from 24.07.1962, 2 BvF 4, 5/61, 1, 2/62 (BVerfGE 14, 197 - Kreditwesen). See also Ambrosius (1998, p. 162), who reports that the similarity was noted by the public.
[115] For the corresponding ruling of the Federal Administrative Court see Bundesverwaltungsgericht (1958).
[116] For a schematic overview of the regulatory structure see figure 3.3 on page 138.

Figure 3.3: **Schematic overview of the regulatory arrangement in West–Germany in 1962**



The centralized twin regulation and supervision of the banking sector from 1934 was essentially re-introduced. Crisis resolution measures, such as the declaration of a bank holiday or a moratorium for the liabilities of a bank were reserved for the federal government. The only credit institutions not subject to most regulation were specialized credit institutions such as the *Bundesbank*, the Federal Post Office or the Reconstruction Credit Institute (KfW). For details on the exceptions see Bundesgesetzblatt (1961, §2). *Source: Own elaboration.*

fought the centralization of the regulatory institutions to the very end. The states even launched a constitutional challenge, claiming essentially that the centralization of state powers without their consent was unconstitutional. However the constitutional court ruled in favor of the central government and 'its' Credit Act.

3.8 Conclusion

The genesis of the German Credit Act of 1961 is one of twists and turns, and certainly not as straightforward as it is traditionally assumed in the literature. Initial drafts for a 'new' Credit Act were substantially different in character than the final version eventually passed by parliament. This is not simply attributable to the fading of Allied influence on German legislation. Instead it is a manifestation of a constitutional struggle between the federal government and the states over the right to regulate the banking sector. The fact that restrictions to competitions were upheld is to a significant extent a reflection of the demand for it by the private banking sector, which feared the competition from the public banking sector.

At the outset of the Federal Republic of Germany, regulatory powers lay with the states' finance ministries. First drafts of a Credit Act largely confirmed the Allied-imposed status quo, and the Finance Ministry under Schäffer seemed like it would have accepted such a Credit Act. The transfer of competence in terms of money and credit, from the Finance Ministry to the Economics Ministry under the leadership of Erhard, was therefore a key turning point. The Ministry under Erhard cooperated closely with the banking associations in preparing new drafts. In particular, the private banks had significant influence. However, at the same time, the Ministry of Economics was torn internally over how much competitive pressure should be allowed within the banking sector. On one hand, there was the 'free' market faction under Müller-Armack's Division I, whose intellectual views were similar to those of Erhard. On the other, there was the Money and Credit Division, Division VI, which, in key positions, contained several former employees of the supervisory institutions (or the Economics Ministry) of the pre-war period, and which was in close contact with the banking associations. The private banking sector, and to some extend the public banking sector as well, sought to maintain the relative calm the restrictions to competition in the banking sector provided. Especially the private credit banks sought the restriction as a necessary shield from the competition of the public banking system. Both the passage of the Antitrust Act and the Bundesbank Act served as important primers for the Credit Act. The Antitrust Act permitted the government an exception to the rule so it could establish a cartel in the banking sector. The Bundesbank Act redistributed the balance of power from the state central banks, to the central bank directorate. This, in turn, changed the stance of the *Bundesbank* towards the Credit Act, from supporting decentralization of banking supervision to supporting a centralized supervisory system.

In a parallel development with the drafts on an Antitrust and a Bundesbank Act, the drafts for the Credit Act showed remarkable change over time: from clearly Allied- (or more accurately, American-) inspired pieces of legislation, back to the path the Germans were on before the Second World War. The first (unofficial) drafts for a new Credit Act were written while the Allies were still involved in German legislative affairs, and while the supervisory institutions, the central bank and the large commercial banks were decentralized. Consequently, the first drafts tried to incorporate Allied demands, which aimed at codifying the status quo. But already then, the Allies main preoccupation lay with the large commercial banks and their decentralization. The Allies wanted to prevent them from recentralizing completely as they saw in them an excessive concentration of financial power. At the same time, the Allies also realized that the decentralized supervisory structure had suffered from political capture – state politicians were using the close link to their personal advantage. Thus, the Allies were open to a reintroduction of centralized supervision.

Indeed, the influence of the Allies in terms of regulatory supervision does not reach much beyond the establishment of the Federal Republic of Germany. The Allies left Germany with a crudely decentralized supervisory system and with no concrete guidelines on how to put the system on a sound footing. The only general guidelines, given to the Germans for an eventual redrafting of their credit act, were the separation of qualitative and quantitative regulation – the central bank should worry about monetary policy and the supervisory institutions should be 'policing' the banks – and the decentralization of regulatory institutions. The latter guideline was scrapped by the Allies in 1950. From the spring of 1951 on, the Americans did not exert any active pressure in terms of banking supervision on the German government. Only on the issue of branching restrictions did Americans continue to exert their influence. Once the Branch Restriction Act of 1952 was passed, the Allies de-facto withdrew completely from matters relating to the German banking system. After 1955, Germany had also regained full legislative independence and Allied influence on all German legislation was negligible. Thus, probably the longest lasting effect on German banking supervision was an indirect one. The new constitution created a federal state and these states were originally given the competence to regulate. But it was also the same constitution that allowed for the central government to take the reigns of banking supervision away from the states. Indeed, what the birth of the German Credit Act of 1961 most vividly portrays, is the struggle between the central government and the federal states in the early Federal Republic of Germany.

One most striking aspect of the (re-)birth of the Credit Act is that the private banks did not try to use this opportunity to rebel against the regulations, even though they were given intimate access to the drafting process. The banks did not jump on the free-market bandwagon advocated by many German (and American) economists of the post-war period. Instead, the banks preferred the cosy, government-cartelized system introduced before the Second World War, which restricted competition. The private banks tried to reign in increasing competition from the public savings bank system by working closely with the government, to prevent major overhauls of the pre World War II system. Throughout the drafting process, there is little evidence that German officials systematically looked outwards at other regulatory systems, in order to determine the regulatory best practices at the time (as they had done between 1931 and 1934). The only reference points for German policymakers was their own Credit Act of 1934 and its subsequent amendments. Merely in the case of deposit insurance did they study the American Federal Deposit Insurance Corporation system.

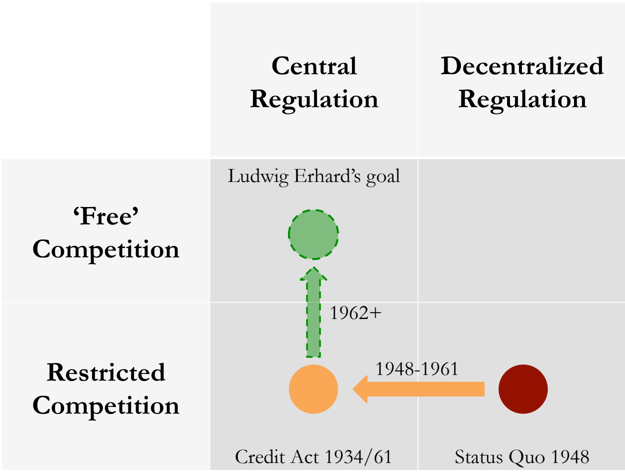
Theoretically, the Germans could have changed their regulatory system in several ways. They could have introduced deposit insurance, a separation of investment and deposit banks, a prohibition or strict regulation of revolving credit, measures against too big to fail or even tackled the privatization of the public banks – which to this day are in public hands. Only deposit insurance was seriously under consideration at one point. It was not adopted because of the special structure of the German banking sector. Public banks and credit cooperatives already had implicit or explicit deposit insurance, and large commercial banks were, even back then, too big to fail and would have required government intervention in case one of them failed.[117] This is probably the most striking part of the birth of the Credit Act of 1961. That the government was well aware of the too big to fail nature of its largest banks and that it deemed that it was a risk the government could not (or should not) tackle. The lack of innovative desire caused the Germans to pass effectively the same Credit Act they had already passed almost thirty years earlier.

The lack of innovative desire can be explained. After all, the centralization of the supervisory institutions was the key issue the federal government wanted to see introduced. However, this provision encountered stiff opposition by the states as the government had learned in a first failed attempt to recentralize the regulatory responsibilities in 1957. Consequently, the government had to rally a two-thirds majority within the lower house of parliament, the *Bundestag*. Every 'innovation' that deviated from the status quo of a, with the banking sector, still popular Credit Act of 1934 would most likely have jeopardized the

[117]Government mandated deposit insurance was only introduced in 1998. A voluntary scheme was introduced in the early 1970s.

necessary two-thirds majority. Consequently, the government played it safe and decided to leave innovative reforms for the future, when a two-thirds majority would no longer be necessary.[118]

FIGURE 3.4: **A schematic overview of the struggle over the Credit Act**



The ultimate goal of Ludwig Erhard and the ordoliberals within his Ministry of Economics was to recentralize regulatory control and to overhaul the regulations of the banking sector in order to introduce more competitive pressures. Eventually it became clear that it was not politically feasible to tackle both issues at the same time. Consequently a two step strategy was adopted. The recentralization of regulatory control happened in a first step by retreating effectively to the Credit Act of 1934. After that, the central government would gradually introduce competition into the banking sector. *Source: Own elaboration.*

[118] For a schematic overview of this rationale see figure 3.4 on page 142.

Chapter 4

A failed Institutional Assimilation

The American attempt to restructure German banking regulation after the Second World War

4.1 Introduction

After the Second World War, the American Military Government undertook drastic efforts to change the banking system in West-Germany (henceforth just Germany). It restructured the entire German banking system, its rules, its regulatory institutions, and its major financial institutions, in an attempt to introduce the principles governing the American banking system.[1] The German banking sector was subject to one of the most comprehensive transformations of a banking system, ever.[2] What makes this little-known episode of German banking history[3] so intriguing is that it can provide important insights into *American* banking history.

[1]The title of this chapter is a nod to the article by Guinnane (1994). In the article he describes an attempt to transplant German-style credit cooperatives into the Irish banking sector. In Germany, such credit cooperatives had performed exceptionally well in providing micro-credit to rural areas. The credit cooperatives were installed upon the Irish banking sector 'from above'. As it turned out, the credit cooperatives failed to thrive in Ireland since the population largely ignored these institutions. Eventually, the 'experiment' was abandoned. The historically grown structures of the banking system and their social context, would simply not accommodate such an additional institution. For a different perspective on why the transplant failed in Ireland see Colvin and McLaughlin (2012).

[2]Reform of the banking system had been pondered by the American Military Government in Japan after World War II as well, but no major changes were implemented. For the Americans' reform of the Japanese banking system see Tsutsui (1988).

[3]I found that it is an almost unknown episode outside of the German-speaking economic history literature. At best the break-up of the largest credit banks, the *Großbanken*, is known, but not the full extent of the American assimilation effort.

In chapter 2 of this dissertation, I concluded that the reason why the American banking system developed into the decentralized structure it did (and why the German banking system did not) was primarily a function of the extensive states' rights – with respect to chartering banks – enshrined in the American constitution. This implies that the regulatory arrangement of the American banking system was only a second-best solution that was held in place by these strong states rights. In the absence of these institutional constraints, no such system would have evolved and persisted. The American assimilation effort in Germany provides a natural experiment to test this hypothesis. The most important elements of the American state banking system were imposed on the German banking system exogenously with the help of military decrees. However, the new German constitution (the *'Grundgesetz'*) lacked the strong states' rights to charter banks present in American constitution. The struggle between the German states – who wanted to retain their newly gained rights – and the federal government – who wanted to recentralize the regulatory structure – was eventually even taken to the constitutional court. If the constitutional court had ruled in favor of the states instead of the central government, parts of the American institutional structure could have survived in the German banking system. Instead, the American institutions disappeared completely. Rather than portraying a supposed resilience of the German banking sector, this episode highlights the weakness of the American decentralized regulatory structure in a different political set-up.

This chapter adds to the literature by presenting the failed Institutional Assimilation as a natural experiment of the American regulatory structure. To the best of my knowledge it is also the first comprehensive account of the American influence on the German banking system for the post-war period all the way up until 1962 – when all of the Allied reforms had been largely reversed.[4] The most detailed historical accounts of the discussions taking place after the Second World War with respect to the banking system are those of Horstmann (1991) and Loehr (1952). Horstmann (1991) describes Allied policy and discussions with respect to the *Großbanken* in detail. However his treatment of other aspects of the banking regulation is light. Additionally, Horstmann's focus only lies on the post War period up until 1952. Loehr (1952) is the official U.S. Military Government historian's account of the Allied attempts to change the German banking system as a whole. Again, Loehr's work only covers the time period up until 1952. Additionally, it lacks

[4]There are, however, several comprehensive works on the American attempt to decartelize and deconcentrate German industry. See for example Berghahn (1986), Murach-Brand (2004) or Partridge (2011).

the inputs from German archival sources and is generally less detailed than Horstmann. Adler (1949) is a most valuable contemporary account of the events from the American perspective on the ground up until 1949. Other works on German banking from that time period only cover specific parts of the banking sector such as individual larg credit banks[5] or the *Bundesbank* and its predecessor the *Bank deutscher Länder*.[6] The history of the regulatory institutions had received little treatment so far. It is touched upon in an edited volume by Pohl (1998) and in Büschgen (1982), but neither make use of archival material. To the best of my knowledge, the first complete analysis of the politics behind the changes to the regulatory institutions in the banking sector based on archival material is the third chapter of this thesis. Thus, this chapter also adds to the research by presenting the history of German banking institutions from 1945 until 1962 from a unified perspective.

The chapter is organized as follows: the next section describes the German and American banking regulations prior to World War 2. This is followed by a discussion of the legal persistence between pre-war and post-war Germany. After this, the original plans of the American Military Government for the German economy and its banking system are presented. It is then contrasted with the actual regulatory developments in the banking system. The final section provides a discussion of the divergence of the outcomes with respect to the original plans, and the interpretation of this episode as an important natural experiment for American banking history.

4.2 German and American banking regulation prior to the Second World War

For much of its history the German banking system was largely unregulated. At the same time, local and regional governments intervened directly in the sector by forming their own credit institutions. As a consequence, by the 1930s the banking sector had developed a most peculiar structure. Apart from the fact that a major share of its banks were government run, it was characterized by comprising tens of thousands small banks, as well as a few hundred larger banks. What was further remarkable about the system

[5] Such as the works on the Commerz-, Dresdner- and Deutsche Bank by Wolf (1995), Ahrens (2007) and Holtfrerich (1995), respectively. Holtfrerich's account also studies the motivations of American intervention in detail.

[6] See for example Dickhaus (1998); Hentschel (1988a,b); Marsh (1992) or Wandel (1980). Wandel also discusses the American motivation and plans for the banking system as a whole.

was, that it had an inherent division of labor and was not yet a system dominated by universal banking.[7] Over 20,000 credit cooperatives specialized on micro-credit in rural areas. More than 2500 public savings banks (or *Sparkassen*) focused on small-scale loans as well as saving deposits in more urban areas. Much of the savings banks' investment was in regional government papers. The Regional Banks (or *Girozentralen*) were the umbrella organizations of the savings banks within a particular region, which helped to even out credit demand and supply inequalities throughout the savings bank system within their region. The credit cooperatives had similar umbrella organizations as well, called the *Zentralkassen*. Mortgage banks would engage only in real estate business. About 1000 private bankers tended to perform the function of stock-brokers and investment advisers, whereas the *Großbanken*[8], some of which had a few hundred branches throughout Germany, would be mainly engaged in wholesale banking, i.e. export finance, mid to large-scale industrial loans, keeping checking accounts for the largest corporations as well as securities trading. So did other regional credit banks.

Germany's central bank (the *Reichsbank*) had a centralized structure as it was typical for European central banks. Through most of its history it was not independent from the government.[9] At the same time, it could open branches throughout Germany and these branches accepted deposits and thus competed directly with other commercial banks to some extent. This gave the *Reichsbank* some information with respect to the conditions of the banking system. However it had no regulatory powers until the 1930s.[10]

Widespread banking regulation was only introduced when a major financial crisis in 1931 forced government to rethink the regulatory framework of its banking system. The immediate cause of the crisis was not the banks' behavior, but the German government's reparation policy. Yet, much of the banking system, including savings banks and the credit banks had overextended credit throughout the 1920s. Furthermore, this credit had been extended on the back of short term foreign debt.[11] While the government had not

[7] Fohlin (2007) and Guinnane (2002) make the case for the division of labor for the period up to 1914. This specialization lasted even well into the 1920s and even 1930s, as it is reflected in contemporary discussions of the banking system. See for example Reichsbank (1933a) and Reichsbank (1933b). See also Pohl, Rudolph, and Schulz (2005, pp. 91-98).

[8] Often they are better known as "*the* Universal Banks". The literal translation of *Großbanken* is 'large banks'. In this chapter *Großbanken* and large credit banks will be referred to interchangeably.

[9] Apart from a brief stint in the 1920s.

[10] See James (1985, pp. 19–25). See also chapter 2 of this thesis.

[11] For modern interpretations of the crisis see Ritschl and Sarferaz (2010), Schnabel (2004) or Temin (2008).

explicitly prohibited this policy, due to the lack of proper bank regulations, it was largely unaware of the critical state of Germany's banking system until the crisis hit.[12]

The regulatory changes first introduced in the emergency decrees of 1931 were extended and codified in the Credit Act of 1934.[13] They created a centralized regulatory supervision of the entire banking sector. Regulation was organized in two central institutions which held extensive powers. The supervisory office, as part of the *Reichsbank*, and the commissioner of the banking system, a regulatory body associated with the Ministry of Economics. The supervisory office was in charge of issuing general rules such as the liquidity and capital ratios, whereas the commissioner's office was to enforce these rules. Cooperation between these two regulatory institutions was close, by necessity. The regulatory reforms of the 1930s also introduced an auditing scheme, stiff barriers to entry in the form of chartering[14] and a state-sanctioned interest-cartel that was meant to stifle competition. Furthermore, investment restrictions were put in place, and the regulatory institutions were given the power to enforce liquidity and capital requirements. However, the reforms of the 1930s did not change the basic structure of the banking sector. Quite the opposite, it cemented the existing structures.

These characteristics would not change significantly during the remainder of the Third Reich. There would merely be a shift in the regulatory powers from the *Reichsbank* and the Commissioner's office, directly to the Minister of Economics.[15] Thus, by the beginning of the Second World War, the German banking system was characterized by a centralized central bank, centralized regulatory supervision, and a cartelized banking sector with significant barriers to entry as well as a 'division of labor' amongst the banking groups.

How did regulation differ in the United States?

Regulating the banks had a much longer tradition in the United States than in Germany. In fact the first attempts to regulate banks went back almost as far as American independence.[16] Banks had to adhere to the regulations of their chartering authority. Prior to the

[12] The confusion with respect of the condition of the German banking system in those days of crisis is vividly portrayed in Born (1967, pp. 98–109).

[13] See Reichsgesetzblatt (1931a,b,c, 1934).

[14] The regulatory authorities could deny virtually any application for a new bank or a new branch, if it wished to do so on. They could do this on the grounds of its 'potential adverse impact on existing banks'.

[15] See the amendments to the Credit Act in Reichsgesetzblatt (1939a,b) and Reichsgesetzblatt (1944).

[16] For the early history of American banking regulation see for example Hammond (1957) and Legler, Sylla, and Wallis (1987). See also Chapter 2 of this thesis.

TABLE 4.1: **The German banking system prior to World War II**

Bank Group	**Assets as a % of all banks 1930**	**1938**	**Number of banks[a] 1930**	**1938**
Public Bank System	**35.3%**	**45.4%**	**2624**	**2558**
Sparkassen	20.6%	29.1%	2583	2517
Public Regional Banks[b]	14.7%	16.3%	41	41
Cooperative Banking System	**9.4%**	**10.5%**	**19115**	**19076**
Cooperative Banks	7.2%	7.8%	19070	19040
Zentralkassen	2.2%	2.7%	45	36
Incorporated Private Banks	**26.8%**	**22.9%**	**186**	**109**
Berliner Großbanken[c]	19.4%	11.6%	6	5
Provinzbanken	2.9%	1.8%	55	37
Spezial und Hausbanken	4.5%	9.5%	125	67
Mortgage Banks	**13.0%**	**11.0%**	**44**	**36**
Pure Mortgage Banks	10.0%	8.1%	33	27
Mixed Mortgage Banks	2.6%	2.5%	3	3
Landschaften	0.4%	0.4%	8	6
Private Bankers	**5.3%**	**1.6%**	**800-1000[d]**	**491**
Other[e]	**10.2%**	**8.7%**	**219**	**132**
TOTAL	100%	100%	**23139[f]**	**22270**

[a]These numbers do not include branches.
[b]Includes the *"Girozentralen"* and other public *"Landesbanken"* and *"Staatsbanken"*.
[c]These are commonly (and somewhat mistakenly) referred to as *the* German universal banks. In Germany all banks could be universal banks, unless their own founding statutes prevented them from engaging in certain business practices.
[d]Exact numbers for private bankers are not available for this year.
[e]The most important banks in this category are government ones with specific functions such as the Golddiskontbank.
[f]This number assumes that there were 950 private bankers in 1930.

Note the size of the Public Bank System with respect to the largest Credit banks – the *Großbanken. Source: Own calculations based on data from Deutsche Bundesbank (1976, p. 121).*

1860s, American banks could be chartered only by state regulatory institutions – usually these were the states' Finance Ministries.[17] Regulation of banks was thus decentralized to the state level. In the 1860s the central government introduced the national banking system in an effort to unify the currency and to replace the state banking system . The former goal was achieved by giving a de-facto note issue monopoly to banks with a national charter. State banks' note emission was taxed so heavily that it was not viable anymore. As a consequence, most state banks either ceased operations or converted their charters into a national one. The American federal government had to go this indirect route to centralize banking regulation, since the constitution did not grant it the power to simply

[17]The exceptions to the rule were the First and Second Bank of the United States, which were chartered by Congress.

take away the states' right to charter and regulate state banks. Thus the need to create incentives for state banks to convert their charter into national banks.[18]

At first it seemed like the plan would work, and that the state banking system would be replaced by the national banking system. The Americans had come close to de-facto unifying banking regulation throughout the country. However, the state banking system staged a comeback and the so-called 'dual banking system' took hold in the United States. In part this was due to the strict regulatory requirements of national banks, and in part due to the spread of cashless transfers. The comeback was further aided by the state regulators lowering regulatory regulatory requirements. Since banks had been given a choice of their regulator – either a national regulator or the respective states' regulator – they could now engage more actively than ever in regulatory arbitrage.[19]

This regulatory arrangement increased further in complexity with the establishment of the Federal Reserve in 1913. The introduction of a (decentralized) central bank to the American banking system was also used, once more, to attempt to unify the banking system. Banks wanting to have access to the re-discount facility of the Federal Reserve had to subject to regulation by the Federal Reserve. While national banks were forced by law to become members of the Federal Reserve System and to subject themselves to its regulations, state banks were free to join. Almost none of the state banks opted-in due to the stringency of the regulations. These were subsequently relaxed for state banks (but not for national banks) in order to increase their membership rates.

During the Great Depression, the regulatory structure of the banking system increased yet more in complexity. Congress mandated the separation of investment and deposit banks and it moved towards slightly more centralized decision making within the Federal Reserve System. It also introduced a deposit insurance scheme. Once more, it was also used as an indirect attempt to unify the regulation of the banking system under the auspices of the Federal Reserve. In the original 1933 Banking Act, all banks wanting to accede to deposit insurance were required to join the Federal Reserve System, if they were not a member already. However, the date by which this provision was to come in force was first delayed and eventually dropped. Thus, at the outset of Second World War, the regulations of the German and American banking systems followed radically different

[18] This and the following paragraphs are based on chapter 2 of this thesis.

[19] To some extend, state banks could already engage in regulatory arbitrage before, by choosing the state in which to incorporate.

Table 4.2: **German and American regulations in 1935**

Structural Regulations	**Germany (1935)**	**United States (1935)**
Regulatory Institutions[a]	Centralized	Decentralized[b]
Central Bank	Centralized	Decentralized[c]
Branching	Free	Restricted[d]
Investment Restrictions	Universal banking[e]	Separation of investment and deposit banks[f]
Deposit Insurance	None	Yes[g]

[a]This also includes the supervisory institutions

[b]Although the national banking system is a centralized one, banks are free to change from one system to another thus making regulation permeable.

[c]Even though the Federal Reserve System had just moved to a more centralized approach to decision making, it can still be characterized as a decentralized banking system as many important competences still lay with the individual Federal Reserve Banks. See Cwik (1970, p. 35).

[d]Inter-state branching was generally prohibited. There was limited intra-state branching however. The individual states could decide whether to allow branching within their state. Most states chose not to allow it.

[e]There was a mandated internal separation for the use of funds depending on their origins.

[f]Technically this separation only applied to National Banks and State Member Banks. State banks that were not members of the Federal Reserve System did not have to adhere to this separation.

[g]Deposit insurance was mandatory for all national banks and for state member banks. State non-member banks could opt in. The Federal Deposit Insurance Corporation also acted as an additional regulatory institution.

approaches.[20] In particular, while the German system was subject to a highly centralized regulatory supervision, the American system was mostly decentralized.

4.3 The Allied reform plans

The immediate aftermath of the Second World War is a highly interesting but complex period. While the German military had officially surrendered, there was no declaration of submission by the German government and neither was there a formal armistice. Instead, the armies of the Allies had occupied the territory, and assumed *"supreme authority"* of Germany. At the same time, the occupiers explicitly refrained from annexing Germany.[21] Such a situation was a novelty from a legal standpoint. The key question for legal experts was whether the nation Germany had ceased to exist as a sovereign nation, or whether it was merely occupied.[22] This question was not only of academic interest, but also of practical relevance when the Allies tried to rebuild the economic and legal system. If

[20]See table 4.2 on page 150 for a comparison.

[21]See the 'Berlin declaration' in U.S. Department of State (1985).

[22]See Kunz (1950) or Rheinstein (1948) for contemporaries' views of this 'legal dilemma'.

Germany had not ceased to exist, then its laws and (banking) regulations would still be applicable.

And indeed, this was how West-Germany was de-facto treated. All the laws and regulations from the Weimar Republic and the Third Reich did, in principle, continue to be in force. Since the Allies were in control of the legislature, the executive and the judicial system, it was in their hand to decide whether the old laws were applied or not.[23] At the same time, the Allies issued proclamations, ordinances or military 'laws' in order to administer the country. These overrode Germany's existing laws. In most cases these did not replace the old laws entirely.[24]

The Allied Control Council's first law repealed all laws enacted during the Third Reich, which were political in nature or which had helped cement the National Socialists' grip on power.[25] The most important laws to be repealed were explicitly listed in the Control Council's law. However, many more laws enacted during the Third Reich were not mentioned. Consequently every single one of them would, in theory, have had to be checked for their National Socialist content. This led to great uncertainty, especially with laws like the Credit Act of 1934, the act specifying the nature of the regulatory institutions and their powers, which had been amended during Nazi rule.[26] Additionally, the central institutions in charge of regulating the banking sector, the Ministry of Economics and the *Reichsbank*, had ceased to function with the end of the Second World War.[27]

The German political set-up was largely reached over a series of conferences between the Americans, the British and the Soviets at Tehran, Yalta and, finally, Potsdam.[28] The

[23]The Directive to Commander-in-Chief of United States Forces of Occupation Regarding the Military Government of Germany (or simply Joint Chiefs of Staff directive 1067 – J.C.S. 1067), described the situation as follows to the American military forces: *"[You are] clothed with supreme legislative, executive, and judicial authority in the areas occupied by forces under your command"* (Joint Chiefs of Staff, 1945).

[24]One can compare this to how EU law superseeds any existing national law of one of its member countries.

[25]See Allied Control Council for Germany (1945).

[26]This uncertainty was further increased when Germany obtained its new constitution in 1949. Thus, every paragraph of every law not explicitly and implicitly repealed by the Allies, needed to be checked for its conformity with the new constitution as well.

[27]The *Reichsbank's* branches in the states capitals were used by the Allies in the initial occupation period, however it's main central bodies in Berlin were not.

[28]Much of the discussions behind the scenes took place at the European Advisory Commission (EAC) that was a joint body of the three Allies set-up to facilitate planning for the post-surrender period. See Hammond (1962, p. 316).

main policy principles for post-war Germany, which these Allies agreed on, were those of demilitarization, denazification, decentralization and democratization.[29]

The Potsdam Agreement installed the Allied Control Council as the supreme governing body of the whole of Germany. Any political or economic system that was to be applied uniformly throughout the four zones, needed approval by the Council. The original plan, as stated in the Potsdam agreement, was to treat Germany as a 'single economic unit'. Of course, this required agreement on the future economic structure of Germany by all four countries. Obtaining such an agreement would prove elusive, especially with respect to the banking system.

4.3.1 American economic policy towards post-war Germany

The American government began studying feasible policies for the post-war treatment of Germany almost with the outset of the American entry into the war in 1941. Nevertheless, first concrete policy proposals for occupation would only be drawn up in the first half of 1944 as the set date for the invasion of France came closer.[30] The *Combined Directive for Military Government in Germany Prior to Defeat or Surrender*, better known as CCS 551, was a joint directive for the American and British armed forces.[31] It was a rather benign directive. It did not contain any provisions requiring a restructuring of the German economy or the banking system. While it gave the military ultimate control over the productive capabilities, the economy was to be kept at full output, with exception of the war industries. No major reconstruction or reorganization was on the cards at that time.[32]

This would change when the first American cabinet-level discussions with respect to the post-war treatment of Germany took place in the Summer of 1944. As a result of the Allied invasion in Normandy, the immediate collapse of the 'Third Reich' and its economy seemed to be a real possibility. The American military in Europe pressed urgently for more concrete policy prescriptions that would be valid after a German surrender as well.[33]

[29] France was not a party at the conferences and consequently did not sign the agreement. Thus, in principle, is was free to pursue its 'own' policy (Clay, 1950, p. X).

[30] For details of the first period up until 1944 see Hammond (1962, pp. 311–326) and Zink (1957, pp. 6–19).

[31] The directive CSS 551 was later weaved into the *American Handbook for Military Government* in Germany.

[32] See Hammond (1962, pp. 327–329), Horstmann (1991, pp. 21–23), Murach-Brand (2004, pp. 28, 30) and Zink (1957, pp. 19–20). The line of a *"stern peace with reconciliation"* taken by the CSS 551 was indeed the line advocated by the U.S. State Department. See Hammond (1962, pp. 343–344, 346).

[33] See Dorn (1957, pp, 490–491), Hammond (1962, pp. 340–341) and Murach-Brand (2004, p. 30).

At about the same time, Secretary of the Treasury Henry Morgenthau, Jr. had become acquainted with post-occupation plans for Germany on a trip to Europe in August of 1944. He and his advisor Henry D. White were outraged by the *"benevolently paternalistic character"*[34] of the provisions vis-a-vis Germany. Both were convinced that a soft peace would not be successful in preventing Germany from waging war again. On his way back to Washington, Morgenthau decided to become heavily involved in the policy planning for post-war Germany. Up to that point Morgenthau and the Treasury had hardly been involved. Morgenthau made good use of his excellent relationship with President Roosevelt to instigate a complete re-think of American policy. In late August of 1944 a cabinet commission was installed by President Roosevelt to re-consider the economic future of occupied Germany.[35]

The commission consisted of the Secretaries of State (Cordell Hull), of the Treasury (Henry Morgenthau Jr.) and of War (Henry L. Stimson). Hull, Morgenthau and Stimson all aimed to democratize Germany through de-militarizing, de-nazifying and decentralizing its political system and its economy. Yet, the main point they failed to agree on, was the long-term economic policy to pursue in occupied Germany. The opinions within the government varied considerably on this point. While Stimson argued for as little intervention as necessary and a quick exit of the military, Morgenthau was arguing for the 'pastoralization' of wide stretches of previously highly industrialized areas of Germany and a long-term engagement. In his *"Suggested Post-Surrender Program for Germany"* (better known as the original 'Morgenthau Plan') he called for the de-militarization, partitioning and decentralization of Germany. On one hand, the plan called for extreme infractions into the German state and the economic system, such as the internazionalization of the Ruhr area. On the other hand, it propagated a hands off approach in operational economic issues such as price controls, rationing and distribution. The economy was to be converted into one highly dependent on foreign trade, in order to take away its capability to re-arm in autarky. Additionally, the German population was to be held to subsistence levels. It was a plan that was extreme in its policy recommendations as it called for the

[34] Cited in Horstmann (1991, p. 25) from the Morgenthau Diary I, p. 443ff.

[35] See Dorn (1957, p. 491), Hammond (1962, pp. 348–356), Holtfrerich (1995, pp. 402–403). and Morgenthau (1946, pp. 125–126).

permanent dismemberment of Germany and it would have prevented economic reconstruction.[36] The Morgenthau plan was followed up by a series of heated memoranda between the commission members and the President's office.[37]

In particular the antitrust experts of the Treasury and the Justice department were determined to reconstruct Germany according to an idealized American model of capitalism. By extension they hoped this would influence the rest of Europe as well. The German economy with its tendency to form cartels served as a stark contrast to the ideal American model. The only major question was how far de-concentration should be taken. Was it about the break-up of just the largest companies or was it about the atomization of the entire German economy?[38] Despite the strong objections from Stimson and Hull and continued opposition throughout the spring of 1945, the basic ideas behind the Morgenthau plan became the official policy of the American Government towards Germany in the initial occupation period.[39] There was to be a strong break between Nazi-Germany and post-war Germany not only in terms of its political system, but also in terms of its economic system. The Joint Chiefs of Staff directive 1067 (or simply J.C.S. 1067) was issued to the military on May 21st, 1945, as the new basic document guiding the policies of the American Military Government in Germany. It contained very much the same policy Morgenthau had advocated for, albeit in a moderated form. In turn, the influence of the J.C.S. 1067, and thus of Morgenthau's ideas, on the Potsdam Agreement was evident as well.[40] However, guidelines were one thing. Their practical application was another matter altogether. This led to severe tensions between the American Military Government in Germany and the federal government in Washington D.C..[41] Soon enough, the Americans had to accept the realities on the ground and adapted their economic policies accordingly.

[36] See U.S. Department of the Treasury (1944) for the original Morgenthau Plan. A reprinted version of plan that Roosevelt took with him to a conference in Quebec can also be found in Morgenthau (1945, pp. 1–4).

[37] Both Hull and Stimson opposed the radical Morgenthau approach to the economy and the German population, whereas President Roosevelt was sympathetic to it. For a comprehensive description of the dispute see Hammond (1962, pp. 353–388).

[38] See Berghahn (1986, pp. 85–88).

[39] For the discussions in the Fall, Winter and Spring of 1944/45 see Dorn (1957), Hammond (1962, pp. 387–427) and Moltmann (1967).

[40] See also Murach-Brand (2004, pp. 39–40). Holtfrerich (1995, p. 405) points out that the J.C.S. 1067 underwent further moderation under the Potsdam agreement. Democratic parties were now permissible and the living standard of Germans would not be allowed to exceed the average of its neighbours. The J.C.S. 1067 had required a special permission for democratic parties and it would grant German living standards not to exceed that of its poorest neighbour.

[41] See Dorn (1957, pp. 481–482) and Stolleis (2008, pp. 280, 290).

Instead of decentralizing the German economy in order to keep it weak, it was supposed to be reconstructed according to the American antitrust ideals.[42]

The different viewpoints within the American government, with respect to German occupation policy, were a key characteristic of the period. There was no clear mandate as to which department was responsible for the occupation policy. Thus, several departments joined in on the discussion.[43] Only over time would the Military Governor General Lucius D. Clay learn to assert himself over the quarrelled departments back home, in part thanks to his superior local knowledge and in part thanks to a withdrawal of the US Treasury from occupation policy.[44] Additionally, with President Truman in power as of April of 1945, the disproportionate influence on the President's office by Morgenthau, and consequently the U.S. Treasury, had come to an end.[45] Nevertheless, many treasury officials and sympathisers with Morgenthau's views were sent to Germany as officials in the American Military Government, where they would hold key positions in the financial and decartelization divisions.[46]

4.3.2 The *Dodge plan* for the German banking system

As outlined in both the J.C.S. 1067 and the Potsdam Agreement, the basic principles of decartelization and decentralization paired with denazification also applied to the banking system. But there was no specific reform prescription other than these principles. However, what the Potsdam agreement did specify was that the banking system would be one of joint responsibility of the four Allies. Thus, any reform of the banking sector should have to be agreed upon in the Allied Control Council.

For much of the initial occupation period there had been no definite American plan as to what to do with the banking system.[47] On one hand, this was due to the fact that

[42]See Berghahn (1986, pp. 88–90).

[43]The fact that the US Treasury was initially so much involved in post-war planning carries home that point. Common sense would dictate that the Department of State or the War Department would be the obvious choices. One, because it is in charge of international affairs and the other, because it was to implement the actual policies on the ground. Indeed, during the early occupation period turf wars were a constant source of disagreement in the American administration.

[44]See Dorn (1957, pp. 494–497) and Wandel (1980, pp. 157–158).

[45]Indeed, Morgenthau was so frustrated by Truman and his administration – Morgenthau was not invited to join the US delegation at Potsdam – that he resigned in July 1945. See Holtfrerich (1995).

[46]See Horstmann (1991, pp. 54–60) and Murach-Brand (2004, pp. 43–45).

[47]For the early deliberations with respect to the Financial system see Horstmann (1991, pp. 54–60). Analyses of the German banking system and corresponding memoranda from mid 1944 until mid 1945 can be found in NARA RG 260, OMGUS, FINAD, Financial Policies & Military Government Legislation, NND 775058, Box 109.

there were much more pressing matters to attend to than the reform of the banking sector, such as the construction of a military administration, as well as dealing with the millions of refugees, prisoners and an impoverished population, which needed to be fed.[48] On the other hand, it was due to the American military on the ground not receiving much policy guidance from Washington either.[49] Washington did not press for immediate reform plans of the banking sector and General Clay and his top advisors (a businessman and a State Department official) did not see any need for reform, given that decisions with respect to the banking system were to be made jointly by the Allied Control Council. Thus, no concrete progress was made on this matter until the fall of 1945.[50]

The first reform plan that was pursued by the Americans was that decided upon by Joseph M. Dodge, the freshly instated director of the finance division of the Office of the Military Government of the United States (henceforth just "OMGUS").[51] The 'Dodge Plan' was presented to the Allied Control Council in November of 1945.[52] Although his proposal did not explicitly say so, it established that the principles of the *American state banking system* should be replicated in Germany. Emphasis was put on the elimination of 'excessive' control of the German universal banking system over German industry. For that matter, the largest credit banks, the *Großbanken*, were to be split into several smaller units and their number of branches were to be reduced. But decentralization should not stop there. The entire banking system was to be decentralized and all banks would be prevented from operating branches in other states. Indeed, Dodge's initial vision went even as far as (eventually) requiring decentralization to the county level, thus introducing American-style unit banking. Conducting business outside a bank's home state was not to be prohibited, but banks were to be kept outside the influence of any other banking or government entity. Not only would this have affected the *Großbanken*, but it also meant that the savings

[48]See the letter from Clay to McCloy from 29.6.1945 in Smith (1974, pp. 35–46).

[49]Zink (1957, pp. 89–90) reports that the issue of German occupation was not a topic of great interest to either the American media or President Truman during the first year of occupation. Domestic problems were much more pressing.

[50]See Holtfrerich (1995, p. 407). Indeed General Clay did not even have a financial or economic adviser in the first months of the occupation. See Clay (1950, p. 202).

[51]Joseph Dodge was chairman of the Detroit Bank and Trust Co. and at the same time the president of the American Bankers Association. He became director of OMGUS finance division in September of 1945. Later, Dodge would also play a key role in the economic restructuring of occupied Japan. See Holtfrerich (1995, p. 407) and Tsutsui (1988, p. 67) for biographical information about Joseph M. Dodge.

[52]For the Dodge Plan, as presented to the Allies, see the Allied Control Council Document DFIN/P(45)33, Subj.: *Elimination of Excessive Concentration of Economic Power in Banking*, dated 30.10.1945, as well as Allied Control Council Document DFIN/P(45)29, Subj.: *Elimination of Bank Power to Invest in Corporation Stocks and Engage in Stock Exchange Transactions*, dated 23.10.1945, both found in NARA RG 260, Records of US Element, Allied Control Authority, Records of the Finance Directorate (DFIN), Master File, 1945–1948, NND: 75043, Box: 353.

banks and the cooperative banks, which had formed umbrella organizations, should now give up this centralized structure as well. The best known feature of the Glass-Steagall Act, the separation of investment and deposit banks, was also to be pursued. This plan would prohibit regular banks from buying or selling stocks for their own account. Another important prohibition was to be that of banks' entitlement to exercise the voting rights of the shares of the banks' customers, so-called "proxy-voting". This arrangement had given banks not only the votes corresponding to their personal share in a corporation, but also that of its customers – an effective way to lever banks' influence without having to invest in a company. Decentralization should also apply to the *Reichsbank*. It was to be abolished entirely and each state would have its own central bank – a structure akin to the Federal Reserve System. The primary regulatory institutions were to be the departments of finance of every state - just like it was the case in the American state banking system. The central bank should be removed from most regulatory matters.[53]

The decision of Dodge to press for complete decentralization was due to two factors. On one hand it was because of the extremely negative image he and many other American officials had of the *Großbanken*.[54] They were considered to be extreme concentrations of economic power that helped to foster and sustain the Nazi dictatorship and its war machine. The old economic structures needed to be torn apart as part of a larger process aimed at restructuring German society as a whole. On the other hand, Dodge was convinced of the superiority of the American decentralized approach to banking. At the same time, he wanted to avoid the regulatory arbitrage and other problems the dual banking system was suffering from in the United States. Thus, only the state banking system was to be replicated, but the national banking system was not.[55]

[53]See also the detailed 'Dodge Memo' sent to German state government officials, where Dodge outlined his plans for *Central Banking and Bank Supervision* dated 01.11.1945, a copy of which can be found in NARA RG 260, U.S. Elements of Inter-Allied Organizations, Records of the Finance Committee of HICOG, The Allied Bank Commission, General Records, NND 775048, Box 2. Interestingly, the introduction of deposit insurance was not part of the Dodge plan. The possibility of introducing deposit insurance was briefly hinted at page 21 of *A Plan for the Liquidation of War Finance and the Financial Rehabilitation of Germany*, dated 20 May 1946, found in NARA, RG 466, Office of the Executive Secretary, General Records, 1947-1952, NND: 968095, Box 5.

[54]This view was shared by a majority of individuals in both government and business. See Horstmann (1991, p. 67). But it was not shared by everyone within OMGUS Financial Branch. See for example the Memorandum to Dodge by E.C. Ophuls from 09.10.1945, Subj.: *Financial Program for the Year October 1945 to Year October 1946*, found in NARA RG260, OMGUS, FINAD, Financial Policies & Military Government Legislation, NND: 775058, Box 69. It advocates for a unified approach towards banking.

[55]See Horstmann (1991, pp. 61–65) for Dodge's intentions. For Dodge's view of the American system see Tsutsui (1988, p. 67). For the unfavorable view Americans had of the *Großbanken* see also Clay (1950, pp. 327-328).

Table 4.3: **The intended impact of the Dodge Plan**

	Germany (1935)	**United States (1935)**	**Dodge Plan (1945)**
Regulatory Institutions	Centralized	Decentralized	Decentralized[a]
Central Bank	Centralized	Decentralized	Decentralized[b]
Branching	Free	Restricted	Restricted[c]
Investment Restrictions	Universal banking	Separation of investment and deposit banks	Separation of investment and deposit banks[d]
Deposit Insurance	None	Yes	Not mentioned

[a]Regulation and supervision should be decentralized to a state level. The central bank should be excluded from banking regulation entirely.
[b]Replication of the Federal Reserve System.
[c]At the very least restriction to the state level. If possible it should even be restricted to a municipal-level, i.e. introduction of unit banking.
[d]Just like it was prescribed in the Glass-Steagal Act of 1933.

4.3.3 Discussions amongst all four Allies

When the American Military Government introduced its *Dodge Plan* to the Allied Control Council in November of 1945, it had hoped to be able to press through this item by the spring of 1946. Indeed, Dodge's plans were discussed on numerous occasions in the Allied Control Council.[56] While there was considerable agreement amongst the American, French and Soviet representatives, that decentralization of the banking system should take place, the British had strong doubts with respect to this policy. They feared that decentralization would make the banking system unstable and jeopardize the recovery of the German and thus British economy.[57] Furthermore, the British were aware that such decentralization would make coordination of banking policy between the Allies difficult. They were only willing to further this policy, if there was to be a central bank of some sort, spanning all four zones. Such a central bank covering both West and East-Germany was unacceptable to both the Soviets and the French at that point in time. Consequently, decentralization discussions within the Allied Control Council stalled in the fall of 1946. The negotiations surrounding a separation of universal banks into deposit and investment banks continued until the Control Council ceased to operate in 1948, but did not yield any tangible results

[56]Loehr (1952, p. 8, fn. 9) reports that 30 proposals for financial reform were drawn up in the Allied Control Council until May of 1946.

[57]Indeed, they considered a more centralized banking system more efficient. After all their own bank system was more similar in structure to the German than to the American system. See Dickhaus (1998, pp. 163–164), Holtfrerich (1995, pp. 410–414) and Horstmann (1991, pp. 68–75) for the British policy approach to the banking system.

either.[58] Instead, while discussions were ongoing in the Allied Control Council, each country went about realizing their visions for the banking system within their own zone. This made any future quadripartite agreement on the issue more unlikely by the day. The most resolute action was undoubtedly taken in the Soviet zone.

4.3.4 Soviet bank reform in East-Germany

The Soviet Military Government irrevocably tore apart the East-German banking system within a matter of months, ensuring that the old 'universal' bank system could not re-emerge. The banks and the transfer system were shut down as soon as the war was officially over. While savings banks and credit cooperatives were allowed to re-open eventually, private banks were nationalized.[59] No compensation was paid to the owners, and depositors did not receive any of their money back. The banks' assets were then used to capitalize five newly founded regional state banks.[60] These were government-run universal banks so to say. The state banks' board of directors consisted almost entirely of political appointees.[61] Last but not least, the five state banks were equipped with a government guarantee to cover any losses that went beyond its reserves and 10% of the capital. This was paired with an explicit order *"[...] not to operate on the basis of profit and loss calculations, but in the 'public interest' [...]"*.[62] Of course the measures taken were a function of the economic system the Soviets were implementing, which saw no place for private initiative. This is why, the Soviet bank reform is not analyzed further in this chapter.[63]

[58] The minutes of the Allied Control Council Meeting from 22.04.1946 (*DFIN/M(46)13*) clearly displays the different positions of the Allies with respect to decentralization. It was found in NARA RG260, OMGUS, FINAD, Financial Policies & Military Government Legislation, NND: 775058, Box 66. Furthermore see also Adler (1949, p. 325), Smith (1974, pp. 429–430), Dickhaus (1998, pp. 163–166) and especially Horstmann (1985). With respect to the separation of investment and deposit banks see the existing drafts printed as an *Appendix to DLEG/P(40)2nd Review* found in NARA RG260, OMGUS, FINAD, Financial Policies & Military Government Legislation, NND: 775058, Box 69.

[59] Only a handful of small private banks were allowed to operate for a few more years until they were forced to close as well. The largest credit banks lost each between 33% and 67% of their branches due to nationalization (Wandel, 1980, pp. 83–84).

[60] They would be the most important banks in the Eastern Zone by the end of 1946 with almost 75% of the assets of the banking sector

[61] Members of the board of directors were the respective state's president, the finance minister, 8 more political appointees and two representatives of the banks' staff.

[62] See Adler (1949, pp. 333–335).

[63] For a detailed account of the Soviet transformation see for example Deckers (1974, pp. 12–98).

4.4 The Institutional Assimilation in West-Germany (1945-1949)

Already within the first year of occupation, it came to significant changes of the western Allies' general economic policies. While the French generally still adhered to the 'Morgenthauian' principles of keeping Germany weak[64], the Americans changed their policy stance.[65] They no longer intended to restrain the German economy. Rather they planned the reconstruction of the German economy on the basis of democratic, bottom-up, federal principles similar to those in the United States. Britain was generally supportive of this approach as well.[66] By the summer of 1947, the Joint Chiefs of Staff directive 1067 was replaced by directive 1779, which had the aforementioned reconstruction at its heart and officially broke with the Morgenthau mantra of keeping the German economy feeble.[67]

Why the change of heart? Three developments were crucial. First, it was soon realized that keeping the German economy weak and having to feed the German population with the help of American taxpayer's money was expensive; widespread famine was not an option. Second, it would be impossible to convince the German population of the superiority of democratic values and institutions, if, in fact, their standard of living was well below that prior to the war and even during the war. Third, the Americans had to acknowledge that, as Secretary of War Stimson and the British had previously argued, the speed of the recovery of Western Europe depended to a large extent on the reconstruction of Germany.[68] Another important point were the dynamics of the Cold War. A feeble Germany was seen as a power vacuum, which the Soviet Union would try to fill. Thus, security considerations became a dominant factor of US policy in Germany.[69] However, even though the J.C.S. 1779 was constructive in terms of rebuilding the German economy, it

[64]This is no surprise, given that France had been invaded by Germany thrice in the previous 70 years as Wandel (1980, p. 42) points out. Instead, German production was to be used for the reconstruction of France.

[65]The Stuttgart speech by Secretary of State James F. Byrnes is emblematic of this change in policy. See Clay (1950, pp. 8, 78–81).

[66]See Stolleis (2008, pp. 288, 308).

[67]See Holtfrerich (1995, p. 406). General Clay had been advocating for a pragmatic policy overhaul since the beginning of 1946 already. See Berghahn (1986, pp. 90–92).

[68]See the explanation by Adler (1949, p. 340), a former high level official in the banking section of OMGUS.

[69]See Murach-Brand (2004, pp. 80–82). See also Hansmeyer (1998, p. 15) or Wandel (1980, p. 158) and their discussion of the prominent role of the Hoover-report. This change in policy, from a punitive one outline in the Morgenthau Plan and the J.C.S. 1067, to one of reconstruction, led the frustrated Henry Morgenthau to conclude that if the policies prescribed would not be applied in the future, *"the foundations for renewed German aggression [...] would have been laid"*. See Morgenthau (1946, p. 129).

still explicitly called for the decentralization of the banking system.[70] Therefore, although the initial occupation period was one of political change, there was policy continuity with respect to banking regulation throughout the first years of the occupation period. Within the Finance Division there was surprisingly little open disagreement over the reform plans laid out by Dodge.[71]

Thus, at the same time that Dodge launched his foray in the Allied Control Council for a quadripartite restructuring, he initiated the assimilation process in the American zone. His plans were sent to the respective German state governments, which were then expected to issue laws that corresponded with Dodge's vision.[72]

4.4.1 Decentralization of the regulatory institutions

The assimilation of the regulatory institutions was probably the easiest task at hand. Even though the Credit Act of 1934 (in its amended form from either 1939 or 1944) might still have remained in force, it could not be applied directly anymore. The directorate of the *Reichsbank* and the Commissioner of the Banking system – the main regulatory bodies – were both dissolved by the Allies at the end of the war. During the initial occupation period the Allies took over regulatory powers. After the re-establishment of state governments, the Americans and the French began to transfer limited regulatory powers to the Finance Ministries of each state (and to a lesser extent to the remnants of the central bank in each zone), paired with the task to establish a dedicated oversight agency.[73] Regulatory powers remained with the Finance Ministries of the states, none of which created a dedicated oversight agency. As of 1946 several proposals were drawn, all of which would have reinstated the German Credit Act of 1934 (in its amended form) on a decentralized basis.

[70] See Holtfrerich (1995, p. 406).

[71] This is in a stark contrast with the Deconcentration Branch of the Economic Division of OMGUS, where officials clashed repeatedly over the extent and the desirability of the decentralization of German industry. For the disagreements within the Deconcentration Branch see for example Berghahn (1986, pp. 98–99), Martin (1950, pp. 187-204) or Murach-Brand (2004, pp. 43–50). It is probably due to the fact that there was a strong presence of Treasury personnel in the finance division. Also, Dodge had an important like-minded ally in Walter Lichtenstein – a former vice-president of the First National Bank in New York, and chief of the Financial Institutions Branch. See Ahrens (2007, pp. 162–163).

[72] This directive was issued on the 12.12.1945. See OMGUS (1949b, No. 6, January 1946, page 12). See also the *Dodge Memo* that was sent to German state government officials, where Dodge outlined his plans for *Central Banking and Bank Supervision* dated 01.11.1945, a copy of which can be found in NARA RG 260, U.S. Elements of Inter-Allied Organizations, Records of the Finance Committee of HICOG, The Allied Bank Commission, General Records, NND 775048, Box 2

[73] The fact that the responsibility for the banking sector shifted from the respective States' Ministries of Economics to the States' Ministry of Finance, was a major break with the German administrative tradition.

The American Military Government rejected these proposals, as it wanted a strict separation between monetary policy and technical supervision. Consequently until 1949, when the Americans passed a corresponding military law, regulatory supervision was relatively light.[74]

The British maintained unified regulatory institutions and a single 'central bank' for their entire zone at first.[75] In 1947 they delegated some authorities to the state governments, but it was only in 1948, when the Americans and the British agreed to form an economic bizone that the British decentralized the regulatory institutions entirely to the state level.[76] From then on, all three western zones had similar arrangements with respect to the regulatory institutions.[77] In every state it was now a duopoly which was in charge of banking regulation: the states' 'central banks' together with the states' ministries of finance. Instead of there being two regulatory institutions for the whole of Germany there were now 20. As of 1948, the Americans pressured the German state governments to prepare a revised banking act to codify the changes to the regulatory institutions. It would take the Germans until 1961 to come up with a 'new' banking act.[78]

4.4.2 Branching restrictions and decentralization of banks

Deconcentration efforts of the banking system focused initially on the three remaining *Großbanken*, the Deutsche Bank, the Dresdner Bank and the Commerzbank.[79] It was not merely a measure of punishing these banks for their involvement in the Third Reich. More importantly, the Americans tried to break-up the large credit banks because they

[74] See BArch102/23052 Letter from Fischer to Kattenstroth from 31.01.1950 as well as OMGUS (1949b, No. 2, p. 2 and No. 5, p. 1), and a copy of a Letter from Jack Bennet (Finance Advisor) to the Finance Divisions in the American zone (undated - probably mid 1948), and the rejection Cable by the Military Government to the Länderrat, dated 28 May 1948. Both documents can be found in NARA RG 260, U.S. Elements of Inter-Allied Organizations, Records of the Finance Committee of HICOG, The Allied Bank Commission, General Records, NND 775048, Box 2. For the law see OMGUS (1949a, Law No. 57 (revised), Art 1 & 2). See also the

[75] They continued to use the structures of the *Reichsbank's* former Hamburg office as a central clearinghouse for their entire zone.

[76] The corresponding ordinance to transfer regulatory power to the Finance Ministries of the states in the British zone came in force on 01.04.1948. See CCG/BE (1949, Ordinance No. 133, Art. 1 & 2). See also Wandel (1980, p. 63).

[77] The Americans would pass a military law to harmonize legislation with the British zone on 15.04.1949. See OMGUS (1949a, Law No. 57 (revised), Art 1 & 2).

[78] See also Chapter 3 of this dissertation.

[79] Two of the other *Großbanken*, the *Reichskreditgesellschaft* and the *Berliner Handelsgesellschaft* were based in Berlin and had no branches. They were shut down and liquidated right at the end of the war by the Soviets. The *Bank der deutschen Arbeit* was also shut down and liquidated by all four Allies, as it was a bank directly linked to the National Socialist Party via the German Labor Front. See Loehr (1952, p. 53).

believed that the concentration of financial power made it easier for Germany to wage war and that decentralization might prevent Germany from building up as rapidly as it did. In particular the contribution of the large credit banks was seen as a crucial element.[80] This idea is somewhat puzzling, not because the large credit banks were not engaged in re-armament and war finance – they undeniably were to some extent.[81] It is puzzling because the country with probably the most decentralized banking system in the world, the United States, had no problem mobilizing its resources and converting its economy into the most efficient armament factory in the world at that time. The American banking system accomplished this with the help of well-developed financial markets. Nothing prohibited Germany from building equally efficient capital markets of her own over time.[82]

The decentralization effort becomes more plausible when it is put into a larger perspective. It formed part of a drive to restructure the German economy along the same federal lines America's economy was built upon. A decentralized regulatory regime and central bank would only make sense if the banks were not operating on a national scale either. Thus, the break-up of the large credit banks was also a regulatory necessity.[83] Indeed, neither the Americans, nor the French proceeded to break-up the major large credit banks immediately after the war ended. It was only in the fall of 1945 that the Americans initiated this development, in parallel with the decision to decentralize the regulatory supervision. While doing so, Dodge and his colleagues were aware that, from an efficiency standpoint, this might not be the ideal solution. But they sincerely believed that the political gains would outweigh the economic costs.[84]

Initially, the decentralization of the three remaining largest credit banks (Deutsche Bank, Dresdner Bank and Commerzbank) did not progress much. After all, the Americans were hoping for quadripartite action on this matter via the Allied Control Council. At the same time that the Americans were trying to obtain a multilateral agreement, the

[80]See for example Adler (1949, pp. 340–341), Horstmann (1991, pp. 63–64) or Clay (1950, pp. 327-328). See also Dodge's *Statement to the Finance Directorate of the Allied Control Council* on 05.04.1946, as *Appendix "A" to DFIN/M(46)11*, which can be found in NARA, RG 260, OMGUS, FINAD, Financial Policies & Military Government Legislation, General Records Re: Financial Policy & Legislation 1945-49, NND 775058, Box 66.

[81]Direct government finance by the large credit banks was limited. Merely 10% of government bonds were held by the large credit banks at the end of the war. The vast majority was held within the Sparkassen-system. See Holtfrerich (1995, p. 415).

[82]See Tooze (2007) for production figures during the Second World War. A similar point regarding the efficacy of decentralized and centralized banking sectors was made by Adler (1949, p. 341).

[83]See Ahrens (2007, p. 163) and Horstmann (1991, p. 67).

[84]See Horstmann (1991, p. 100).

three *Großbanken* attempted to re-establish their former unity across the western zones of occupation with the silent agreement of the German state governments, even though this was clearly against the plan set forth by the American Military Government. This prompted the American Military Government to issue a 'cease and desist' order on the 12th of March, 1946, representing a first 'cut' to the zone level. Banks within the American zone (and soon thereafter in the French zone too) were prohibited from contacting their banking headquarters located outside of their zone. The three *Großbanken*, were explicitly prohibited from cooperating in any way with their former headquarters in Hamburg.[85] However, the banks were generally allowed to maintain correspondence accounts with banks outside their zone. The ordinance was the first step to turn the Dodge Plan into policy actions that concretely affected the banking system in its structure and operation.[86] Contrary to this, the British tried to avoid change in the banking system in their zone. Yet, they had to accept the realities created by both the French and the Americans, that restricted banks based in the British zone from expanding into the other zones.

It was only in the first half of 1947 that the three remaining *Großbanken* were broken up into even smaller units. The quadripartite solution had not materialized, and the German state governments or the banks themselves had not taken any action either.[87] The *Großbanken* had already been divided along the zonal lines. Now they were broken-up to the state level. The names of the resulting institutes were to be changed as well, so as not to resemble their former affiliation. Additionally, custodians were appointed that were expected to manage and administer the property of the banks within each state. This was first decreed on May 6th, 1947, in the American zone, followed by the French on October 1st, of 1947.[88] By April 1st, 1948, the British followed suit as part of an arrangement that had lead to the economic Bizone between the American and British zone. The British agreed to decentralize their banks, since they realized that in a 'Bizone', the Americans would have the upper hand, and that the British were unlikely to be able to put the

[85] Anticipating a Soviet occupation of Berlin, the Deutsche Bank, the Dresdner Bank and the Commerzbank, had begun to relocate their head offices from Berlin to Hamburg before the end of the war. See Hansmeyer (1998, p. 21) and Horstmann (1991, pp. 42–46, 75–81).

[86] For the ordinance see Horstmann (1991, p. 105).

[87] The Americans had just passed Military Law No. 56, which prohibited an 'excessive concentration of economic power' on 27.01.1947 (OMGUS, 1949a, Law No. 56). There was also a major reshuffle within the Finance Division that was aimed at reviving the stalling deconcentration efforts. See Horstmann (1991, p. 111).

[88] The American Military Law Nr 57 became effective on 06.05.1947. It came as a surprise to the majority of the banking sector. Merely the Deutsche Bank saw it coming. See Horstmann (1991, pp. 117–118) and Holtfrerich (1995, pp. 420, 422). For the law see OMGUS (1949a, Law Nr. 57: Custodians for Certain Bank Organization) or the reprint in the aforementioned Holtfrerich.

American decentralization drive into reverse. Thus, their strategy was to make the best out of their situation – and the best, from the point of view of the British, was to have the Americans shoulder a larger share of the financial burden of occupation. Consequently, they advocated for both a bizonal budget and a real bizonal central bank. Thus, while the Americans agreed to installing a central bank for both zones, the British agreed to decentralize their banking sector in turn. And so, out of three Großbanken became thirty.[89]

The attempt to finally extinguish the centralist ambitions of the *Großbanken* was a botched reform. Again it was expected from the Germans to eventually pass a democratically legitimized law codifying the assimilation. Also, legally, the newly founded institutes were subsidiaries of the 'old' *Großbanken*, which formally continued to exist. The old *Großbanken* had no operational business of their own and the board of directors and the oversight board were both 'disfunctionalized' by the Allies. It was like a financial conglomerate with a dysfunctional central body, which was prohibited from interacting with all its subsidiaries. Nevertheless, the legal shell of the 'old' *Großbanken* lived on. The *Großbanken* 'problem' had not been solved, after all.[90]

What had happened to the *Girozentralen* and the *Zentrallkassen* – the regional umbrella organizations of the Savings Bank System and the Credit Cooperatives? They too were large (universal) banking organizations that in some cases were active in several states and also served as clearing houses. Interestingly enough, for the most part, they were able to fly below the Americans' radar. The Military Government was focusing on the the *Großbanken*, and it largely overlooked the *Girozentralen* and *Zentralkassen*. Only in the summer 1948, when the *Großbanken* had been decentralized and a central bank established, did OMGUS' Finance Division develop a keener interest in the *Girozentralen* and *Zentralkassen*. They too were to disappear entirely. More than a threat to security they saw them as instistutions that were undermining the recently established central bank and its effort to create a unified clearing system. Both the Sparkassen and the Credit Cooperative system had developed alternative cashless payment systems alongside the central bank's system prior to the Second World War. Consequently, the Military Government

[89] Each of these banks could maintain branches within their state. See figures 2 and 3 on pages 167 and 168 respectively, for an overview of the break-up. See also Holtfrerich (1995, pp. 422-423, 431) and CCG/BE (1949, Ordinance No. 133: Decentralization of banks).

[90] The Allies were aware of this problem. See for example the Memo by Kelleher to James from 21 August, 1950, Sub.:*Status and Problems of German Banking Reorganization*, found in NARA, RG 466, Office of General Counsel, Decartelization Division, General Subject Files, 1948-55, NND: 903642, Box 1. See also Ahrens (2007, p. 174), Loehr (1952, pp. 54–55) and Wandel (1980, pp. 89–90).

asked for a working group of German officials[91] to come up with proposals to restructure the savings bank and credit cooperative systems, including the dissolution of the umbrella organizations. The Germans dodged the task by presenting a memorandum declaring the unfeasibility of such a move. No further actions were taken by the Allies until the establishment of the Federal Republic of Germany in 1949. The public savings bank system and the credit cooperative system remained largely unscathed by the decentralization efforts. Only the branching restrictions applied to them – as far as they applied to any bank.[92]

Table 4.4: **The balance sheet size of the 30 decentralized subsidiaries of the former *Großbanken* by region**

		31.12.1949	31.08.1950
		(in Million DM)	
	American Zone		
	Hessen		
a)	Hessische Bank, Frankfurt a. M.	219	279
b)	Rhein-Main-Bank, Frankfurt a. M.	213	316
c)	Mitteldeutsche Creditbank, Frankfurt a. M.	63	88
	Bayern		
a)	Bayerische Creditbank, München	182	185
b)	Bayerische Bank für Handel und Industrie, München	112	142
c)	Bayerische Discontobank, Nürnberg	38	42
	Württemberg-Baden		
a)	Südwestbank Stuttgart	301	363
b)	Allgemeine Bankgesellschaft, Stuttgart	103	127
c)	Bankverein für Württemberg-Baden, Stuttgart	58	76
	Bremen		
a)	Disconto-Bank, Bremen	102	78
b)	Bremer Bank, Bremen	78	84
c)	Bremer Handelsbank, Bremen	21	21
	British Zone		
	Nordrhein-Westfalen		
a)	Rheinisch-Westfälische Bank, Düsseldorf	818	1032

[91]The working group was made up of officials of the recently established central bank and the finance department of the bizonal economic administration.

[92]See the Memo by Adolphe Warner to the Allied Banking Council from 06.11.1948, Subj.: *Background for Savings Bank Decentralization*, found in NARA RG 260, OMGUS, FINAD, Financial Policies & Military Government Legislation, Correspondence Re: Financial Policy & Operations, 1946-49, NND: 775058, Box 90. See also the Letter by the Finance Adviser of the British Zone, Sir Eric Coates and the Finance Adviers of the American Zone, Jack Bennett, to the Chief of the Finance Group of the Bipartite Control Office of the U.S. Army from 09.06.1948, as well as a Memorandum on the *Decentralization of Banking* from 04.02.1949, both of which can be found in NARA RG 260, U.S. Elements of Inter-Allied Organizations, Records of the Finance Committee of HICOG, The Allied Bank Commission, General Records, 1948-51, NND: 775048, Box 2.

		31.12.1949	**31.08.1950**
		(in Million DM)	
b)	Rhein-Ruhr-Bank, Düsseldorf	431	514
c)	Bankverein Westdeutschland, Düsseldorf	416	558
	Niedersachsen		
a)	Nordwestbank, Hannover	133	156
b)	Niederdeutsche Bankgesellschaft, Hannover	65	95
c)	Merkur-Bank, Hannover	67	98
	Hamburg		
a)	Norddeutsche Bank in Hamburg	279	284
b)	Hamburger Kreditbank, Hamburg	220	277
c)	Hansa-Bank, Hamburg	177	143
	Schleswig-Holstein		
b)	Lübecker Bank für Handel und Industrie, Lübeck	9	12
c)	Holsten-Bank, Kiel	23	28
	French Zone		
	Baden		
a)	Oberrheinische Bank, Freiburg i.Br.	110	123
b)	Süddeutsche Kreditanstalt, Freiburg i.Br.	21	22
	Rheinland-Pfalz		
a)	Rheinische Kreditbank, Ludwigshafen/Rhein	121	127
b)	Industrie- und Handelsbank, Mainz	59	71
c)	Mittelrheinische Bank, Mainz 17	21	
	Württemberg-Hohenzollern		
a)	Württembergische Vereinsbank, Reutlingen	43	48
b)	Bankanstalt für Württemberg und Hohenzollern, Reutlingen	6	9

Note:

a) formerly Deutsche Bank

b) formerly Dresdner Bank

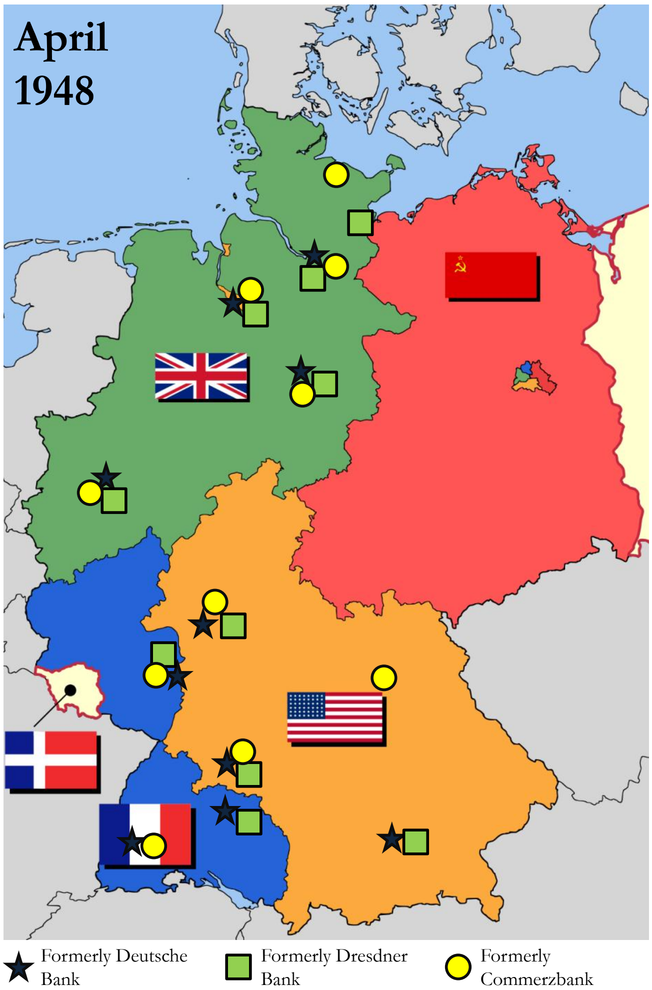
c) formerly Commerzbank

In 1950 the *Großbanken* had been decentralized for about 2-3 years already (depending on the occupation zone). Most of them were able to expand their balance sheets. *Source: BArch B102/28179, "Abschrift: Bilanzsummen der 30 Nachfolgeinstitute der Großbanken (in Mill. DM)".*

4.4.3 A federal central bank and a new currency

The decentralization of the German central bank was one of the key objectives in the American decentralization effort. The original *Reichsbank* structure differed greatly from

FIGURE 4.1: **Out of 3 became 30**



The successor banks of Deutsche Bank, Dresdner Bank and Commerzbank and their corresponding headquarters by the end of April of 1948l. *Source: Own work based on a map by Wikimedia Commons (2008).*

the American Federal Reserve System, in three key ways: first, it had a centralized decision making body. Second, it was subject to political influence. And third, it was actively competing with commercial banks through its branches. The Americans preferred a central bank modeled after the Federal Reserve, more decentralized, less susceptible to political influences and more limited in function, especially not as a competition to commercial banks.[93]

The first official proposal for a central bank was made in the spring of 1946 by Josef

[93] See Loehr (1952, pp. 10–11).

M. Dodge in the Allied Control Council.[94] Dodge introduced the idea of installing a Germany-wide (yet decentralized) *"Länder Union Bank"* in an effort to break the British resistance in the discussions surrounding the decentralization of the banking system as a whole. While it did indeed break British opposition, it created opposition with the French and the Soviets who opposed any centralized monetary authority, and consequently the proposal stalled – and with it the quadripartite talks surrounding the decentralization of the banking system as a whole as well.[95]

The German state governments of the American zone had been requested to develop proposals for the introduction of state central banks of their own. At first, they were reluctant to do so, but eventually they came up with drafts. From the American perspective, the initial drafts were uncomfortably close to the old *Reichsbank* system. However, by the fall of 1946 under strong American pressure, they presented a satisfactory draft, which the German state governments of the American zone were allowed to pass into law.[96]

On the 1st of January 1947, the 'new' state central banks were created. They were modelled after the Federal Reserve Banks in the sense that they would be led by an independent board of directors, whose members were to represent all parts of the economy. Also, the state central banks' shares were to be sold to member banks within the state no later than two years after the founding date of the state central banks.[97] It was hoped that the respective state governments would embrace the state central banks as a means of influencing regional economic policy, which would not prove to be the case.[98] As the state central banks did not have the authority to issue money, their main function was that of clearinghouses and of fiscal agents for the state governments. To a limited extent they were also involved in the regulation of the banking sector. However, every major decision by the state central banks had to be approved by the Military Government. As

[94]That is why it is sometimes also known as the 'Second Dodge Plan'. See Allied Control Council Document DFIN/P(46)39, Subj.: *Proposal for a new Laender Union Bank*, dated 05.04.1946, found in NARA RG 260, Records of US Element, Allied Control Authority, Records of the Finance Directorate (DFIN), Master File, 1945–1948, NND: 75043, Box: 353. Also reprinted in Wandel (1980, pp. 174–175).

[95]See Horstmann (1985, pp. 11–13) and Wandel (1980, pp. 55–59).

[96]In Hesse, the Military Government had to decree the passage of the corresponding law. See Wandel (1980, p. 61).

[97]However, this never happened and they remained in control of the respective states. See (Loehr, 1952, pp. 9–11) and Martin (1950, p. 190).

[98]See the memo by Warner to Pumphrey, Subj.:*Decentralization of banking*, dated 09.02.1950, found in NARA, RG 466, Office of General Counsel, Decartelization Division, General Subject File, 1948-55, NND: 903642, Box 1.

usual, the French shadowed American policy and followed suit just a few months later.[99] These state central bank laws in Bavaria and Württemberg-Baden were to be the only ones during the assimilation attempt that the Americans (and the other Allies) did not have to pass as military decrees.[100]

The British Military Government only agreed to decentralize the 'central bank' within their zone once the preparations for a merger of the American and British zones into a 'Bizone' had gathered steam. As part of the Bizone deal, the British decentralized their banking sector, the regulatory institutions and the central bank. In return, the Americans agreed to establishing a real central bank for the Western Zones - not just a coordinating body as they had preferred.[101] To the Americans, coming to an agreement with the British was more important in terms of reviving the German economy than the exact structure of the future central bank.[102] After all, it would only be a provisional central bank for the western zones, which was needed as a prerequisite for desperately needed currency reform.[103] As usual, the French trailed the Americans – and this time also the British – by three months in joining the new Central Bank System.[104]

The *"Bank deutscher Länder"*[105] (BdL), as the new central bank was called upon its establishment in March of 1948, was largely based on the Länder Union Bank Plan that had been proposed by Dodge in the Allied Control Council two years earlier. It did not lead to an exact replica of the Federal Reserve System, but it was close to it.[106] To some extent the BdL was a compromise between British and American viewpoints.[107] It was headed by a directorate, based in Frankfurt, which carried out the policies decided upon by the central bank council. The central bank council was mainly composed of

[99] The state of Bremen, which had been part of the British zone but became part of the American zone on 21. January, 1947, passed a similar state central bank law soon thereafter. For a more detailed discussion and the various laws see Adler (1949, pp. 327–328), Loehr (1952, pp. 10–12) and Wandel (1980, pp. 59–65).

[100] Even so, the German government in the American Zones was not democratically legitimized at the point in time, but nominated by the American Military Government. See Horstmann (1991, p. 110).

[101] See Dickhaus (1998, pp. 164–165) and Holtfrerich (1995, pp. 422–423, 431).

[102] See Smith (1974, pp. 429–430, 435).

[103] Inflation was galloping, black markets and the cigarette currency were widespread. Currency reform had been on the agenda in the Allied Control council since mid-1945, but agreement failed due to political reasons. See Wandel (1980, pp. 132– 156, 162–165).

[104] See Wandel (1980, p. 68).

[105] The literal translation is *"the Bank of the German States"*.

[106] See the comparison by Cwik (1970) or Wandel (1980, pp. 80–81).

[107] See Buchheim (1999, pp. 74–80), Dickhaus (1998, pp. 164–166) and Marsh (1992, pp. 144–150) for a treatment of the Allied discussions in the run-up to the founding of the Bank der Länder. See also Deutsche Bundesbank (1998) for the limited involvement of German experts on this matter. However, please not that this source does not provide specific references.

the presidents of the state central banks and was nominally independent from German political influences.[108] However, it was super-seeded by the newly formed Allied Banking Commission (ABC), which had veto power over any council decisions. The ABC was even based in the same building as the central bank. The BdL had no branches and was a banks' bank. It could only engage with the German states' central banks, the German or Allied governments, or other foreign central banks. The state central banks were also involved in the regulation of the banking sector, together the states' regulatory institutions.[109] After the currency reform of 1948, the Bank deutscher Länder would be also given the note issuing monopoly.[110]

With respect to the *Reichsbank*, the Bank deutscher Länder differed in four key respects: control was more decentralized, it did not compete with commercial banks anymore, it imposed minimum reserve requirements and it had a monopoly on bank balance settlement across states.[111] The establishment of the BdL was also a 'return of the old guard'. Many senior figures in the newly-founded BdL had already been working at the *Reichsbank* before the Second World War. In particular, the president of the new directorate, Wilhelm Vocke, had been member of the old *Reichsbank* directorate prior to the Second World War. Nevertheless, the old guard was outnumbered and outvoted by the presidents of the state central banks.[112]

4.4.4 Only partial resistance to the assimilation

Interestingly, German resistance to the American assimilation efforts varied. Not all measures were vigorously opposed and not all the states opposed in equal measure. The decentralization of the regulatory institutions to a state level and the transfer of competence to

[108] Indeed, there was no central central German government yet, which could have influenced it directly, as Marsh (1992, p. 144) points out.

[109] Thus by 1949, 20 institutions were involved in the regulation of the banking sector. Their actions would be coordinated in a central commission for banking supervision. See for example Honold (1956, p. 86).

[110] For the BdL Law see OMGUS (1949a, Law No. 60) and CCG/BE (1949, Ordinance No. 129). For a comparison of the *Reichsbank* and the BdL see Deutsche Bundesbank (1988, pp. 88–91). For an overview of the West-German currency reform see Bennett (1950), Buchheim (1988, 1999) and Häuser (1998).

[111] See Loehr (1952, p. 12–13).

[112] Indeed, the influence of *Reichsbank* figures on German central banking would not wane until the 1970s. See Marsh (1992, pp. 20–22, 159–161) for a treatment on the "return of the old guard". Apparently, the Allies tried to avoid the full-fledged return of the old *Reichsbank* guard. See Wandel (1980, pp. 74–77) for the Allies' initial difficulties in finding qualified individuals to lead the new central bank. Prior to the establishment of the Federal Republic of Germany OMGUS moved to harmonize state central bank legislation in the zones. See OMGUS (1949a, Law Nr. 57 (revised)).

the Finance Ministries was accepted by the German states without much ado. And there was of course no federal government any longer, which could object. The introduction of state-level central banks caused some resistance from German state government officials at first. Not so much because of the decentral structure, they soon began to appreciate the federal powers it came with, but because of the extent of political influence the government would have over the state central banks. The Americans were not prepared to grant the state governments any direct political influence. The state governments wanted at least some. Once the BdL was put in place, its structure was accepted and not opposed in the first years of its existence.[113]

The trickiest part of the assimilation was undoubtedly the introduction of branching restrictions and the decentralization of the *Großbanken*. Branching restrictions had generally not existed since the emergence of the German nation state. And there was no German interest group that sought a restriction of branching. Thus, the branching restrictions amounted to an imposition of American ideology. Unlike the powerful unit bank lobby in the United States, branching restrictions had little support in Germany. And even back in the United States, branching became more wide-spread during this period. The *Großbanken* had been reduced in numbers, and had been badly shaken up by the war, but they still possessed a disproportionate amount of political clout in West-Germany. They would not decentralize voluntarily. On the contrary, right after the war had ended, the *Großbanken* went about re-establishing their unity. Later on they even ignored Allied orders to cease active cooperation between the former Hamburg 'headquarters' and the local entities in other zones. Cooperation continued on a covert basis. Information flows between the headquarters in the British zone and the corresponding banks in the other zones became more time consuming, but they never ceased.[114]

[113]See Deutsche Bundesbank (1988, pp. 29–31), Holtfrerich (1995, pp.415–419), Horstmann (1991, pp. 96–103, 110–111), and Loehr (1952, pp. 10–11). Indeed, the BdL was able to build a remarkable degree of independence from both the ABC and the German government, which also increased its reputation with the public, as Berger (1997, pp. 434–435) points out.

[114]See the description of the 'covert' management of the Dresdner Bank via the Hamburg headquarters in Ahrens (2007, p. 164). For a more general overview of the extent of cooperation see Horstmann (1991, pp. 187–188) or Holtfrerich (1995, pp. 411–412). During the war, the large credit banks had already prepared themselves for some kind of de-centralized operation in order to secure the existence of the banks. The banks operative divisions were relocated to other cities throughout Germany. These preparations began as bombings of Berlin, where their headquarters were originally located, intensified and the defeat and occupation of Germany became more certain. For the preparations of the large credit banks see Horstmann (1991, pp. 42 – 46). It is likely that these preparations benefited them in maintaining contact even after the Allies prohibited them to do so.

German state officials were generally opposed to the proposed changes to the *Großbanken* as well. The notable exception was the government of the state of Württemberg-Baden, which was led by committed federalists, who actually favored such a move, but only under the condition that the necessary measures were taken to ensure the continued economic and financial integration with the rest of the country. The government of the state of Hesse was willing to compromise and consequently drafted a proposal for the decentralization of the *Großbanken*. This foresaw that the branches of the three large credit banks active in the state would have been merged into a single large credit bank. It was meant as a partial concession to the Allied demands of nationwide decentralization, while at the same time bringing about greater regional concentration. A first draft of the bill was shown by the Hessian government to representatives from both the large credit banks and industry, who vehemently opposed it and quickly succeeded in having the bill withdrawn. Even so it is also highly doubtful, whether it would ever had a chance to be accepted by the American military government. After all, the bill would have created a regional behemoth. The *Großbanken* refused to cooperate outright with the American demands, even though they were aware that they might not be able to prevent Allied decentralizing actions. They anticipated that control would eventually be returned to a German federal government. And if the *Großbanken* and the German governments had not taken part in their dismantling it would eventually be easier to demand the recentralization on the grounds that the decentralization had been an American imposition in the first place. Consequently, the lobbied the state governments to remain passive.[115]

One of the most vehement opponents of the decentralization of the *Großbanken* and the introduction of branching restrictions was the Minister of Economics of the state of Bavaria, Ludwig Erhard.[116] He advocated for a federal political system, but with a centralized economic system, with supraregional capital, which saw no role for branching restrictions or decentralization of the *Großbanken*. However, the German state officials did not engage the Allies head-on in this matter. Instead they went on a path of passive resistance by remaining largely inactive. After all, this topic was not one of general interest to the public, and hence politicians were not subject to public pressure. The only pressure they were subject to, was the American military government, and of course

[115]See Adler (1949, pp. 325–329), Holtfrerich (1995, pp. 415–416, 419) and Horstmann (1991, pp. 96–103).

[116]Only a few years later he would become Economics Minister and, eventually, Chancellor of West-Germany.

the affected banks' and insturies' interest groups. At best, they would submit memoranda describing the undesirability of decentralizing the banking sector down to the state level. These memoranda by both state government officials and representatives of the *Großbanken* highlighted the historical role of the *Großbanken* in the German banking system and their future role in the reconstruction the German economy, as well as the legal complexities involved in a break-up.[117] The bureaucrats' and legislators' passive resistance was very much in line with the banking sector's opinion when it came to the break-up of the *Großbanken*.[118] When the break-up of the *Großbanken* did take place, it failed to divide the *Großbanken* into separate legal entities. By doing so, it kept the major force resisting the assimilation in place.

4.5 In reverse gear (1949–1961)

As it stood in 1949, the American assimilation effort was surprisingly successful.[119] The restructuring of the banking sector was often touted as a hallmark of successful deconcentration policy by American officials.[120] Yet, the reforms were introduced via military decrees and now it was up to the recently elected German government to transform these Military decrees into democratically legitimized laws. The recently adopted constitution would play a key role in this process.

4.5.1 A new constitution

After intense discussions, a new constitution for a Federal Republic of Germany was proclaimed on the 23rd of May 1949. Since the Allies were still the occupying force, they had to approve the constitution for it to enter into force. During the drafting process, the American Military Government went to great lengths to avoid giving the German officials

[117] See Ahrens (2007, p. 169), Holtfrerich (1995, p. 415) and Horstmann (1991, pp. 96–103). It is interesting to note that the decentralization did not have any major adverse effect on the credit availability of the German economy. The contrary was often claimed by the banks in an effort to make their case. See Horstmann (1991, p. 181).

[118] Horstmann (1991, pp. 199–200) quotes an enquiry by the Office of the Director of Intelligence in the American zone amongst bankers, industrialists and bureaucrats with respect to the banking reforms just conducted, with the following remark: *"All contacted bankers are opposed to decentralization!"*.

[119] See table 4.5 on page 175 for a comparison of the original Dodge plan and its actual implementation.

[120] See for example the *Report of Conference with General Clay, Berlin, Germany*, dated 19. 12. 1948, found in NARA, RG 466, Office of General Counsel, Decartelization Division, General Subject Files 1948-55, NND: 903623, Box 5. The other 'success story' often touted was that of the industrial conglomerate I.G. Farben. For the break-up of the I.G. Farben see Borkin (1978) or Kreikamp (1977).

TABLE 4.5: **The Dodge plan and its implementation by 1949**

	Germany (1938)	**Dodge Plan**	**West-Germany (1949)**
Regulatory Institutions	Centralized	Decentralized	Decentralized[a]
Central Bank	Centralized	Decentralized	Decentralized[b]
Branching	Free	Restricted	Restricted[c]
Investment Restrictions	Universal banking	Separation of investment and deposit banks	Universal banking
Deposit Insurance	None	Not mentioned	None

[a]To the state level.
[b]Largely modeled after the Federal Reserve. See Cwik (1970) or Wandel (1980, pp. 81–82).
[c]To the state level.

the impression that the Americans were forcing a constitution upon them. To that end, the Allies had given the parliamentary council (the *Parlamentarischer Rat*) guidelines according to which the council was expected to draft the new constitution. A federal structure was one of the key characteristics the Allies requested in those guidelines.[121]

Even though the Germans were working on a new constitution behind closed doors, the Allied Military Governments made sure that they were well informed of the developments, so that they could intervene and steer the committees in the desired directions. The Allies intervened several times in the early drafts, because they perceived a lack of federalism, in particular in financial matters. They wanted the Germans to strengthen the rights of the states, and even provided the Germans with revised versions of the corresponding articles.[122] While the American Military Government intervened strongly for a decentralized fiscal arrangement that would give the states independent sources of income, it failed to intervene when it came to the responsibilities of regulating the banking sector. It was left in the field of the concurring legislation.[123] This kept the right to legislate in the hands of

[121]This was in addition to the obligatory notions of republicanism, democracy, rule of law, adherence to the fundamental human rights, etc. The Americans were federalists by nature. The French saw a federal system as a way of weakening the German central government. Indeed, this time around the French were stronger 'federalists' than even the American representatives, whereas the British did not feel strongly about this issue. See Wagner (1975, pp. XVI–XIX) and Feldkamp (1995, p. XXXII).

[122]See Feldkamp (1995, pp. XXVIII–XXIX and 120–130). The Germans wanted to maintain the constitution's flexibility. For the time being, a more decentralized arrangement was acceptable to them. But Germany was to be fully re-integrated into the European and the world economy. This, the Germans officials argued, would make a move towards a more centralized government indispensable in the long-run. See Werner (1986, pp. 352–355).

[123]For the American intervention in fiscal matters and their failure to give the state the unalienable right to regulate the banks see Feldkamp and Müller (1999, pp. XLI–XLVIII) and Feldkamp (1995, pp. 131-144). For the article of the German constitution listing all areas of the concurring legislation, including that of banking, see Bundesgesetzblatt (1949, Art. 74).

the states, unless the central government deemed it necessary to issue a uniform law for the entire country for reasons of practicality or economic unity. This implied that there was no firm constitutional barrier for the central government to eventually re-centralize the regulation of the banking sector. Furthermore, the temporary nature of the Bank deutscher Länder was also enshrined in Article 88 of the Constitution.[124]

4.5.2 HICOG replaces OMGUS

The establishment of the Federal Republic of Germany heralded the beginning of a new epoch. However, the Allies had not given Germany its full sovereignty just yet. Germany could not establish relations with other countries, her currency was not freely convertible and in many crucial areas, including banking and antitrust, her laws were still subject to approval by the Allies. These rights were exercised by the newly established Allied High Commission (also known as the High Commission for Occupied Germany).[125] The Americans wanted to make sure that the Germans would pass the relevant laws under their auspices to turn the structural reforms into permanent institutional changes. The establishment of the Federal Republic of Germany and the passage of the so-called 'occupation statute' also meant that non-defense responsibility of Germany was transferred (in the American case) from the U.S. Department of War to the Department of State. OMGUS was now replaced by the the Office of the U.S. High Commissioner for Germany (generally abbreviated as HICOG[126]). With it came important personal and structural changes. Almost none of the most senior figures of OMGUS were retained for HICOG.[127]

[124] Change in central bank matters was certainly a possibility, but not a certainty. Indeed, the entire constitution was considered to be temporary in nature. After all, a constitution for the whole German nation could only be written by a reunited Germany. Consequently, the term *Grundgesetz* (basic law') was adopted instead of *Verfassung* (constitution). See Bundesgesetzblatt (1949, Präambel and Art. 88). For a document outlining creation of the German constitution and the various amendments see the *Documents on the Creation of the German Federal Constitution*, prepared by OMGUS, dated 01.09.1949, found in NARA, RG 84, Germany: Berlin Mission, Allied Kommandatura Secretariat, Classified Files, 1945-1990, NND: 948811, Box 194.

[125] This was established in the 'Occupation statute', which entered into force on 21.09.1949. It is published in Allied High Commission for Germany (1950, pp. 5–7). For the establishment of the U.S. High Commissioner for Germany and the Allied High Commission see Lee (1951). For its relation with the German government see Plischke (1952).

[126] Strictly speaking, the correct acronym is USHCG, since HICOG referred to the entire (Allied) High Commission for Occupied Germany. However, in the American documents from that time period HICOG is generally used equivalent to USHCG.

[127] See Zink (1957, p. 49) and Lee (1951, pp. 58, 69–73). Jack Bennett, who had been financial advisor of the American military governor General Clay and a staunch proponent of the decentralization of the banking sector, returned to the United States in 1949. His successor, Shepard Morgan, did not see the need to press on further. He is quoted as saying that *"this is a period of recovery rather than reform [...] We*

Unlike OMGUS, HICOG did not even have a dedicated finance division anymore.[128]

Nevertheless, the period of transition in 1949/1950 lead to a brief impetus amongst the Americans to press for a completion of their Institutional Assimilation of the banking system before a new federal government took over and was fully functioning.[129] The unfinished break-up of the *Großbanken* was to be tackled. Also the reform of the *Girozentralen* and *Zentralkassen* and the introduction of the separation of investment and deposit banks were briefly back on the table.[130] However, it was soon realized that imposing additional decentralizing changes would cause insurmountable opposition. Not only with the German government, but also with the British Military Government, who had agreed to the decentralization only reluctantly in the first place.[131] Thus, instead of aggressively pursuing new reforms, the American Military Government shifted towards the preservation of the institutional changes. The Germans were expected to replace the military laws by democratically legitimized ones. In order to prevent re-concentration, the American

have already gone too far in endeavouring to force Germans to adopt American practices and procedures." See Horstmann (1991, p. 199).

[128] As Ahrens (2007, p. 203) points out, the policy directives to the Office of the U.S. High Commissioner did not explicitly call for any further structural changes to the banking sector. Financial affairs were now part of the Economic Division. Matters relating to the restructuring of the banking sector were henceforth handled by the decartelization and deconcentration division that was part of the Office of General Counsel. See the organizational chart of the Office of the U.S. High Commissioner printed as attachments in Lee (1951, pp. 84, 87). For a summary of the policy directives issued to the Office of the U.S. High Commissioner see the secret policy report: *HICOG Fundamentals, Authority, Policy and Responsibilities*, prepared by the Office of the Executive Secretary, HICOG, Apo 757, dated 15. March 1950, found in NARA, RG 466, Office of the Executive Secretary, General Records, 1946-1952, NND: 968095, Box 5. See also the confidential letter of Hoyt Price to the U.S. Ambassador, dated 08.03.1948 in which he lobbies for a unified economic division in HICOG, due to the lack of a unified policy in OMUGS, found in NARA, RG84, Office of the Political Advisor for Germany, Berlin, Miscellaneous Classified Records, 1948-1949, NND: 863528, box 1.

[129] The assimilation had stalled completely in the course of 1948. The main reasons for this was a British blockade paired with passive resistance at all levels on the German side. For details see Horstmann (1991, pp. 173–177).

[130] See the Military Government draft laws *Elimination of power of banks to engage in stock exchange transactions and to divest in certain securities* and *Registration of certain instruments of control of economic enterprise*, both dated 1949, the Memo by Heymann (Legal Advisor of the U.S. Decartelization Element) to March (Finance Group - Bipartite Control Office) from 31.08.1949, Subj.:*Draft Laws on Bearer Shares and Bank Participation in Stock Exchange Transactions*, the Memo by Kelleher to James from 21.08, 1950, Subj.:*Status and Problems of German Banking Reorganization*, the confidential message by Acheson of the State Department to HICOG, dated 04.12.1950, all of which were found in NARA, RG 466, Office of General Counsel, Decartelization Division, General Subject Files, 1948-55, NND: 903642, Box 1. See also the excerpt of the American directive from 29.11.1949 found in NARA, RG 466, Office of General Counsel, Decartelization Division, General Subject Files, 1945-55, NND: 903623, Box 5.

[131] See the letter by the outgoing British High Commissioner for Germany to the U.S. High Commissioner for Germany McCloy from 24.06.1950, found in NARA, RG466, Office of General Counsel, Decartelization Division, General Subject Files, 1948-55, NND: 903623, Box 5, and a position paper by the U.K. Member of the Allied Control Council, Subj.: *Decentralization of Banking - A Paper by U.K. Member*, Appendix C to FIN/P(50)1, dated 22.12.1949, found in NARA RG 84, Germany, Berlin Mission, AK Secretariat, Classified Files, 1945-1990, NND: 948806, Box 106. See also Adler (1949, pp. 339–341), Berghahn (1986, pp. 98–103) and Dickhaus (1998, pp. 163–165).

Military Government intervened numerous times in the drafting processes. Simultaneously, the Americans pursued a re-education program that was aimed at convincing the Germans policymakers and businessmen of the advantages of the American decentralized, 'anti-trust' approach to the economy.[132]

4.5.3 Removal of branching restrictions: *Großbanken* again

Given the need to codify Allied legislation into democratically legitimized law, the issue of the *Großbanken* came to the forefront almost immediately.[133] The Allies were aware of the unfinished nature of their reforms, and so were the *Großbanken*. In 1948/49 the French and the Americans had already begun drawing up plans to abolish them once and for all, while the *Großbanken* took the necessary countermeasures to prevent just that. The fact that there was a unified German government backing the *Großbanken* certainly aided their cause, and so did the return of the old banking elites from the denazification programs.[134] The *Großbanken* were also aided by the British, who had never shared the same enthusiasm for this measure as the Americans. On the contrary, they were convinced of the importance of the *Großbanken* for reviving German industry and as a consequence the (European) economy. As a result, the British outright blocked the liquidation of the remains of the large credit banks. Not only were they critical of the need for such a measure in purely economic terms, but they feared that a liquidation of these banks would jeopardize British banks' claims against them, which had been pending since a standstill agreement during the 1931 financial crisis. Consequently, Allied discussions did not yield any concrete results even though numerous drafts had been drawn up that would have liquidated the legal shells of *Großbanken*.[135] On the contrary, from then on British officials began advocating the recentralization of the German banking system.[136]

[132]See Berghahn (1986, p. 103–105) and Murach-Brand (2004, pp. 126, 137). See also the letter from Müller-Armack to the American HICOG from 12.02.1953, Subj.:*Lectures of U.S. Antitrust Experts in Germany*, found in NARA, RG466, Office of General Counsel, Decartelization Division, General Subject Files, 1948-55, NND: 903623, Box 5. In this letter he explicitly asks for American officials to lecture on the American antitrust concepts in the economics ministry as part of a larger American exchange program aimed at re-educating German government officials at all levels.

[133]This topic was also picked up by the general public. See Horstmann (1991, pp. 208–209, fn. 67–77)

[134]Many of them had been held by the Allies, since they wanted to try them for war crimes. These trials did not materialize in most cases. See Horstmann (1991, p. 177–181) for the return of the 'old elite'. Two of Chancellor Adenauer's most trusted advisors were the bankers Abs and Pferdmenges.

[135]See Adler (1949, p. 341), Ahrens (2007, p. 202), Horstmann (1991, pp. 189–217) and Loehr (1952, pp. 52–58).

[136]See Holtfrerich (1995, pp. 440–441, 445-446).

It had become hard to justify the reorganization of the banking sector. The economic revival of Germany was the priority now, so why did the Allies insist on weakening the most prestigious banks? Their role in the industrialization had, after all, become mythical.[137] If the reforms were about the efficiency of the banking system, why not apply the efficiency of a historically grown system that adapted to the local conditions? If the reforms were about decartelization and freedom, why not let the Germans choose freely?[138] Amidst growing German resistance from a centralized German government and the British government's opposition to press ahead with additional reforms, a tipping point was reached in the winter of 1949. The Americans lost not only the British as a crucial ally in this matter, but also their own drive for further decentralization. In March of 1950, the Allies officially asked the German government to come up with a proposal on how to resolve the 'legal' issues of the *Großbanken* and their subsidiaries. The initiative had gone over from the Americans to the German government and it would remain there.[139] The only thing that remained at that point in time, was the Americans' hope that German policymakers and businessmen would come to value the changes introduced to the *Großbanken*.[140]

Leading German bankers of the decentralized *Großbanken* immediately seized the opportunity and presented their own plan (the *Abs-Plan*) for partially removing the branching restrictions and thus allowing for a partial re-integration of the *Großbanken* within three seperate banking districts (North, West and South).[141] The *Abs plan* was generally welcomed amongst the federal government, business and industry.[142] A notable exception was the central bank council, which was dominated by the state central banks, who feared for their existence. Dividing Germany into three banking regions would certainly trigger calls for a reduction in the number of state central banks. And even if the number of state central banks would not be reduced. While the directorate of the BdL was in favor the plan, it clashed repeatedly with the BdL's central bank council over this matter. There

[137] This mythical status was later reflected by Gerschenkron (1962).

[138] See Loehr (1952, p. 126). For a detailed overview of the positions see also the Memo by Klopstock to Pumphrey, Subj.:*Re-centralization of German Banking*, dated 02.02.1950, found in NARA, RG 466, Office of General Counsel, Decartelization Division, General Subject Files, 1948-55, NND: 903642, Box 1.

[139] See Horstmann (1991, pp. 194, 210, 216–217).

[140] See also Loehr (1952, p. 126).

[141] See BArch B102/28179, *"Vorschlag betreffend die zukünftige Struktur der deutschen Aktienbanken"*, submitted by H.J. Abs, C. Goetz and P. Marx on 31.05.1950. A complete as well as a summary English version of the plan can be found in NARA, RG 466, Office of General Counsel, Decartelization Division, General Subject Files, 1948-55, NND: 903642, Box 1. Abs, Goetz and Marx had been key figures in *Großbanken*-matters for quite some time already. In particular Abs played the central role in staging a 'defense'. See Ahrens (2007, pp. 210–211) and Horstmann (1991, pp. 190, 204–210).

[142] See Holtfrerich (1995, pp. 446–449).

is evidence that some of the smaller states' central banks saw the the reorganization of the banking districts even as a potential trigger for a reorganization of German states altogether. The Allied High Commission did not make matters easier on the German side by releasing an opinion that it considered it sensible that the banking districts should be congruent with the State Central Banks area of operation, effectively calling for the abolition of a number of state central banks if the plan to re-centralize went ahead. It was only when the finance ministry leaked rumors to the press that the Abs plan with the three banking districts had been accepted both by the Allies and the German government. This alarmed the state central banks of the largest states, which were quick to propose to have six banking districts. This would have secured their survival, but not that of the smaller state central banks. The small-states' central banks were naturally alarmed by this development and they consequently sided with the *Großbanken* in their attempt to establish three banking districts. In return, the *Großbanken* and the Finance Ministry supported the smaller states in decoupling the recentralization of the *Großbanken* from the questions relating to the restructuring of state central bank districts and of state boundaries.[143]

The finance ministers of the three southern German states (Hesse, Württemberg-Baden and Bavaria) used this opportunity to obtain concessions.[144] After all they were reneging on federal principles. And if need be, they could delay the entire recentralization process of the *Großbanken*. If united, they could even block it with their vote in the *Bundesrat*. Hesse soon pulled out of this coalition after representatives of the banks outlined the (tax) benefits of having the German financial capital in its state. The remaining two states, Bavaria and Württemberg-Baden, consequently signalled a willingness to compromise, as their coalition could no longer block the recentralization. They demanded to have two of the *Großbankens'* southern banking districts headquarters to be based in their state capitals of Munich and Stuttgart. As a consequence of the opposition of the state central banks and the southern states, the recentralization issue dragged on over several months, before the German government finally presented a first draft to the Allies for approval.[145]

[143]See Holtfrerich (1995, pp. 439–453), Horstmann (1991, pp. 219–243) and Wolf (1998b, pp. 86–87).

[144]Interestingly, Holtfrerich (1995, p. 454) reports that the Economics Ministries of the states were in favor recentralization and even passed a resolution urging the federal government to work in this direction.

[145]See Holtfrerich (1995, pp. 454–459), Horstmann (1991, pp. 249–261) and Wolf (1998b, pp. 86–87). Horstmann (1991, p. 250) and Holtfrerich (1995, p. 454) report that it was the states in the American zones that were opposed to the recentralization in part because the Americans had placed federalist-leaning individuals in key positions such as the State Central banks. Holtfrerich (1995, p. 450) also reports that these states and some of state central banks federal sentiments were even stronger than that of the American High Commission at the time.

Approval by the Allies was still necessary, since Germany had not yet regained full legislative autonomy. The British High Commissioner was fully supportive of the German *Abs plan*. Indeed, the chief author, Hermann J. Abs had conferred with the British several times before publishing the detailed plan. Nevertheless, the German government and Abs were both aware that a complete restoration was not an option as long as the Americans had a say. For their part, the American HICOG representatives had realized that they could not avoid a partial removal of branching restrictions and re-concentration of the *Großbanken*.[146] Instead, they made an effort to introduce provisions in the German regulatory landscape, which they considered to be of importance. The number one banking practice the Americans wanted the German central government to ban was that of proxy voting. They also tried to convince the Germans of the necessity to introduce shareholder registration.[147] As the discussions dragged on, the German government was seriously concerned of an 'I.G. Farben episode'. In the summer of 1950, the Allies had issued a military law that broke-up the industrial conglomerate I.G. Farben without any prior involvement or advance notice of the German side. Now the government feared that any further delay caused by German infighting over the exact details might trigger yet another such an action by the Allies.[148]

The Branch Restriction Act, which was eventually passed by the German parliament with the approval of the Allies, introduced three banking zones as it had been proposed in the *Abs plan*. Each bank had to choose a banking zone in which to operate, and it could not maintain subsidiaries or branches in other zones.[149] The *Großbanken's* 30 offspring were allowed to merge within their respective zones as new legal entities. In order to be able to cover all three banking zones, each of the three universal bank groups would be composed

[146] For the sympathy of the British for the German cause see the Memo by Klopstock to Pumphrey, Subj.:*Re-centralization of German Banking*, dated 02.02.1950, found in NARA, RG 466, Office of General Counsel, Decartelization Division, General Subject Files, 1948-55, NND: 903642, Box 1. For an analysis from within the German Economics Ministry of the situation in the summer of 1950 see BArch B102/28179, Memo by Dr. Henckel, 1310-V/7, Subj.:*Neuorganisation der Großbanken*, dated 01.06.1950. Holtfrerich (1995, p. 454) also reports that the Korean War might have shifted American policy priorities further towards economic reconstruction rather than ensuring the strict adherence to federalism in Germany.

[147] For a presentation of the discussions taking place see Ahrens (2007, pp. 202–221), Horstmann (1991, pp. 261–286) and Loehr (1952, pp. 58–67). For archival material from the German Economic Ministry refer to BArch B102/28179.

[148] See BArch B102/28179, Memo by Henckel, Subj.:*Neuordnung der Großbanken*, dated 12.10.1950 and Memo by Kremer, Subj.:*"Vermerk über die Unterhaltung auf dem Petersberg mit den Finanzberatern der Hohen Kommissare am 8.5.1951 über das Großbankengesetz"*, dated 10.05.1951.

[149] For the Act see Bundesgesetzblatt (1952). Colloquially this act was called the *Großbankengesetz* – the law of the large (universal) banks.

of three 'subsidiaries'.[150] The 'subsidiaries' were even allowed to change their names so as to resemble the universal bank in whose tradition they stood. However, they were prohibited from owning shares of each other, and board members were prohibited to have a seat on another 'subsidiary's' board.[151] In order to obtain approval from the Allies, the German government promised to introduce safeguards to the practice of proxy voting in the corporate legislation. This was meant to keep banks from assuming too much financial power. Banks were to obtain explicit permission from their customers, if they wanted to make use of the voting rights associated with their customers' shares in other companies. Additionally, the German government had to refrain from further reforms with respect to branching restrictions and the *Großbanken* for a period of three years.[152] This provision alone shows clearly how little the Americans believed in the long-term persistence of even these 'reformed' branching restrictions. And indeed, the Branch Restriction Act of 1952 would only be a temporary stopgap on the route to the restoration of the *Großbanken*.[153] In the meantime, the 'subsidiaries' of each bank cooperated closely with each other and they even signed legally binding contracts in which they agreed on pooling their gains and losses.[154]

Sure enough, three years after the first Branch Restriction Act, Germany's occupation status was lifted and Germany regained full legislative autonomy and restricted sovereignty in 1955.[155] Not long thereafter, the decentralization in the banking sector imposed by the Allies would be largely reversed. The Branch Liberalization Act from 24. December, 1956, was indeed a major Christmas present to the *Großbanken* groups.[156] It allowed any bank to operate throughout Germany without any restrictions. This also implied that the universal bank subsidiaries could merge and they soon did. The restitution of the *Großbanken* was completed.[157]

[150]Consequently this was also called the *"3 ∗ 3 solution"*. See figure 4.3 on page 184 for the subsidiaries and figure 4.2 and table 4.6 on pages 184 and 183, respectively, for an overview of the size of the Großbanken groups.

[151]For every stock owned in the former *Großbanken*, shareholders were given one stock of each of the three new 'subsidiaries', as well as a fourth share of a 'trunk' institute, which represented a claim on assets held in East Germany and elsewhere abroad. For details see Ahrens (2007, pp. 245-248).

[152]See Horstmann (1991, pp. 283–284) and Loehr (1952, p. 67).

[153]By 1952 there was already a consensus amongst the German government, parliament and banking that complete recentralization of the *Großbanken* was only a matter of time. See Ahrens (2007, p. 220).

[154]For an example of such a pooling contract see that of Gruppe Deutsche Bank (1955, p. 6).

[155]Allied soldiers remained stationed in Germany and she was required to join the North Atlantic Treaty Organization. Full and unrestricted sovereignty would only be restored in 1991 after reunification had taken place and the "Two plus Four Agreements" became effective.

[156]See Bundesgesetzblatt (1956).

[157]Ahrens (2007, pp. 124–125) points out that the National Socialists' arization process of the 1930s had a longer lasting impact on the personnel continuity of the large credit banks than the denazification and

Table 4.6: **The *Großbanken groups* in international perspective in 1950/51**

	Balance sheet size (in mio. US$)	
Bank	**1950/51**	**1930/31**
Bank of America (USA)	7,022	1,061
The National City Bank of NY (USA)	5,580	1,973
The Chase National Bank (USA)	5,228	2,215
Barclays Bank (UK)	5,126	2,207
Midland Bank (UK)	4,030	2,085
Lloyds Bank (UK)	3,608	2,050
Guaranty Trust Company of New York (USA)	3,095	1,863
Continental Illinois Bank and Trust Company (USA)	2,554	1,129
Royal Bank of Canada (CAN)	2,249	852
Bank of Montreal (CAN)	2,004	786
Canadian Bank of Commerce (CAN)	1,606	686
Nederlandsche Bank (NL)	1,578	372
Credit Lyonnais (F)	878	596
Deutsche Bank Group (D)	842	1,174
Philadelphia National Bank (USA)	823	456
Société Génerale (F)	744	577
Schweizerischer Bankverein (CH)	618	317
Banca Commerciale Italiana (ITA)	601	957
Dresdner Bank Group (D)	525	603
Schweizerische Kreditanstalt (CH)	524	352
Comptoir National D'Escompte de Paris (F)	511	408
Züricher Kantonalbank (CH)	470	233
Banco di Roma (ITA)	464	227
Banco di Napoli (ITA)	442	260
Credito Italiano (ITA)	408	487
Nederlandsche Handel-Maatschappij (NL)	398	266
Mitsubishi Bank (JAP)	388	376
Mitsui Bank (JAP)	364	431
Commerzbank Group (D)	347	430
Amsterdamsche Bank (NL)	295	430
Rheinische Girozentrale und Provinzialbank (D)	271	226
Schweizerische Volksbank (CH)	254	329
Bayerische Hypotheken- und Wechselbank (D)	250	247
Rotterdamsche Bank (NL)	250	165
Banque Cantonale de Berne (CH)	172	112
Banque de Paris et des Pays - Bas (F)	169	166
Hollandsche Bank - Unie N.V. (NL)	117	32
Solothurner Kantonalbank (CH)	90	56

Note that in 1950/51 the *Großbanken* groups did not officially operate as groups yet. *Sources: own work based on data from Thomas Skinner & Co. (1931, 1951, pp. 505–1476 & pp. 19–868). German bank data for 1950/51 is from BArch B102/28179, "Abschrift: Bilanzsummen der Nachfolgeinstitute der Großbanken nach den Bastameldungen per 30. September 1951" and "Abschrift: Bilanzsummen der größten Banken in Nordrhein-Westfalen und Bayern". Exchange rates were used from Board of Governors of the Federal Reserve System (1943, 1976, pp. 663–682 & pp. 1035–1047).*

decentralization efforts of the Allies. Of the 13 members on the board of Dresdner Bank in 1957, merely one of them had joined the bank after the Second World War.

FIGURE 4.2: **The *Großbanken Groups'* balance sheet sizes by region in 1951 (in mio. DM)**

Region	**Deutsche Bank Group**	**Dresdner Bank Group**	**Commerzbank Group**
Western banking zone	**1,458**	**780**	**775**
Nordrhein-Westfalen	1,458	780	775
Northern banking zone	**693**	**604**	**389**
Hamburg	386	372	192
Bremen	114	90	28
Niedersachsen	193	126	139
Schleswig-Holstein	–	16	30
Southern banking zone	**1,382**	**818**	**291**
Hessen	322	375	127
Bayern	244	173	46
Württemberg-Baden	439	159	96
Württemberg-Hohenzollern	67	10	–
Baden	145	28	–
Rheinland-Pfalz	165	73	22
Total	*3,533*	*2,202*	*1,455*

Note: the banking zones did not yet exist at this point in time and thus the *Großbanken Groups* are fictional. *Sources: BArch B102/28179, "Abschrift: Bilanzsummen der Nachfolgeinstitute der Großbanken nach den Bastameldungen per 30. September 1951".*

FIGURE 4.3: **When 30 became 9 in 1952**

Deutsche Bank Group	**Dresdner Bank Group**	**Commerzbank Group**
Rheinisch Westfählische Bank, Düsseldorf	Rhein-Ruhr-Bank, Düsseldorf	Bankverein Westdeutschland, Düsseldorf
Süddeutsche Bank, München	Rhein-Main-Bank, Frankfurt	Commerz- und Disconto-Bank, Hamburg
Norddeutsche Bank, Hamburg	Hamburger Kreditbank, Hamburg	Commerz- und Credit-Bank, Frankfurt

The *3 ∗ 3 solution* that resulted from the Branch Restriction Act of 1952 (also known as *Großbankengesetz*). *Sources: Ahrens (2007, pp. 238, 241), Gruppe Deutsche Bank (1955, p. 6) and Wolf (1995, pp. 22-23).*

4.5.4 From Bank deutscher Länder to Bundesbank

Article 88 of the German constitution required the government to pass a new law for a *Bundesbank*, in order to put the central bank on a democratically legitimized footing.[158] It is easy to infer from this that the Germans politicians would have grabbed this opportunity to shed themselves of the American 'dictate' and resurrect the *Reichsbank*. However, the process was not straight forward. The Bundesbank Act that was passed in 1957 did restore several of the characteristics of the *Reichsbank*, but not all of them. Furthermore, the path towards a new Bundesbank Act resembled a serpentine with several exits, each of which would have led to a different Bundesbank Act. Over the 7 years of the deliberation process a total of 25 official drafts[159] were put forward. Proposals ranged from one spectrum to the other: from simply adopting the existing *Bank deutscher Länder* as the new *Bundesbank*, to a reinstatement of the *Reichsbank*.[160] During these negotiations the Germans debated vigorously to what extend to roll back the changes imposed by the American occupiers. Two points were the main focus of these discussions. One was the extent to which the German government would control the central bank. The other was the organizational structure of the central bank – whether to maintain the decentralized system or whether to revert to a centralized approach.[161]

In the first years of the Federal Republic of Germany, the Bundesbank Act was drawn up under the auspices of the Federal Government's Finance Ministry. The Ministry, under the guidance of federalist Minister Hans Schäffer, had a favorable view of the decentralized organization of the BdL-System.[162] However, the Finance Ministry wanted to give the federal government direct control over the future Bundesbank, in order to be able to force it to finance job creation programmes and to prevent it from counteracting the governments expansionary fiscal policy by tightening monetary policy. He wanted to avoid a state within a state In this he was backed by Chancellor Adenauer as well as a number of parties in the *Bundestag*, the Christian Social Union (CSU), the Socialdemocratic Party (SPD) as

[158]See Bundesgesetzblatt (1949, Artikel 88).
[159]See Hentschel (1988a, p. 10).
[160]For a comparison of the most important drafts between 1952 and 1957 see Deutsche Bundesbank (1988, p. 195).
[161]See Deutsche Bundesbank (1988, Vorwort), Hentschel (1988a, p. 2), Stern (1999, pp. 112–113) and Wolf (1998a, p. 120). Other important, but less controversial issues were with respect to the legal form and the monetary tools available to the Bundesbank.
[162]Indeed the BdL System had performed well in its first years of existence and even built a solid reputation inside and outside of Germany. See Dickhaus (1998, p. 179). For Schäffer's federalist tendencies see for example Hentschel (1988a, p. 14).

Table 4.7: **Conceptual overview of the different interest groups with respect to the Bundesbank Act in1950**

	Decentralized Structure	**Centralized Structure**
Direct government influence	Schäffer (Finance Ministry), Adenauer (Chancellor), CDU ('Southern Group'), CSU, SPD	CDU ('Northern Group'), DP
Central Bank Independence	BdL, *Bundesrat*	Ludwig Erhard (Economics Ministry), FDP

Note: The positions shown here are conceptual in nature. The actual positions are not necessarily as clear cut and indeed more nuanced and did shift in the subsequent years. *Source: Own elaboration based on information from Berger and Haan (1999, pp. 23–24), Deutsche Bundesbank (1988) and Hentschel (1988a, pp. 10–16).*

well as numerous members of the CDU.[163] Adenauer and Schäffer even thought about assigning the federal government half of the future Bundesbank's share capital (and thus seignorage profits), and to relocate the future Bundesbank from Frankfurt to Cologne, just next to Bonn, the capital.[164]

Their position was vigorously opposed by those that either favored the centralization of the central bank, such as the Economics Ministry under Ludwig Erhard and the Free Democratic Party (FDP), or those that attempted to maintain the central bank's independence from the federal government, such as the BdL itself and the German states. Erhard also wanted to keep the Bundesbank nominally independent. He advocated for more subtle measures to influence the Bundesbank, such as the nomination of its directors, rather than outright government ordinances as Schäffer suggested.[165] Within the BdL itself, the president of the directorate, Vocke, supported Erhard in his drive for greater centralization of the central banks' structure. However he was outvoted by the presidents of the state central banks who dominated decision making within the BdL-System.[166] The constitution itself contained no restrictions as to the structure or the independence of the future Bundesbank. Consequently any of these arrangements was legally feasible.[167]

[163]CDU delegates who had constituencies in the 'northern' states supported this line fully, whereas those who had constitutencies in the 'southern' states tended to prefer a decentralized structure of the central bank.

[164]See Berger and Haan (1999, pp. 23–25) and Hentschel (1988a, pp. 10–12). The question whether the Bundesbank was to have its headquarters in Cologne resurfaced in 1956 again. See Deutsche Bundesbank (1988, pp. 133–136).

[165]See Hentschel (1988a, pp. 11; 14).

[166]See Vocke's Letter to Minister Erhard, Subj.: "*Zentralbanksystem künftigen Problemen nicht gewachsen*" from 12.08.1950, reprinted in Deutsche Bundesbank (1988, p. 165). See also Hentschel (1988a, pp. 11–15).

[167]See Bundesgesetzblatt (1949, Artikel 88).

In the fall of 1950, it seemed as if the Finance Ministry's position would prevail and a corresponding Bundesbank Act could be passed by the lower house of parliament, the *Bundestag*.[168] However, members of the Free Democratic Party (FDP) and the German Party (Deutsche Partei, DP), which formed part of the ruling coalition between the CDU/CSU, FPD and the Deutsche Partei (DP), came out strongly in favor of a centralized structure for the Bundesbank. Moreover, they began questioning the constitutionality of the BdL system. In particular its decentralized nature and the lack of political legitimization of its actions was critized. Additionally, Erhard (and Justice Minister Dehler) also came out strongly in favor of the centralization once more and also voiced constitutional doubts.[169] Shortly thereafter, the Allied High Commission announced that it wanted to renounce its rights in the area of currency and money, under the precondition that a German law was passed that compensated for the discontinuation of the Allied Banking Commission.[170] Minister Schäffer immediately tried to seize the opportunity to install the federal government in place of the Allied Banking Commission, giving it the power to issue direct guidances to the BdL-system and to veto any of its policies. This sneak-attack on the independence of the BdL-System was resisted successfully by the Economics Ministry and especially the BdL itself. Schäffer was forced to compromise and instead the German parliament was asked by the government to pass a provisional law that stipulated that the BdL should merely support the federal government in its general economic policy. The Allied Banking Commission's veto power was reduced to a suspensive veto that gave the federal government the possibility to suspend BdL policy decisions for a 8 days. Thus, the Bundesbank's independence from the German government was kept largely intact. However, in exchange for this independence, 20% of the bank's profits in 1951 and 1952 was allotted to the federal government.[171] From that moment on, the Allies had renounced their privileges to actively shape this particular legislative process, not that they had interfered much in the first place. Indeed, more than anything else this legislative process was a constitutional struggle between federalists and centralists.

[168]Whether the mere passage in the *Bundestag* sufficed for the Bundesbank Act was unclear. Schäffer argued that no consent of the upper house of parliament, the *Bundesrat*, was needed in the case of the Bundesbank Act. The *Bundesrat* contested this interpretation of the constitution. In any case, if the *Bundestag* have passed the Bundesbank Act without the consent of the *Bundesrat*, it is certain that the states would have launched a constitutional challenge.

[169]See Hentschel (1988a, pp. 12–13, 19). See also the overview of the different interest groups in 1950 in table 4.7 on page 186.

[170]The BdL's economic policies had been subject to the approval of the Allied Banking Commission.

[171]See Berger and Haan (1999, p. 24), Berger (1997, p. 435), Hentschel (1988a, pp. 17–18) and Marsh (1992, pp. 164–167).

The attempts by Chancellor Adenauer to increase the governments influence over the Bundesbank weakened over the next years. This can be attributed to both Erhard's and the BdL's success in winning the media's and thus public's opinion, which insulated them from further government attempts to influence the Bundesbank.[172] But the struggle over the degree of federalism continued as before. When the competence for money and credit was transferred from the Finance Ministry to the Economics Ministry in the spring of 1952, the Finance Ministry was not prepared to give up just yet. Consequently, both ministries published separate drafts for a Bundesbank Act, either of which failed to rally the unanimous support of the cabinet. While the Finance Ministry's draft stipulated the continued decentralization, the Economics Ministry's draft would have centralized the central bank. In November of 1952, Chancellor Adenauer grew impatient with the inability of his cabinet, and in particular Erhard and Schäffer, to reach a consensus. He wanted to pass the Bundesbank Act before the end of the legislative period in 1953. Consequently, Adenauer decided to forward the Finance Ministry's bill – which he personally favored – to the *Bundesrat* for parliamentary consultation, where it was received favorably. Thus, once more it seemed as if the Finance Ministry was about to reach its goal to keep the decentralized BdL-structure in place, albeit with more direct government influence on the central bank. However, in the lower house of parliament, the *Bundestag*, the Finance Ministry's bill faced the stiff opposition from the centralists in the FDP, which presented Erhard's draft as a counter proposal to the Finance Ministry's bill. They could also count on the SPD, which had changed course and now supported the centralization. The bills were almost identical in their technical details such as the scope of monetary tools they assigned to the central bank. The major difference was of course the future structure of the central bank. In a number of parliamentary sessions both bills were discussed, but no stable majority could be found for either a central or a decentral structure of the Bundesbank. As a consequence, the passage of a new Bundesbank Act was deferred to the next legislative period.[173]

In the following legislative period, the Economics Ministry under Ludwig Erhard was

[172]See Berger and Haan (1999, pp. 25, 27, 35–36).

[173]See Hentschel (1988a, pp. 21-31). In the outgoing legislative period, the FDP had also called upon the constitutional court to challenge the *Bundesrat's* opinion that it had to consent to the future Bundesbank Act and that no such act could be passed against it approval. The FDP believed that the constitution gave the *Bundesrat* no such veto power. In July of 1953, the constitutional court declared the challenge invalid, as it could only rule on legislative proceedings that had led to actual laws, but that it could not rule on bills that parliament may intend to pass.

solely put in charge with the work on a new Bundesbank Act. However, ministerial work on the act began to pick up steam only towards the end of 1955. Neither Erhard nor Adenauer wanted to force this issue early on in the parliamentary period. This gave the Erhard and the government more time to form a consensus. Additionally Erhard spent much of his time with the passage of an Antitrust Act, which was to be a cornerstone of his social market economy.[174] In 1955 and 1956 Adenauer once more tried to challenge the independence of the central bank when the BdL tightened monetary policy and criticized Adenauer's plan to expand fiscal policy. The expenditure was meant to buy Adenauer favors with the electorate prior to the next election in 1957. Intriguingly, the BdL was openly supported by Economic Minister Erhard, who was worried about inflation, and Finance Minister Schäffer, who preferred to use the funds for German rearmament. Together the two Ministers drew up a joint stabilization plan for the budget. Adenauer reacted strongly by attacking both his ministers and the BdL, and vowing to "discipline" them. The reaction by the public media outlets, as well as financial and small business interest groups was to come out heavily in support of the BdL's independence and the stabilization plan of the Erhard and Schäffer. In turn, Adenauer had to acquiesce and accepted both the central bank's independence and the stabilization plan. Adenauer's silver lining in this episode was that he could subsequently shift responsibility for the relatively tight monetary and fiscal policy on the BdL and his ministers, securing him another election victory.[175]

With the issue of the independence of the future Bundesbank settled, the only controverisal issue that remained was its organizational structure. It had already been difficult for the Economics Ministry to obtain a consensus in cabinet, especially since Schäffer and the BdL, continued their opposition to a centralized arrangement.[176] Erhard had been instructed by Adenauer to find a common ground with both, before forwarding a bill to parliament. However, Schäffer attempted to delay the reform, just as Erhard had done back in 1953, whereas the BdL put forward their own proposal, which amounted to a two-tier system with some central elements. While this was supported by Schäffer, it was rejected by the Economics Ministry as the decentral elements outweighed the central ones.

[174] See Hentschel (1988b, pp. 80–83, 87).

[175] For this episode see Berger and Haan (1999, pp. 25–27), Deutsche Bundesbank (1988, p. 116), Hentschel (1988b, p. 95), Kitterer (1999, pp. 168–172) and Stern (1999, p. 114).

[176] Schäffer also played a key role, since a centralized solution meant significant fiscal burdens for the federal government. During the currency reform of 1948, the state central banks had been allocated equalization claims by the state governments amounting to DM8.7 billion. If the state central banks were converted into federal government institutions, it was expected that the federal government would also take over these liabilities from the states. See Häuser (1998, pp. 48–51) and Hentschel (1988b, p. 97).

Both Adenauer and especially Erhard began to press for action to ensure the passage of the Bundesbank Act before the end of the legislative period. This insistence of Adenauer and Erhard seems to have caused the BdL to accept a compromise offered by the Economics Ministry that foresaw a centralized structure, but with decentral elements. It also guaranteed the Bundesbank's independence. At last, a bill was agreed upon in the fall of 1956, which was forwarded to the *Bundesrat*.[177]

Whereas there was little disagreement about material questions such as the scope of the Bundesbank operations, the *Bundesrat* outright opposed the central bank structure outlined in the government's bill. Furthermore the *Bundesrat* made it clear that it believed that any change to the BdL's structure would require its approval and that it would not hesitate to launch a constitutional challenge if need be. After all, the states' administrative rights were being affected by such a move. The upper house of parliament proposed a number of changes that made the bill much more similar to the structure outline by Finance Minister Schäffer's unsuccessful bill from 1953. The cabinet in turn dismissed the proposals by the *Bundesrat* and it also denied that the Bundesbank Act needed approval by *Bundesrat*. It consequently forwarded the bill, as well as the *Bundestag's* opinion and the government's reply to the opinion, to the *Bundestag*. There the bill encountered the opposition of the federalist CSU, which had prepared an alternative bill almost identical to the demands of the *Bundesrat*. The rest of the lower house of parlament was also largely undecided. It was then the task of the *Bundestag's* Committee for Money and Credit to act as a mediating forum between the government, both houses of parliament and the BdL. But it was clear that neither of the two organizational proposals, the government's or the CSU's, could be passed as is. One compromise by the commission's chairman, Scharnberg, found the necessary majorities in both houses of parliament.[178]

In the summer of 1957 the Bank deutscher Länder was finally replaced by the Bundesbank. Even the states voted in favor of the Bundesbank Act and no constitutional challenge was brought forward. The buildings, assets, and personnel of the BdL became part of the Bundesbank. To some extent, the federal structure was maintained as the state

[177] See Hentschel (1988b, pp. 80–97, 99).

[178] It is noteworthy that the BdL opposed the compromise and instead proposed once more its two tier system with central elements. It also urged to postpone the Bundesbank Act for the next legislative period. Ironically, this BdL opposition may have played a role in nudging the other actors towards accepting the compromise. See Deutsche Bundesbank (1988, p. 191–194) and Hentschel (1988b, pp. 87–111). See Deutsche Bundesbank (1988, p. 195) for an overview of the key differences of the main proposals throughout the legislative process.

central banks continued to exist in name. However, they were degraded to the status of branches and they no longer owned the central bank. As compensation, the state central banks were granted the responsibility to engage with banks only operating in parts of the country as well as with the local authorities. The center was responsible for banks that operated nationally, for operations involving the federal government, for foreign exchange dealings and for open market operations. The center could not issue orders to the state central banks either, merely guidelines. Henceforth, the central government owned the central bank, which gave it the power to appoint the members of the directorate.[179] In turn, the Bundesbank was to support the general economic policies of the government. But other than that the Bundesbank was independent in its policies. The central bank council consisted in equal numbers of members from the directorate and the state central banks.[180] Thus, the American decentralization efforts were rolled back substantially and some of the old *Reichsbank* privileges were introduced as well, but only after 7 years of intense parliamentary negotiations between the states, the parliament, the BdL and the central government.

4.5.5 The (re-)birth of the Credit Act of 1961

The path towards a new Credit Act would take more than 13 years. Its history finds an important parallel in that of the Bundesbank Act of 1957: both legislative processes were characterized by a fierce federalist struggle between the German federal government and the states.[181]

The Allied changes to the supervisory institutions were introduced in a piecemeal manner. This created a situation of legal uncertainty. The Allies had also refrained from passing their own military law outlining a new credit act. Consequently, the Credit Act of 1934 (in its amended form of 1939 or 1944) was still the primary source of legislation for the regulation of the banking sector. As a consequence of the decentralization of the

[179] Although this seems to have had almost no influence on the independence of the Bundesbank as Berger1997 points out. Indeed, the Bundesbank came to be known for being a particularly independent central bank.

[180] See Bundesgesetzblatt (1957b) for the legislation. See also Hentschel (1988b, pp. 113–114), Wolf (1998a, pp. 120–123). See Marsh (1992, pp. 20–22) for the personnel continuity between the Third Reich and the senior levels of the Bundesbank. And last but not least see Deutsche Bundesbank (1988, p. 265) for an excellent overview of the differences between the BdL System and the Bundesbank, as well as the initiators the different proposals.

[181] This subsection is based on Chapter 3 of this thesis.

regulatory structures, banking regulations were not applied uniformly throughout the German states.[182] In 1948, the American Military Government began pushing the Germans towards drafting a new Credit Act. One that would replace the old act and restore legal certainty. The American Military Government wanted the Germans to adopt a two-tier regulatory scheme, where the government was in charge of policing the banking sector and where the central bank was no longer directly involved in the supervision of the banking sector and instead focused primarily on monetary policy.

Work on a new Credit Act began under the auspices of the BdL in corporation with the Special Committee for Banking Regulation, which was a body founded in 1948 by the German states to harmonize their regulatory practices. The first drafts were prepared by early 1950. These incorporated the changes introduced by the Allies: the decentralization of regulation, the transfer of competence to the Ministries of Finance and the dissociation of the central bank in regulatory matters. A final draft of the Credit Act was forwarded by the working group to the Ministry of Finance in 1951.

At this time, the Ministry of Finance was engulfed in a struggle for subject-matter competence with the Ministry of Economics. The Ministry of Economics under Ludwig Erhard was trying to bring back the competences for Money and Credit to its Ministry, where traditionally it had always been been. The struggle lasted for almost three years (1949-1952). Eventually, subject-matter competence did indeed return to the Ministry of Economics. As a consequence of the transfer, work on a new Credit Act began from scratch in 1953 within the Ministry of Economics. The 1934 Credit Act (in its amended form from 1939) was taken as the starting point, rather than the draft prepared by the Bank deutscher Länder. In the following years there were severe internal disagreements within the Economics Ministry, whether the banking sector should be subjected to competitive pressures or not. Whereas one division, which represented Minister Erhard's preferences, argued for virtually free competition in the banking sector, another division, which was formally in charge of drafting the Credit Act and which was in close contact with the banking associations, advocated to maintain the banking sector cartelized. There was, however, unanimity over the goal to recentralize banking regulation eventually. In 1957, just before the end of the legislative period, the Economics Ministry attempted to centralize the regulatory institutions with a brief amendment to the Credit Act. This attempt failed

[182]The Credit Act of 1961 eventually had to revoke 35 laws and decrees passed both before and after the Second World War, in order to re-establish regulatory homogeneity.

as both the states and the BdL resisted the centralization. Not only was the bill delayed in parliament by the states, but it also became clear that the Economics Ministry would not be able to rally the necessary supermajority in the lower house of parliament, to override a potential veto by the states in the upper house of parliament. Consequently, the amendment was not voted upon before the legislative period came to an end in 1957.

It was only after the passage of the Bundesbank Act and the German Antitrust Act in the summer of 1957 that the first official draft of the Credit Act made available to the public in early 1958. This draft took another three years to make its way through the German parliament. On its way it encountered stiff resistance from the German states. Just like the states in the U.S., the German states were not prepared to give up their regulatory privileges either. The federal government and the lower house of parliament supported the law. Crucially, the Economics Ministry was able to obtain the support of the central bank, which had significant political influence and which had helped to defeat a previous attempt to recentralize the regulation of the banking sector. Eventually, after several attempts by the states to derail the project, the Credit Act was passed by the *Bundestag*, only to be rejected almost unanimously by the *Bundesrat*. However, this rejection was in turn overruled by the *Bundestag* with near unanimity. The conflict between the states and the central government continued in constitutional court. The states argued that the transfer of power from the states to the central government was illegal, since such a measure required the consent of the *Bundesrat*. The constitutional court dismissed the case referring to the German constitution, which had explicitly granted the central government to powers to unify regulation of the banking sector.

The Credit Act of 1961 looked strikingly similar to the Credit Act of 1934. Almost all regulatory elements found in the 1934 Credit Act, could be found in the Credit Act of 1961. A few elements had been added, a few had been subtracted, others had merely changed in scope. The most important characteristics were the same, however: a *centralized* supervisory authority for virtually the *entire* banking sector[183] with *extensive* powers, in particular that to impose an interest rate cartel. The only significant changes were twofold. First, the central bank was less involved in regulatory affairs than it had been in the 1930s. This was in line with the original American demands for the banking system, but are attributable not to American intervention, but to the Bundesbank's reluctance to

[183] Again like in 1934, with the exception of the mortgage banks.

accept a greater role in regulatory affairs. And Second, the regulatory agency could no longer restrict entry to the banking sector or branching on the grounds of economic necessity. This was because of a court ruling in 1958 that referred to the constitutional clause that allowed businesses to freely chose their trade. By restricting entry to the sector, the government was infringing on this right.

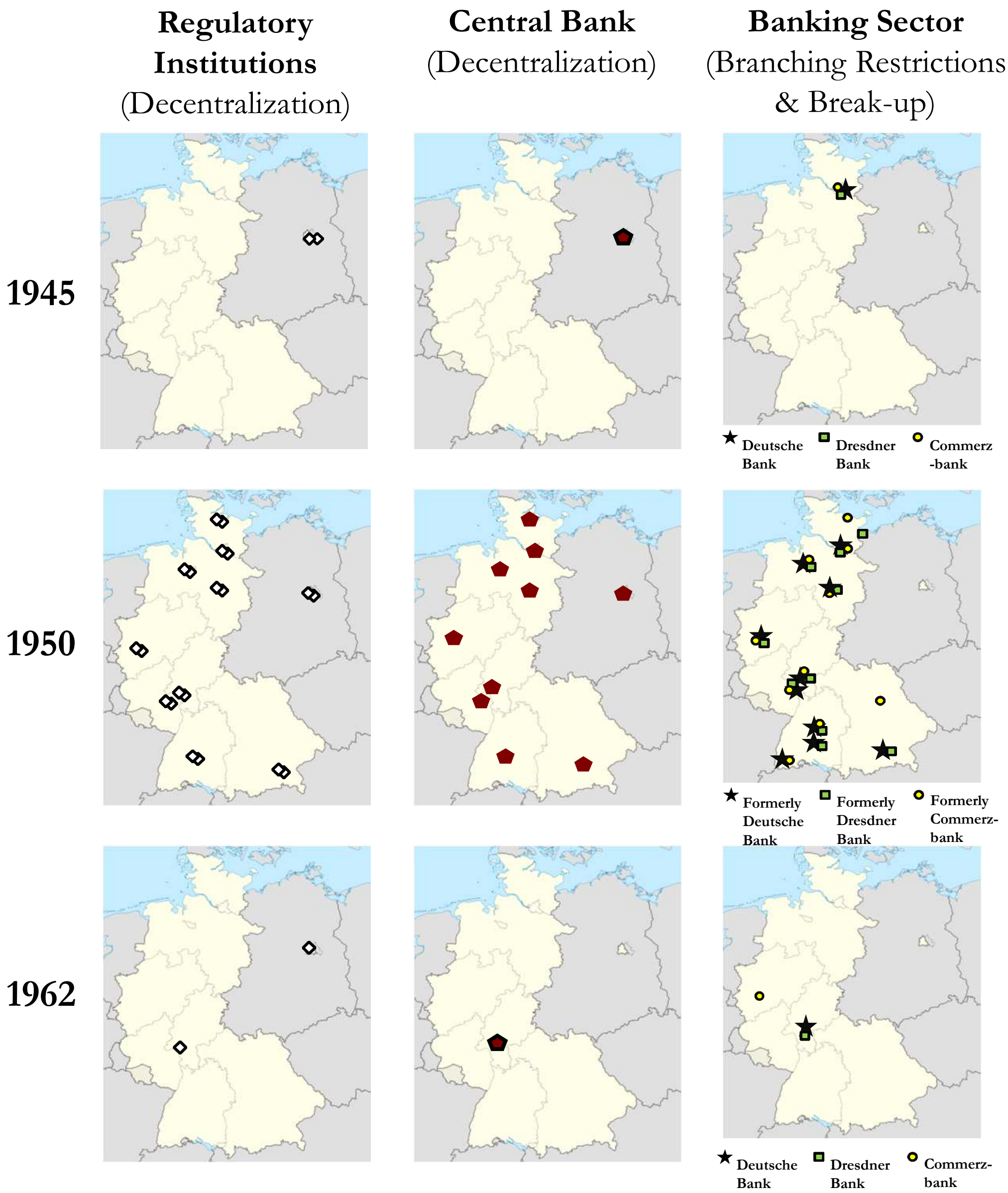
The reason why the two Credit Acts looked so similar is because the Economics Ministry primary objective was to recentralize control over the banking sector. And since it was clear that the states would reject any such proposal, the Economics Ministry had to secure a supermajority in the *Bundestag* that could overrule a veto by the *Bundesrat*. And the surest way to obtain the necessary supermajority was to return to the provisions of the Credit Act of 1934, and to refrain from implementing innovative changes, such as introducing competitive pressures into the banking system, until the recentralization of control over the banking sector had taken place and a supermajority was no longer necessary.

4.6 Conclusion

The Americans tried to transplant their ideological principles of decentralization and antitrust into a banking system that was generally characterized by just the opposite; centralization and cartelization had dominated the German banking landscape prior to the Second World War. Germany's largest and most iconic banks were broken down into much smaller units. This was flanked with a new regulatory approach, which introduced branching restrictions and a degree of regulatory decentralization previously unknown in Germany. In a major break with German administrative tradition, the responsibility for the banking sector was transferred from the Ministries of the Economy to the Finance Ministries on both a federal and central level. Furthermore, a central bank was established that was similar to American Federal Reserve System.

Despite being able to introduce major changes to the banking system by 1950, the Americans' ambitious plan largely failed in the end. The mark left on the large credit banks by the American intervention is small. At the end of the 1950s the *Großbanken* reemerged as the branching restrictions were abolished. The Bundesbank also shed itself of much of the American ballast. Instead it reintroduced many tried and tested *Reichsbank* structures. Remarkably, the Bundesbank was able to maintain its independence from

Figure 4.4: **The Failed Institutional Assimilation**



A schematic overview of the changes imposed by the Allies on the regulatory institutions, the central bank and the banking sector, and their subsequent reversal. Note: A map of the West-German borders between 1952–55 has been used for all these years in order to reduce complexity. *Source: own elaboration based on a map by Wikimedia Commons (2011).*

German government influence. Last but not least, the Credit Act of 1961 turned out to be the younger brother of the Credit Act of 1934. Thus, much of the American mark disappeared barely a decade after it had been made. Indeed, the most lasting impact the Americans had on the German banking system was less in the form of outright intervention in the banking or industrial sector, but more an indirect one via the German constitution.

Why did the Institutional Assimilation fail? Of course it is easy to infer just from the results that Germans were universally opposed to all institutional changes imposed by the Americans, and that the decentralization effectively rises and falls with the influence of the Americans. However, such an explanation is not satisfactory, since it does not reflect the actual events, in particular the vigorous constitutional conflict that took place between the states and the federal government. In the case of the branching restrictions and the decentralization of the *Großbanken*, initially the states opposed the recentralization because they correctly feared that it could serve as a trigger for greater centralization of the central bank. Some city-states even feared that it could lead to their disappearance altogether. After the states secured the federal government's assurance that such questions would not be treated in parallel with the recentralization of the *Großbanken*, the southern states tried to obtain concessions for their agreement, which they did in the form of tax income from the headquarters of the regionally re-merged *Großbanken* based in their respective states' capitals. Matters were even more complex with the institutional changes to the central bank and the regulatory structures. The institutional outcomes of these struggles were not evident ex ante at all. By changing the institutional framework, the Americans had also changed the power balance between the states and the federal government. Subsequently the states wrangled to defend their newly gained responsibilities, whereas the federal government attempt to retake them.

Four factors contributed to the failure of the assimilation, one of which was easy to overlook, but it turned out to be crucial. The first shortcoming was the delay and incomplete nature of the reforms. As with any reform, time tends to be on the side of the incumbent rules, regulations or practices. The Americans were aware of this. Yet, they still tried to reach as broad a compromise as possible. First, they hoped for a compromise involving all four of the Allies, then for action taken by the Germans themselves and finally they tried to obtain an agreement with the remaining three western Allies. While intending to reach a cooperative solution, precious momentum was lost. It was only after $1\frac{1}{2}$ years of virtual stalemate that the Americans decided to press ahead with the reforms, and, sure enough, the French soon followed and so did the British. This delay would not have caused much of a problem by itself, especially when it came to decentralization of the central bank and the regulatory institutions. However, the delay paired with the botched break-up of the *Großbanken* and the introduction of branching restrictions were a major headache for the Allies. The Americans had failed to eliminate the most vigorous opponents of their assimilation effort in the form of the *Großbanken*. The delay in implementing the assimilation allowed the *Großbanken* to recover from the initial chaos after the surrender and to stage a more structured response. Ironically, it seems likely that the Americans seem to have overestimated the impact of the *Großbanken* on the (war) economy, while dramatically underestimating their political impact. Had they not, then the break-up of the *Großbanken* might have succeeded.

The second shortcoming was the fact that the Americans had to pass all of their reforms as a 'military law' – effectively an order. Proper democratically legitimized legislation was to follow by the German legislators at a later stage. It was generally understood that the imposed institutional changes were 'temporary' in nature. Temporary not in the sense that they would be rolled back in the near future, but temporary in the sense that the Germans would eventually democratically decide on their own, on which system to adopt. Consequently, the use of military decrees made it harder for the status quo bias to perform its 'magic'.

A third important factor in the failure of the Institutional Assimilation was a policy reversal that took place within the American administration as OMGUS was replaced by HICOG, which exchanged much of the key personnel. Not only did the Americans switch from an active to a passive role, focussing instead on re-educating the German businessmen and policymakers. But, by the time the Federal Republic of Germany had been set up, many of the new American officials on the ground were less firm in their convictions about the optimality of the American banking system and consequently about the desirability of imposing those reforms on Germany in the first place. This view was certainly strengthened by strong British opposition to any further institutional changes once the federal Republic of Germany had been created.

None of the preceding three factors are sufficient. Americans failed to implant the necessary safeguards in the German constitution that prevented recentralization. This is what made all the difference. The German constitution, too, was formulated under American supervision. Its constraints set the political and economic playing field. However, the American officials seem to have failed to recognize the importance of having sufficiently strong states' rights included, if the American institutions were supposed to survive in the regular democratic process. As a matter of fact, the German states fought long and hard with the federal government to retain the privileges the Americans had given to them.

The legislative process over the reform of the central bank law was long and drawn out. At one point it even seemed that the American Federal Reserve model, that the BdL had inherited, might find a democratic majority. In the case of the regulatory institutions, the states fought even harder to retain their supervisory rights. And here at one point it too seemed like the American model might be adopted. In the end, the states could not retain these privileges either, as the constitutional court ruled in favor of the central government, who went ahead and stripped control over banking regulation from the states. The constitution allowed the Germans to centralize their banking system much more than the Americans had initially anticipated.

This historical episode can tell us something not only about German banking regulation, but also American regulatory history. If one assumes that there are two regulatory systems to chose from: the American decentralized regulatory system and the German centralized system with. Let it be assumed that the German banking system with centralized regulatory supervision is superior to the other.[184] Then the main question is, of course, why did this 'superior' arrangement not materialize in the United States? The answer to this question is likely to be found with the states' constitutional right to charter banks, which kept the United States trapped in a suboptimal equilibrium.[185] Now, is there a way to test such a hypothesis? One would have to find the identifying variance, i.e. one needs to find a country with a constitution that did not contain the same states' rights as the American constitution, and where the American system was introduced exogenously. In such a case one would predict that the American system would not prevail in the long-run, i.e. that there would be a switch from a 'bad' equilibrium to a 'good' equilibrium.

The German case after World War II was just such a scenario. The Americans project their regulatory system upon the German one. If one looks at the German constitution from 1949 then one can see that it was clearly federal as well. However, it also included the banking matters as part of the concurrent legislative powers. Unlike the United States, the central government was able to claim exclusive jurisdiction over banking matters, if it deemed it vital, which it eventually did. Similar to the United States, the German states fought the centralization efforts in the banking sector vigorously. Only that this time, unlike in the United States, it was in vain. It was the relatively more centralized

[184] This is merely a speculative assumption for the sake of this argument, which would have to be tested more thoroughly. However, as financial markets become more integrated, the tendency of regulatory structures worldwide have clearly been towards more centralized arrangements, rather than less.

[185] This is argued in chapter 2 of this thesis.

constitution, which made all the difference. Therefore, the failed assimilation could be interpreted as concrete evidence that the American decentralized banking system, with the multiple chartering authorities, has been kept in place artificially through constitutional forces. Put differently, if the political process was not constrained by the constitution and was free to choose the regulatory institutions (as there was in the case of Germany), a system such as the American decentralized regulatory arrangement would not survive for as long as it did. If this rationale is accurate, there is no need to look for economic explanations that have helped sustain the American regulatory system.

Would the Institutional Assimilation have had a chance if the Americans had acted more swiftly and more boldy? A brief look at the developments in Soviet-ruled East Germany show that permanent radical change to a banking system is possible. However, East Germany was being transformed into another dictatorship with a different economic set-up, whereas the western Allies wanted to implant the notion of democracy. Thus, dictating a new order of things was almost impossible from the moment Germany had its own democratically legitimized parliament. Nevertheless, it seems plausible to assume that had the Americans successfully eliminated the most vociferous advocates of a centralized banking system – the *Großbanken* – and had the U.S. implanted 'safeguards' in the constitution in the form of impenetrable state rights to regulate the banking system, that the assimilation could indeed have succeeded. The states were taken in by the federal system, which gave them greater power. They were not prepared to let it go. Even more, had the constitutional court ruled in favor of the states rights in 1962, then we could still see a decentralized regulatory system in Germany today.

Chapter 5

Epilogue

After the passage of the Credit Act in 1961 and the Constitutional Court's ruling in 1962, the issue of banking regulation did not subside. The question of whether to introduce additional competitive pressures, which was one of the two key issues debated in the genesis of the Credit Act of 1961, continued to be a matter of debate in the banking circles.[1]

A ruling from the Federal Administrative Court in 1958 had already abolished the requirement to obtain the government's approval, if banks wanted to open new branches. This unintentional liberalization[2] led to a sharp increase in the number of bank branches being established throughout Germany. Between 1957 and 1967, the number of banks and their branches increased from 26,333 to 37,144. At the same time a mild concentration process took place, as the total number of banks shrank. But even so the overall result was a net increase in banking offices. This increased the competitive pressures to some extent.[3] Competitive pressures also increased as some of the *Sparkassen*, and most of their parent institutions, had increasingly turned into full-fledged universal banks, to the dismay of the other private credit banks and the credit cooperatives. The private banks in turn discovered that many of the small and medium scale clients of the *Sparkassen* had become sufficiently wealthy so as to become a lucrative business opportunity, which they

[1] It was hardly ever a topic of general political interest. See for example Muthesius (1967, p. 3).

[2] It was unintentional since it did not originate in actions taken by either the legislative or the executive branch of government.

[3] On average, the number of banking offices increased by about 1250 per year during this period. See Ambrosius (1998, pp. 157–158) and Büschgen (1982, pp. 398–399). For the concentration process see also Pohl (1982d, pp. 460–483).

intended to tap. And in order to tap this market, they needed to find a way to break the dominance of the public banking sector in this segment.[4]

Already in the spring of 1961, as Ludwig Erhard struggled to obtain the necessary supermajority in parliament to secure the passage of the Credit Act of 1961, he convinced the lower house of parliament to install a government commission under the auspices of his Economics Ministry. The internal commission was to study the feasibility of introducing deposit insurance. It was also to investigate the nature of competition within the banking sector, to identify distortions to competition, which needed to be removed in order to establish a level playing field. This commission was strongly supported by the association of the private banks, and the association of the credit cooperatives, who saw it as an opportunity to defend themselves from the competitive pressures of the public banking system, and to bring about competition on more equal terms. After all, the public banks still enjoyed important privileges over non-public banks, such as the implicit government backing as well as tax exemptions.[5] This issue was a highly sensitive topic and Erhard was well aware of this. The public banks naturally saw this Enquête as a major threat not only to their privileges, but also to their very existence as a public institution. Consequently they attempted to discredit the Enquête altogether, by questioning its objectivity and by accusing the private banking sector of calling for the help of the federal government to masquerade their own inefficiency.[6] The final report of the Enquête, was only published in 1968.

The commission was not tasked with analyzing the question of whether to liberalize the interest-rate restrictions. Nevertheless, this discussion grew increasingly in intensity within the relevant circles. As of 1961, the public banks welcomed a gradual abolition of the interest rate cartel. After all, they benefited from a number of government subsidies that gave them an important competitive advantage over private-sector banks. In turn, the private-sector banks vigorously opposed any liberalization. It secured their rents and more importantly it shielded them from additional competitive pressures from the public

[4]See Pohl et al. (2005, pp. 305–308).

[5]See Deutscher Bundestag (1968, pp. II–III). Please note that the final report does not state the personnel composition of the commission. Thus, it is likely that the report was prepared by members of the Economics Ministry, who had previously asked experts for their opinion on this matter.

[6]See Pohl et al. (2005, pp. 307–308, 341).

banks. They argued that the liberalization would lead to higher interest rates, ruinous competition, greater concentration and ultimately financial instability. In early 1960s, the Bundesbank also officially opposed to abandon the interest-rate restrictions, as it still saw the restriction as an important tool, safeguarding its monetary policy transmission.[7]

A cautious liberalization took place in 1965, when interest rate restrictions on deposits with a duration of over 30 months were abandoned by a decree of the Federal Supervisory Office. Before announcing this decision it had consulted the Economics Ministry, the Bundesbank and the banking associations on this matter. Note that the states were not officially involved in determining the terms of the interest rate restrictions anymore, and could therefore not object, if they had wanted to. The liberalization was introduced alongside a number of refinements to the interest rate restrictions that linked short term lending rates to the discount rate, as well as establishing ceilings to short term deposit rates. While the public banking system welcomed the gradual liberalization, it was opposed by the private banking sector, as they feared the renewed competition from the *Sparkassen* system.[8] A consequence of the partial liberalization of deposit rates was that banks subsequently began to refinance themselves cheaply by issuing medium term notes that were not subject to the restrictions, and, unlike regular deposits, were not subject to reserve requirements. Subsequent adjustments in the regulations failed to contain the banks' circumvention of the interest rate restrictions. This development came hand in hand with the increasing internationalization of German banks, which expanded operations into the Euromarket by establishing subsidiaries abroad, in particular in Luxemburg. Some observers saw this as

[7] See Ambrosius (1998, pp. 164–165) and (Muthesius, 1967, pp. 1–2). See also Ashauer (1982, p. 323), Becker (1967, p. 18) and Pohl et al. (2005, p. 337) for the position of the public banks. See Büschgen (1995, p. 703) for the opposition of the influential Deutsche Bank. See the opinion piece Gespräch des Tages (1965), which reports that proponents of interest-rate liberalization were intellectually 'stoned to death' by the opponents in the banking sector in the late 1950s and early 1960s. Similarly see the opinion piece by Muthesius (1966, p. 1).

[8] See Becker (1967, p. 18), Ambrosius (1998, pp. 165–166) and Franke (2000, p. 9). Henckel (1966) pointed out that official cartelization of the banking sector began in 1912. In 1931 it was transformed into a government-sanctioned interest rate cartel (i.e. the banks agreed on interest rates limit, which the government then declared universally binding), and now interest rates were outright decreed by the government, without a prior agreement by the banking associations. Technically, the liberalization in 1965 was also the first time that the Federal Supervisory Office issued a decree with respect to interest rate restrictions. Prior to that, the no longer existent state regulatory agencies had always taken the consensual decisions of the banking associations and then declared them universally binding. See Franke (1999, p. 257).

the first step towards a complete liberalization of interest rates.[9]

And indeed, the discussion surrounding the liberalization of interest rates became more intense.[10] The private banks' associations continued their stiff opposition and painted a grim picture of financial conditions, should interest rates be further liberalized. They were only willing to accept a liberalization of interest rates, if it went in hand with the abolition of the tax privileges for the public banks. At the same time, many of the associations' member banks reacted to the changing conditions and took advantage of the new liberties given to them. In turn, proponents of liberalization, i.e. the *Sparkassen*, the Economics Ministry and the Federal Supervisory Office, began to point out that 'grey' markets had already effectively undermined the interest rate restrictions. Additionally, they pointed out empirical studies, which indicated that an abolition would not have an adverse effect on the transmission mechanism of the Bundesbank's monetary policy, and that it might even have positive effects. Furthermore, the Bundesbank's position shifted towards cautious liberalization as well. What the proponents of liberalization had in common was that all believed that the most sensible way to proceed would be to further loosen restrictions once more in a few years time, and to abandon them after another period of adjustment.[11]

The interest rate restrictions were eventually abolished altogether in the spring of 1967. The timing of the liberalization was remarkable in the sense the Erhard-led government, which was presumably in favor of liberalization, had just collapsed in the wake of a growth slowdown that had led to higher unemployment. A grand coalition government between the SPD and CDU with Georg Kiesinger at its head, and Karl Schiller as economics minister took over from Ludwig Erhard. The grand coalition quickly resorted to implementing anticyclical fiscal and monetary policy and it was supported in this by the Bundesbank.[12] It was in this environment that Economic Minister Schiller, who had

[9]See Ambrosius (1998, p. 165–166), Büschgen (1995, p. 632), Franke (2000, p. 10), Franke (1999, pp. 257, 259) and the opinion pieces by Gespräch des Tages (1965) and Henckel (1966). Henckel was a senior bureaucrat of the Economics Ministry at the time. For an overview of the internationalization of the German banks after the Second World War see Büschgen (1982, pp. 383–396).

[10]The first issue of the bankers' magazine *Zeitschrift für das gesamte Kreditwesen* in 1966 was dedicated to this question. It contained opinion pieces by all the relevant actors on the question of whether or not to liberalize interest rates any further.

[11]See Becker (1967, p. 18, 20), Draheim (1966), Heide (1966), Henckel (1966), Hoffmann (1966), Janberg (1966), Kalkstein (1966), Könnecker (1966), Looff (1973, pp. 11–12), (Muthesius, 1967, p. 1) and Muthesius (1966).

[12]See Pohl and Jachmich (1998, pp. 203–207).

not been much of a supporter of free-market ideas, pushed for the complete liberalization of interest rates, as he hoped that they would be pushed lower by this step.[13] The private banking association attempted to prevent further interest-rate liberalization until the very last momen and when the government announcement came it was a surprise to all banks. No-one had expected such a swift and complete liberalization. The monumental importance of the liberalization – after of 36 years of government sponsored interest-rate cartelization – was reflected in the banking associations' subsequent behavior. In order to smooth the transition from an environment of restricted short term interest rates to one of complete interest-rate freedom, the banking groups' associations issued non-binding recommendations on interest rates to their members.[14] The interest rate recommendations were at first tolerated by the government, but eventually became a source of disagreement between the Federal Supervisory Office for the Banking Sector and the Antitrust authorities, as the latter saw these recommendations as a violation of the Antitrust Act. The banks reacted in the early 1970s by first abolishing the recommendations altogether, and later replacing them with softer guidelines.[15]

Within a couple of months of the abandonment of the interest rate restrictions, the government further liberalized competition in the banking sector by annulling restrictions to competitive behavior. These had restricted the advertisement practices of banks and had been in place since 1928, after which they were incorporated into the Credit Act of 1934. This liberalization was supported by all banking associations, as they now accepted the changed circumstances and saw greater marketing expenditures as a way to outcompete

[13]The irony of these developments was not lost to contemporary observers. See for example (Muthesius, 1967, p. 2).

[14]See Ambrosius (1998, p. 166), Büschgen (1982, p. 375), Pohl and Jachmich (1998, p. 207) and (Muthesius, 1967, p. 1–3). Lore Bähre, a subsequent president of the Federal Supervisory Office, acknowledged that the liberalization of interest rates was necessary, because of the circumvention and the complexities of maintaining such a system with banks, which were active internationally. According to her, the Federal Supervisory Office favored to liberalize interest rates gradually, much like the public banks. The complete liberalization of 1967 took the Federal Supervisory Office somewhat by surprise. She attributes the liberalization with the federal government's desire to lower interest rates – which the liberalization did not succeed in achieving. See 7. Symposium zur Bankengeschichte (1982, pp. 47–52). For the interest-rate recommendations see also the opinion pice Gespräch des Tages (1967) and one of the announcements by the association of the private banks in the *Zeitschrift für das gesamte Kreditwesen*, Vol. 8., No. 8, p. 17, 1967.

[15]See Ashauer (1982, p. 323) and Büschgen (1982, pp. 400–401). For an analysis of the economic effects of the interest rate liberalization see Looff (1973).

each other. Within the next decade, financial institutions significantly increased their advertising and marketing expenditures.[16]

Last but not least, the government also reduced the tax advantages the public banks enjoyed. Whereas they were previously exempt from corporate taxation, they were now subject to it – however to a much reduced rate compared to private credit institutions. Even so, the association of the public banks attempted to lobby for an indirect compensation, to restore its competitive advantage. It demanded, once more, that the implicit government backing (the *Gewährträgerhaftung*) should be taken into account when calculating the *Sparkassen's* capital. After all, as public institutions they could not access markets to raise capital and could only do so through retained earnings. However, the public banks were unsuccessful and no exemption was granted.[17]

By the end of 1968, when the Enquête had finally published its final report, major liberalization had taken place in the German banking sector. Competition amongst banks was no longer restricted; a first since the late 1920s.[18] Each bank group was both a winner and a loser of the reforms. Whereas the public banks profited from the long-sought removal of the barriers to competition, they had to accept corporate taxation for the first time in their history. Conversely, the credit cooperatives and the private credit banks that had tried to prevent the removal of the restrictions to competition, could at least be satisfied that the savings banks' special treatment had been rescinded to some extent.

In its final report in 1968, the Enquête recommended the introduction of a unified government-mandated system of deposit insurance, in order to cushion the impact of the increase in competition in the banking sector. Yet, no such measure was taken. Instead, discussions between the banking associations, the relevant government ministries and the Federal Supervisory Office ensued. In these the banking associations eventually agreed to self-regulatory measures, promising to establish guarantee funds, if they had not already done so like the Credit Cooperatives, that would insure depositors up to a certain amount.

[16] See Büschgen (1982, pp. 401–402).

[17] See Ashauer (1982, p. 323) and Pohl et al. (2005, p. 340–341).

[18] A proposed amendment to the Antitrust Act would even have taken liberalization even further, as it would have rescinded the exemption of the banking sector from the general prohibition on cartelization, but it failed to come to fruition. See for example Möschel (1972, pp. 548–552) for an analysis of the draft amendment.

Even the public banks agreed to establish a fund of their own. Banks that were not members of any of the banking associations, were soon encouraged by the Federal Supervisory Office to nevertheless join the guarantee fund scheme. In the aftermath of the 1974 Herstatt crisis, the private credit banks rushed to introduce an improved private deposit insurance scheme. Government-mandated deposit insurance was introduced in Germany only in 1997 as part of the harmonization of financial legislation within the EU. In an ironic turn of history, the finance ministry was again given the subject matter competence over money and credit in 1972, where it continues to remain to date.[19]

In the shadow of the debate with respect to competition in the banking sector, another discussion began in the mid 1960s with respect to the structure of the banking sector. This question had not been raised in Germany since the 1930s. Once more the question was raised, whether universal banking was desirable or if the separation of investment and deposit banks should be introduced in Germany as well. This time around the trigger for this discussion on the potential separation was not another banking crisis, but the sluggish development of capital markets in Germany vis-a-vis the Anglo-Saxon world. Critics of universal banking had pointed out – once more – the potential conflicts of interest that could arise within universal banks, which would inhibit the efficient allocation of funds. After all, the private interest was dominating welfare or public interest considerations within corporations. The discussion eventually led to a government commission in 1974, which, in its final report of 1979, recommended to maintain universal banking, however.[20]

[19]See Büschgen (1982, pp. 376–378). He does not mention why the chancellor took the decision to transfer competence back to the finance ministry. For an chart of the liberalization of the German financial market until 2000 see for example Franke (2000, p. 7).

[20]It argued that the advantages of the separation would not outweigh the costs incurred by the inherent of conflict of interest. See Büschgen (1982, pp. 356-360). He also reports that the ruling Social Democratic Party (SPD) had included a demand to abolish universal banking in its policy framework for the years 1975-1985. However, the SPD-led government showed no actual intention to push this agenda.

Chapter 6

Conclusion & Discussion

6.1 Conclusion

This thesis set out to investigate the evolution of the structure of banking regulation of two federal political systems: that of the United States and Germany. It aimed at explaining why Germany introduced a regulatory monopoly and why the United States opted for a decentralized regulatory architecture. Furthermore, it set out to explain why there seems to be such a strong path dependence between the banking regulations introduced in Nazi Germany and those drawn up in post-war Germany, even though the German banking system was subject to a massive structural intervention by the American military government that aimed to decentralize all aspects of the banking system. The main driver behind these developments is found in the varying degrees of constitutional states' rights to regulate the banking sector, rather than in diverging macro-prudential considerations.

The findings suggest that at several times throughout its history, the American federal government actively tried to bring about a unified regulatory banking system under national supervision. First, with the establishment of the national banking system (1861–1865), then with the introduction of the Federal Reserve System (1910–1917) and again with the addition of the Federal Deposit Insurance (1930–1935). All of these institutional additions can be interpreted as an attempt by federal policymakers to set the incentives in such a way that would compel state banks to subject themselves to national regulation. In exchange, these banks would obtain competitive advantages vis-a-vis banks not submitting to national regulation. The federal government had to take this indirect route, since the constitution prevented it from explicitly prohibiting states to charter banks. The states' right to charter and to regulate banks is enshrined in the constitution. Not even the constitutional clause on the supremacy of federal law could break this states' right.

Every single one of these indirect centralization attempts failed as they were easily 'loopholed' either by legislation or financial innovation soon after their establishment. There was no doubt, however, that influential parts of the American policymaking elite considered a unified banking system superior, in terms of stability, to the decentralized arrangement that was in place. Furthermore, each attempt to bring about a centralized regulatory system was accompanied by the creation of new institutions. Subsequent attempts to centralize regulation did not reform or supersede the existing regulatory institutions and instead created new ones alongside the old ones. Thus, the 'regulatory ruins' of previous attempts persisted and evolved into political actors themselves and ultimately contributed to a further decentralization of the regulatory structure.

In Germany, matters were quite different. The federal government tried to avoid regulating the banking sector for as long as it could.[1] It was aware of certain deficiencies within the sector, but it delegated the responsibility to the *Reichsbank*. In turn, the *Reichsbank* worked together with the banking associations in order to overcome the deficiencies, and to keep the federal government's profile in regulating the banking sector small. The *Reichsbank's* corporatist regulation was succesfull in the sense that up until the Banking Crisis of 1931, the German government had no intention to introduce widespread regulation. It shied away from the responsibility associated with it and it relied completely on the *Reichsbank*. The crisis, however, forced the central government to regulate. It needed to rescue Germany's largest commercial banks as they were considered too big to fail. It also needed to bail-out the public Sparkassen system, which, in theory, was supervised and backed by the states. Thus, as the central government took a large stake in both private and public banks, it felt compelled to introduce a centralized regulatory regime in return. In addition to that, the American system was often brought forward as a negative example against decentralized regulation.

The German central government encountered no resistance in introducing a central regulatory regime. By 1931, the German government had resorted to governing with the help of emergency decrees, which did not require parliamentary approval. Contrary to the American case, there were no constitutional barriers to a centralized regulatory solution

[1] Merely pure mortgage banks were restricted in their activities. Also, the emission of banknotes was mostly restricted to the central bank.

either. At the same time, the regulation introduced by the German government was understood to be temporary in nature only. A permanent system would only be introduced after the 'structural defects' in the banking system had been identified and erased. The fact that the German banking system (and consequently the banking regulations) retained its shape, and was not outright nationalized entirely by Nazi ideologues, is attributable to Hjalmar Schacht. Hitler valued his expertise, and this allowed Schacht to 'hijack' the reform deliberations and to stage a bank inquiry, whose outcome was largely determined before it even began. It eventually proposed a regulatory system according to his personal preferences, which was very much in line with the system first introduced as emergency decrees by the Weimar government.

After the Second World War, American military government officials, some of which were staunch supporters of the antitrust ideology and thus of independent unit banking, managed to project many of the principles governing their own state banking system onto the German one. This implied the decentralization of the German banking system by introducing branching restrictions, by breaking-up of the largest banks, by federalizing the central bank and by decentralizing the regulatory institutions. These institutional changes were pursued with religious zeal until 1949. The American assimilation effort of the German banking system came to a halt with the establishment of a German federal state based on democratic principles. From then on, the primary policy goal for the Allies was to turn Germany into a sovereign nation within Western Europe, rather than the implementation of fresh American economic ideas. In terms of the banking sector, the policy was to ensure that the large commercial banks did not re-establish themselves completely and that at least some level of decentralization or antitrust thinking was maintained in the banking sector.

German businessmen and policymakers rejected the introduction of branching restrictions and the decentralization of its largest commercial banks. Other large commercial banks that were in state hands did not suffer much of a decentralization, although this was discussed by the American military government as well. This inconsistency in the behavior of the American occupiers made their arguments, that they were attempting to reduce financial concentration, seem incoherent to Germans. Consequently, the policy appeared as a punishment, rather than a benevolent institutional reform. At the same time, the decentralization of the large commercial banks was not carried out completely, as the legal shells of the former large institutions lived on throughout much of the period. Thus, it was relatively easy for the banks to reunite once branching restrictions were lifted again. The branching restrictions, that had been introduced in parallel with the decentralization of the largest commercial banks, were motivated by banking ideology rather than by economic considerations. Even in the United States, branching restrictions were a controversial topic. In Germany, where these had not had much of a historical precedent, they were only seen with disbelief. There was no influential interest group in support of unit banking in Germany. Thus, in the case of the decentralization of the largest banks and the branching restrictions it was the American influence that held them in place. Once the Allied High Commission withdrew from German banking politics, the changes to the largest credit banks and the branching restrictions were reversed. While there was some opposition from the BdL and from some German states to the abolition of branching restrictions, these were not motivated by belief in the necessity of restricting branching. Rather, for the BdL the opposition reflected a fear that the abolition of branching restrictions might go hand in hand with reforms to the decentral organizational structure of the BdL. The opposition of the southern states reflected an attempt to extract fiscal rents for their political support.

The decentralizing changes to the central bank structure and to the regulatory structure, however, had a much better chance at survival than it is often implied in the existing literature. Indeed, the first drafts of both the Credit Act and the Bundesbank Act largely reflected the decentralized status quo that was introduced by the Americans. It was only after the subject matter competence for money and credit changed from the Finance Ministry to the Economics Ministry, that more centralized drafts were drawn up. Just like in the United States, the primary bone of discord were states' rights. It was not the American influence that held the decentralized arrangement in place in Germany for so long, but it were the German states. They were not willing to give up their newly gained competences to the central government. The German states fought every attempt by the central government to extend its control over the banking sector, but eventually they had to concede defeat. The constitution, as it was ultimately interpreted by the constitutional court, had given the central government the right to unilaterally legislate in the field of money and credit without the consent of the states, provided that it had a sufficiently large majority in the lower house of parliament. Had the constitutional court ruled in favor of states' rights, Germany might well have a decentralized regulatory regime today.

The need for a supermajority is the key reason, why Germany retreated to its pre World War II central regulatory system. The central government's primary objective was to re-establish centralized regulatory control over the banking sector. In order to do so, it had to build a sufficiently large coalition that could overrule the states' veto. Any modification to the pre-war Credit Act, even if progressive in nature, would have threatened the parliamentary supermajority. Thus, going back to the old consensus path was the easiest way for the central government to strip the states of their rights to regulate and supervise the banking sector. Innovative reforms, such as the introduction of deposit insurance, the reform of the public banking sector, or even the introduction of competitive pressures, were discussed and also supported by Economics Minister Ludwig Erhard. But ultimately, they were left to the future in order not to jeopardize the supermajority. The only changes in the Banking Act of 1961 with respect to that of 1934 were primarily modifications that were due to the new constitution and the modified central bank, but they were not due to the American assimilation effort. Another clear indicator of the federal conflict is the fact that the Central Bank Act and the Credit Act were only passed as late as 1957 and 1961, numerous years after the American military government had ceased to actively shape German legislation and policy.

Thus, the most lasting impact the American military government had on the German banking system was less in the form of outright intervention in the banking sector, but more an indirect one via the German constitution. It too, was formulated under the supervision of the Americans and its Allies, and it contained elements of the American federal set-up. The constraints of the German constitution set the political and economic playing field. Although the *Grundgesetz* was certainly federal in nature and gave the states extensive responsibilities, it allowed Germans to centralize their economic and thus banking system much more than the American banking reformers would probably have liked to see. It seems like American policymakers were not careful enough in the drafting process of the German constitution, to ensure that appropriate decentralizing safeguards for the banking sector were implanted. Ultimately this omission sew the seeds for the failure of their decentralized banking system to take hold in Germany.

And indeed, the years following the passage of the German Credit Act of 1961 saw changes in the regulatory framework. An extensive government commission was set-up to investigate the banking sector. Amongst other things, it suggested the introduction of a deposit insurance scheme, and it addressed the issue of competitive inequalities between government and private banks. However no major change arose from this other than the introduction of private deposit insurance schemes rather than a government insurance scheme. Indeed, government deposit insurance was introduced in Germany only in 1997 as part of the harmonization of financial legislation within the EU. But other major liberalizations took place just a few years after the passage of the Credit Act of 1961. The state enforced interest-rate cartel, which had effectively been in place since 1932, was abolished in 1967. Similarly, restrictions on banks' advertising practices also expired a few months later that had been first introduced 1928. Both these measures increased competitive pressures within the banking sector. As a measure of compensation for the private banks, who had continued to advocate a restriction to competition in order to protect themselves from the public banking sector, the public banks were, for the first time in their history, required to pay corporate tax – although not quite at the same level as private sector banks. More liberalizations would follow in the subsequent years, but the structure of the regulatory institutions remained unchanged. In an ironic turn of history, the finance ministry was again given the subject matter competence over money and credit in 1972, where it continues to remain to date.

The post war period in Germany also holds insights for American regulatory history. In Chapter 2 of this thesis, I concluded with the hypothesis that it was the states' rights, which kept the American decentralized regulatory system in place and that in the absence of strong states rights, no such system would persist over time. The American intervention in Germany after the Second World War can be interpreted as a test of this hypothesis. After all, the Americans exogenously forced their decentralized banking principles onto the German banking system. Since the German federal constitution did not contain the same extent of states' rights with respect to chartering banks as its American counterpart, one would expect that the decentralized institutional arrangement would not persist. And indeed this it what happened. Germany reverted to a centralized framework of regulating its banking sector.

What is further striking is that one could observe almost the same, intense constitutional conflict between the states and the federal government as there was in the United States. The German states fought the federal take-over equally vigorously. They even began to use similar arguments to those put forward by proponents of the decentralized state banking system in the United States. However, in the German case, the constitution did not give the states the same powers with respect to the banking sector and, eventually, they were stripped of their regulatory privileges. Thus, this episode provides additional leverage to the hypothesis that it was indeed the states' rights and not an economic explanation that kept the American decentralized regulatory system in place.

It is also telling that after deciding to introduce comprehensive banking regulation in the wake of the financial crisis of 1931, German policymakers actively chose their regulatory framework at three points in time. They selected their preferred set-up during the Weimar Republic (in 1931 after the Banking crisis), during the Third Reich (with the 1933/34 Banking Commission) and after the Second World War (1949–1961). And every single time the top policymakers came to the conclusion that a centralized system of regulating the banking sector was preferable to a decentralized one. The only time that there was a strong opposition towards a centralized system of regulation was because of the American regulatory gift to the states after the Second World War.

The findings of this thesis may lead to a re-interpretation of *the long shadow of Hjalmar Schacht*. In the banking sector, the shadow is clearly visible, however it was not quite as long in the banking sector as it may have been in other parts of the economy. It began to dissipate in the mid 1960s, when a deliberate liberalization of the banking sector set-in. Also, Schacht's shadow may have been prolonged by the fact that the Allies introduced a federal constitution. At the outset of the Federal Republic of Germany, many important economic control mechanisms were not in the hands of the federal government, but in those of the states. Thus, the central government had to engage in a federal struggle with the states, in order to reinstate its legislative superiority over economic matters. This was not only the case in the banking sector, but in other sectors too. The struggle over German Antitrust Act reflects a similar process. It, too, significantly strengthened the role of the Economics Ministry in regulating the economy.[2] And the only way for the federal government to secure the necessary supermajority to do so, was to retreat to the existing centralized corporatist economic order that had largely been established during the Third Reich. Only once the central government had successfully recentralized economic control, could it then move to liberalize the economic structure.

[2]See for example Hüttenberger (1976).

Such a re-interpretation of German post-war economic history essentially inverts the Olson hypothesis. Instead of a liberalization taking place at the outset of the German Federal Republic, this interpretation suggests that institutional change was unlikely at the outset, as control over the economic order was decentralized. Only over time, when the federal government regained control, was it able to break up vested interests. And only then was it able to introduce real institutional change that allowed it to emerge from the shadow of Hjalmar Schacht. Thus, even though Ludwig Erhard may not have been able to introduce many of his liberal economic principles himself, he nevertheless provided the ground-work for future liberal reforms by recentralizing economic control over the economy with the federal government, and in particular with the Economics Ministry. While Erhard was not the German Margaret Thatcher he is often made to be, he made Margaret Thatcher-style reforms possible in Germany by overcoming the American-induced institutional sclerosis. This may be an important legacy of Ludwig Erhard – one that had been largely overlooked so far.

This view of Erhard's accomplishments are in line with the biographic portrayals of Ludwig Erhard. These generally portray his post-political period as that of an exhausted and unfulfilled man.[3] According to the interpretation put forward in this thesis, Ludwig Erhard would have spent most of his political career not creating the free-market economy he advocated so strongly, but rather he spent his political capital fighting with vested interests, which sought to maintain the restrictions to competition, and with the states in an effort to reestablish the federal government's control over the economy. By the time he was elected Chancellor, presumably the apex of his political power, he had spent most of his political capital and made so many enemies in the prior struggles, that he was unable to introduce any major free-market reforms. He retired from political office frustrated that he was not able to bring about the legendary social market economy he became so famous for.

To sum up, in answering the research questions, this thesis makes the following original contributions to knowledge: (1) This thesis offers a novel perspective on the evolution of the structure of American banking regulation by interpreting it as being largely driven by constitutional conflict (2) it shows that prior to the Banking Crisis of 1931 there was no intention to introduce a comprehensive regulatory structure for the banking sector

[3] See especially Hentschel (1998) and Mierzejewski (2004).

in Germany (3) It provides a reassessment of the origins of the German Credit Act of 1961 as a non-deterministic process (4) It interprets German banking regulation after the Second World War as a failed Institutional Assimilation, which provides evidence that the decentralized regulatory arrangement of the American banking system was held in place by strong states' rights. In the absence of strong states' rights such a system would not persist and, indeed, in Germany it did not (5) It re-interprets German post-war economic history as being driven by the need of the German federal government to re-establish supremacy over economic matters. This assigns a new important role for Ludwig Erhard in German post-war competition history, as being an enabler of liberalization rather than being a liberalizing force himself.

6.2 Future Research

There are several ways to build on this line of research. One could compare the American approach to the banking sector in Germany and in Japan.[4] Why was American banking policy in Japan much less ambitious than in Germany?[5] Given that the Americans had the sole control over Japan it would have been much easier for them to implement a desired change. Indeed, Joseph Dodge, who had crucially stimulated the institutional changes in Germany was later assigned to Japan as Economic Adviser. Why did he not pursue banking reforms with equal vigour, given that the German and Japanese banking structure was similar in many respects? One could also compare the regulatory policies undertaken by the Allies in Austria with those that took place in Germany. After all, Austria was also under the occupation of the four powers. Did the Allies pursue different regulatory policies? If so, why? And if not, do we find a different development than in Germany? It would certainly also be fascinating to study recent American efforts at state-building in Afghanistan and Iraq. Which approaches have been taken in terms of the banking system in these countries? Was there an American learning process from the German and Japanese experiences?

After the Second World War, there were movements in the United States to centralize the regulatory institutions at various times.[6] But centralization continues to be elusive to

[4]This would be analogous to the PhD Thesis of Partridge (2011), who compared the outcomes of American industrial Antitrust efforts in Germany and Japan after World War II

[5]See Tsutsui (1988) for an account of American banking policy in Japan.

[6]See for example Pierce (1977, pp. 605–607), Robertson (1966, p. 686) or Scott (1977, p. 46).

this day, even though banks now often operate on a national scale. Why is this so? Even more perplexing, how come the American federal government is even unable to merge its existing federal supervisory institutions? Where exactly does this inability to centralize, even at the federal level come from? Why are the 'regulatory ruins' so hard to make away with despite the obvious shortcomings of such a decentralized system when it comes to crisis prevention and resolution?

It would also be interesting to study the German regulatory development from 1961 onwards and its subsequent interactions within the European framework of banking regulation. To what extent did European pressures force changes upon the German regulatory framework, if at all? Why did subject-matter competence over the banking system return to the Finance ministry in the 1970s? Did German banks play an important role in lobbying European and International decision makers during the Basel negotiations and the negotiations to create the European Monetary Union? And if so, to what extent? After all, Germany was a main opponent to a unified regulatory system of the banking sector for the Eurozone. Was the failure to implement centralized banking supervision and regulation alongside the monetary union another case of a constitutional conflict between states (the EU countries) and the federal government (the EU level) or was it primarily due to bank lobbying?[7]

Last but not least, this thesis opens up the opportunity to engage in a more comprehensive and systematic meta-study based on existing research that documents and analyzes to what extent the *shadow of Hjalmar Schacht* persisted in the various sectors of the German economy. Only then will we be able to better judge to what extent the proposed hypothesis, that Erhard was an enabler of liberalization rather than a Margaret Thatcher himself, is indeed applicable to other sectors of the economy.

[7]See James (2012, Loc: 532–539) a treatment of the political economy of a unified regulatory system within the European framework.

6.3 Lessons for today

The exact causes of the recent financial crisis is controversial to say the least.[8] Regulators have naturally received much of the blame for the crisis even though a number of safeguards have failed in multiple countries at the same time.[9]

The political dynamic of current attempts to overhaul the regulatory structure in the European Union follows similar, though not identical, patterns as those outlined in this thesis. After all, the European Union is a looser federation than both Germany and the United States were in the time period studied and it does not yet possess significant financial resources of its own. Furthermore, it is characterized by a core of countries that have decided to engage in a monetary union and a periphery that has decided, for the moment, not to join the monetary union. However, the severity of the current financial crisis has made it clear that an integrated financial market with a monetary union only has only a realistic probability of survival if there is some kind of banking union that allows for a single supervisory and crisis resolution mechanism.[10] Given the findings of my thesis, one would expect the European states would not be willing to give up their regulatory responsibilities lightly. And indeed, the wrangling over the extent of a regulatory situation is already in full swing. One can already observe some states negotiating to retain their regulatory powers.

Based on my research, a crucial element of the future regulatory structure will be to what extent the European leaders will be able to forge a coherent, centralized system under the leadership of the ECB. It will be important to re-shape the existing regulatory institutions into full-fledged European (and not national) institutions. Otherwise, the danger is that Europe will end up with a semi-centralized regulatory framework in which

[8] See for example Lo (2012). The American Financial Crisis Inquiry Commission (2011) (FCIC), which was officially tasked with examining the causes of the financial crisis, contains a majority opinion as well as two dissenting opinions. Not even the dissenters could agree in their dissent. For the majority opinion see Financial Crisis Inquiry Commission (2011, xv–xxviii) and for the first dissenting opinion see Financial Crisis Inquiry Commission (2011, pp. 411–440).

[9] Sheng (2009, pp. 387–388) suggests that blaming only the regulators is too easy. After all, *"four lines of defence for financial stability"* needed to be breached for the crisis to occur: 1. Self-discipline (corporate governance), 2. External auditors and advisors (investment banks, lawyers, consultants, 3. Sunshine or transparency mechanisms (rating agencies, market analysts and media) and last but not least 4. Government regulation (financial regulators and criminal enforcement agencies).

[10] See the first blueprint to the proposed banking Union by the European Commission (2012b), the conclusion by the Council of the European Union (2012) on the Single Supervisory Mechanism, as well the agreement of the European Council (2012) on a raodmap for the completion of the economic and monetary union, which encompasses the banking union.

the regulatory ruins take on a political life of their own that could potentially counteract the policies of the center, the ECB. My findings also suggest that when it comes to EU treaty changes or even the drafting of an EU constitution, care should be taken to officially transfer powers to charter, regulate and supervise the banking sector to the EU level, rather than leaving it to the individual states. If the central regulatory institutions are to be truly independent from the states, the EU level will have to be given a much more significant measure of fiscal power as a percentage of EU GDP. After all, crisis resolution mechanisms may require regulators to recapitalize or wind down banks. They also need to be readily available as time is of the essence, and in a decentralized structure with overlapping responsibilities the resolution process can be drawn out, increasing uncertainty and thus delaying economic recovery.

Interestingly, the way the American federal government has been able to significantly extend its reach of the banking sector during the past three to four decades, seems to have been by reducing restrictions and by lowering regulatory standards for national banks and state member banks. The race in regulatory laxity seems to have persisted up until the beginning of the financial crisis of 2007, but not only between national and state chartered banks, but also between federal regulatory agencies.[11] Although the government may have managed to bring much of the formal banking sector under some kind of federal control, primarily under the FDIC which administers the deposit insurance, the problem of the multiplicity of regulatory institutions and jurisdictions has still not been solved. It has merely been transferred to the federal level.[12]

The fragmentation of regulatory responsibility and consequently of information has led to a failure of regulators to see the dangers building up within the system. Additionally, diverging opinions, responsibilities and fiscal capacities amongst the regulators has also prevented the smooth implementation of crisis resolution mechanisms.[13] Not only has the United States still not found a way to combine the regulatory ruins left from previous

[11] This view is often reflected in the contemporary legal literature on federal preemption of state law. See for example Johnson (1995) or Natter and Wechsler (2012). Abrams and Settle (1993, p. 701) suggest that the S&L crisis at the end of the 1980s weakened the small bank lobby as well as state regulators, thus paving the way for countrywide branching.

[12] Neither has the federal government been able to take away the states' constitutional power to charter and regulate banks. Some of the largest commercial banks are indeed state banks that are members of the FDIC, but not members of the Federal Reserve System. See Federal Reserve Board (2012) for an overview of the largest commercial banks in the U.S..

[13] This seems to be one of the main messages of the first hand account of the crisis of Treasury Secretary Paulson (2010). Similarly see also the findings of the Financial Crisis Inquiry Commission (2011). In Europe this problem was arguably even more pronounced and has not yet been solved.

attempts to regulate the banking sector into a unified regulatory system, but as part of the Dodd-Frank Act, it continued to expand the number of federal regulatory and supervisory institutions.[14]

[14] To the American Congress' credit one has to acknowledge that it abolished the Office of Thrift Supervision (OTS) that was established as regulator of federal savings and loan associations during the 1930s as the Federal Home Loan Bank Board. The OTS was notorious for attempting to attract more banks under its regulatory fold, by offering lax regulatory standards. Its regulatory functions were transferred to the other federal regulatory institutions. For an overview of the current regulatory structureat the Federal level in the United States see for example Jickling and Murphy (2010). The overview does not include the state-level regulatory institutions.

Bibliography

7. Symposium zur Bankengeschichte (1982): "Podiumsdiskussion," in *Der Zusammenhang zwischen wirtschaftlicher Entwicklung und Bankengesetzgebung*, Fritz Knapp Verlag, Frankfurt, 37–63.

Abelshauser, W. (1975): *Wirtschaft in Westdeutschland 1945–1949, Rekonstruktion und Wachstumsbedingungen in der amerikanischen und britischen Zone*, Schriftenreihe der Vierteljahrshefte für Zeitgeschichte, Nr. 30, Deutsche Verlagsanstalt, Stuttgart.

——— (1979): "Probleme des Wiederaufbaus der westdeutschen Wirtschaft 1945–1953," in *Politische Weichenstellungen im Nachkriegsdeutschland 1945–1953*, ed. by H. A. Winkler, Vandenhoeck & Ruprecht.

——— (1983): *Wirtschaftsgeschichte der Bundesrepublik Deutschland (1945–1980)*, Suhrkamp.

——— (1991): "Die ordnungspolitische Epochenbedeutung der Weltwirtschaftskrise in Deutschland: Ein Beitrag zu Entstehungsgeschichte der sozialen Marktwirtschaft," in *Ordnungspolitische Weichenstellungen nach dem Zweiten Weltkrieg*, ed. by D. Petzina, Duncker & Humblot, Berlin.

Abramovitz, M. (1986): "Catching Up, Forging Ahead, and Falling Behind," *Journal of Economic History*, 46, 385–406.

Abrams, B. A. and R. F. Settle (1993): "Pressure-group influence and institutional change: Branch-banking legislation during the Great Depression," *Public Choice*, 77, 687–705.

Adler, H. A. (1949): "The Post-War Reorganization of the German Banking System," *The Quarterly Journal of Economics*, 63, pp. 322–341.

Admati, A. and M. Hellwig (2013): *The Bankers' New Clothes: What's Wrong with Banking and What to Do about It*, Amazon Kindle Edition, ASIN: B00BBYLPYY, Princeton University Press.

Ahamed, L. (2010): *Lords of Finance: 1929, the Great Depression, and the Bankers Who Broke the World*, Windmill Books, London.

Ahrens, R. (2007): *Die Dresdner Bank 1945–1957*, R. Oldenburg Verlag, München.

Allied Control Council for Germany (1945): "Law No 1 from the Control Council for Germany (Berlin, 20 September 1945): Repealing of Nazi Laws," in *Official Gazette of the Control Council for Germany*, Published on 29.10.1945, 1, 6–8.

Allied High Commission for Germany (1950): *Basic Law and Occupation Statute*, Policy Reports Secretary, Office of Executive Secretary, HICOG.

Alston, L. J., W. A. Grove, and D. C. Wheelock (1994): "Why Do Banks Fail? Evidence from the 1920s," *Explorations in Economic History*, 31, 409 – 431.

Ambrosius, G. (1998): "Intensives Wachstum (1958-1965)," in *Geschichte der deutschen Kreditwirtschaft seit 1945*, ed. by H. Pohl, Fritz Knapp Verlag, Frankfurt, 149–202.

Andrew, A. P. (1908): "Substitutes for Cash in the Panic of 1907," *The Quarterly Journal of Economics*, 22, pp. 497–516.

Ashauer, G. (1982): "Entwicklung der Sparkassenorganisation ab 1924," in *Deutsche Bankgeschichte, Band 3*, Institut für bankhistorische Forschung e. V., Fritz Knapp Verlag, Frankfurt am Main, 277–348.

Bagehot, W. (1915): *Lombard Street: A Description of the Money Market*, reprinted in 1978 by Arno Press, New York, original publisher: Smith, Elder, London.

Bähr, J. (2006): "Unternehmens- und Kapitalmarktrecht im "Dritten Reich": Die Aktienrechtsreform und das Anleihestockgesetz," in *Wirtschaftssteuerung durch Recht im Nationalsozialismus: Studien zur Entwicklung des Wirtschaftsrechts im Interventionsstaat des "Dritten Reichs"*, ed. by J. Bähr and R. Banken, Vittorio Klostermann, Frankfurt am Main, 35–69.

Bähre, I. (1982): "Der Zusammenhang zwischen wirtschaftlicher Entwicklung und Bankenaufsicht von 1934 bis zur Gegenwart," in *Bankhistorisches Archiv, 8. Beiheft*, Fritz Knapp Verlag, Frankfurt, 23–34.

Balderston, T. (1991): "German Banking between the Wars: The Crisis of the Credit Banks," *The Business History Review*, 65, 554–605.

——— (1993): *The Origins and Course of the German Economic Crisis: November 1923 to May 1932*, Haude & Speer, Berlin, schriften der Historischen Kommission zu Berlin, Band 2 Beiträge zu Inflation und Wiederaufbau in Deutschland und Europa 1914-1924.

Balleisen, E. and D. Moss, eds. (2009): *Governments and Markets: Towards a New Theory of Regulation*, Cambridge University Press.

Bankenenquete 1908/09 (1909a): *Die Verhandlungen der Gesamtkomission zu den Punkten I – V des Fragebogens. Stenographische Berichte*, Ernst Siegfried Mittler und Sohn.

——— (1909b): *Die Verhandlungen der Gesamtkomission zu Punkt VI des Fragebogens. (Depositwesen.). Stenographische Berichte*, Ernst Siegfried Mittler und Sohn.

——— (1910): *Materialien zur Frage des Depositwesens (Punkt VI des Fragebogens)*, Reichsdruckerei.

Barkai, A. (1988): *Das Wirtschaftssystem des Nationalsozialismus*, Fischer, Frankfurt am Main.

Barnett, G. (1911): "State Banks and Trust Companies since the Passage of the National-Bank Act," in *National Monetary Commission*, Government Printing Office, Washington, 61st Congress, 3rd Session, Document No. 659, available online via FRASER at http://fraser.stlouisfed.org/docs/historical/nmc/nmc_659_1911.pdf, last accessed 17.01.2013.

Barth, J. R., G. Caprio, and R. Levine (2006): *Rethinking Bank Regulation: Till' Angels govern*, Cambridge University Press.

Battilossi, S. and J. Reis, eds. (2010): *State and Financial Systems in Europe and the USA: Historical Perspectives on Regulation and Supervision in the Nineteenth and Twentieth Centuries*, Ashgate.

Baumol, W. J. (1986): "Productivity Growth, Convergence, and Welfare: What the long-run Data Show," *American Economic Review*, 76, 1072–85.

Beck, T., R. Todorov, and W. Wagner (2011): "Bank Supervision Going Global? A Cost-Benefit Analysis," European Banking Center Discussion Paper 2011-033, Tilburg University.

Becker, G. S. (1983): "A Theory of Competition Among Pressure Groups for Political Influence," *The Quarterly Journal of Economics*, 98, 371–400.

Becker, W.-D. (1967): "Der Mythos der Zinsreglementierung," *Zeitschrift für das gesamte Kreditwesen*, 20, 18–20.

Bel, G. (2006): "Retrospectives: The Coining of "Privatization" and Germany's National Socialist Party," *The Journal of Economic Perspectives*, 20, 187–194.

——— (2009): "Against the mainstream: Nazi privatization in 1930s Germany," *Economic History Review*, 63, 34–55.

Benkler, Y. (2009): "Law, Policy and Cooperation," in *Government and Markets: Toward a New Theory of Regulation*, ed. by E. Balleisen and D. Moss, Cambridge University Press.

Bennett, J. (1950): "The German Currency Reform," *Annals of the American Academy of Political and Social Science*, 43–54.

Benston, G. J. (1990): *The Separation of Commercial and Investment Banking: The Glass-Steagall Act Revisited and Reconsidered*, Oxford University Press, New York and Oxford.

Berger, H. (1997): "The Bundesbank's path to independence: Evidence from the 1950s," *Public Choice*, 93, 427–453.

Berger, H. and J. d. Haan (1999): "A State within the State? An Event Study on the Bundesbank (1948–1973)," *Scottish Journal of Political Economy*, 46, 17–39.

Berghahn, V. R. (1986): *The Americanisation of West German Industry 1945–1973*, Berg Publishers Ltd., Leamington Spa / New York.

Berman, D. M. (1964): *In Congress Assembled: The Legislative Process in the National Government*, MacMillan, New York.

Bermann, G. A. (1994): "Taking Subsidiarity Seriously: Federalism in the European Community and the United States," *Columbia Law Review*, 94, pp. 331–456.

Bissing, W. M. F. v. (1933): "Die Schrumpfung des Kapitals und seine Surrogate," in *Untersuchung des Bankwesens 1933, Teil I, Band 1*, Carl Heymanns Verlag, Berlin, 57–112.

Board of Directors of the Federal Deposit Insurance Corporation (1959): *Report to Insured Banks: December 31, 1958 (25th Anniversary)*, Washington D.C.: Federal Deposit Insurance Corporation.

Board of Governors of the Federal Reserve System (1915): "Second Annual Report of the Federal Reserve Board for the Year ending December 31, 1915," available online via FRASER at http://fraser.stlouisfed.org/docs/publications/arfr/1910s/arfr_1915.pdf, last accessed on 28.01.2013.

——— (1931-1932): "Federal Reserve Committee on Branch, Group and Chain Banking," reports that assemble and digest information on branch banking as practiced in the United States and elsewhere, the unit banking system of the country, and the effect of ownership of bank stocks by investment trusts and holding corporations, available online via FRASER at http://fraser.stlouisfed.org/author/?aid=1699, last accessed on 11.03.2013.

——— (1932a): "Bank Suspensions in the United States, 1892–1931," material prepared for the information of the Federal Reserve System by the Federal Reserve Committee on Branch, Group, and Chain Banking, available online via FRASER at http://fraser.stlouisfed.org/docs/historical/federal%20reserve%20history/frcom_br_gp_ch_banking/suspensions_1892-1931.pdf, last accessed on 21.03.2013.

——— (1932b): "Banking Groups and Chains," material prepared for the information of the Federal Reserve System by the Federal Reserve Committee on Branch, Group, and Chain Banking, available online via FRASER at http://fraser.stlouisfed.org/docs/historical/federal%20reserve%

20history/frcom_br_gp_ch_banking/banking_groups_chains.pdf, last accessed on 11.03.2013.

——— (1932c): "Branch Banking in the United States," material prepared for the information of the Federal Reserve System by the Federal Reserve Committee on Branch, Group, and Chain Banking, available online via FRASER at http://fraser.stlouisfed.org/docs/historical/federal%20reserve%20history/frcom_br_gp_ch_banking/branch_banking_us.pdf, last accessed on 05.02.2013.

——— (1932d): "The Dual Banking System in the United States," material prepared for the information of the Federal Reserve System by the Federal Reserve Committee on Branch, Group, and Chain Banking, available online via FRASER at http://fraser.stlouisfed.org/docs/historical/federal%20reserve%20history/frcom_br_gp_ch_banking/dual_banking_system_us.pdf, last accessed on 11.03.2013.

——— (1932e): "Summary of the Reports," material prepared for the information of the Federal Reserve System by the Federal Reserve Committee on Branch, Group, and Chain Banking, available online via FRASER at http://fraser.stlouisfed.org/docs/historical/federal%20reserve%20history/frcom_br_gp_ch_banking/summary_of_reports.pdf, last accessed on 11.03.2013.

——— (1936): "Unification of the Commercial Banking System," confidential memorandum, available online via FRASER at http://fraser.stlouisfed.org/docs/historical/banksusp/unifcomm_bog_193612.pdf, last accessed on 19.04.2012.

——— (1936-1938): "Bank Suspension Study," memoranda on possible means of improvement of the existing banking structure, available online via FRASER at http://fraser.stlouisfed.org/publication/?pid=684, last accessed on 11.03.2013.

——— (1937a): "Branch Banking in the United States," material prepared for a study for the purpose of determining possible means of improving the banking structure, available online via FRASER at https://fraser.stlouisfed.org/docs/historical/banksusp/branbaus_bog_1936.pdf, last accessed on 22.01.2013.

——— (1937b): "Complexities of Banking Laws and Practices Associated with Multiple Banking Jurisdictions," confidential memorandum, available online via FRASER at http://fraser.stlouisfed.org/docs/historical/banksusp/comlawpr_bog_1937.pdf, last accessed on 04.03.2013.

——— (1937c): "Some Competitive Aspects of the Dual Banking System Evidenced By Statutory Changes and Administrative Practices," confidential memorandum, available online via FRASER at http://fraser.stlouisfed.org/docs/historical/banksusp/comasduev_bog_1937_.pdf, last accessed on 04.02.2013.

——— (1939): "Twenty-Fifth Annual Report of the Board of Governors of the Federal Reserve System Covering Operations for the Year 1938," available online via FRASER at http://fraser.stlouisfed.org/docs/publications/arfr/1930s/arfr_1938.pdf, last accessed on 04.03.2013.

——— (1941): "A Plan to Improve Federal Banking Supervision," Confidential Memorandum, possibly written by J.P. Dreibelbis, available online via FRASER at http://fraser.stlouisfed.org/docs/historical/eccles/043_08_0005.pdf, last accessed on 04.03.2013.

——— (1943): *Banking and Monetary Statistics 1914-1941*, Washington: Board of Governors of the Federal Reserve System.

——— (1976): *Banking and Monetary Statistics 1941-1970*, Washington: Board of Governors of the Federal Reserve System.

Borchardt, K. (1976): "Währung und Wirtschaft," in *Währung und Wirtschaft in Deutschland 1876–1975*, ed. by Deutsche Bundesbank, Fritz Knapp Verlag, Frankfurt am Main.

Bordo, M. D. (1985): "Some Historical Evidence 1870–1933 on the Impact and International Transmission of Financial Crises," NBER Working Paper No. 1606.

Borkin, J. (1978): *The Crime and Punishment of IG Farben*, Free Press, New York.

Born, K. E. (1967): *Die deutsche Bankenkrise 1931: Finanzen und Politik*, R. Piper & Co Verlag, München.

——— (1982): "Vom Beginn des Ersten Weltkrieges bis zum Ende der Weimarer Republik," in *Deutsche Bankgeschichte, Band 3*, Institut für bankhistorische Forschung e. V., Fritz Knapp Verlag, Frankfurt am Main, 15–146.

——— (1983): *International Banking in the 19th and 20th Centuries*, Berg Publishers Ltd.

——— (1985): *Wirtschafts- und Sozialgeschichte des Deutschen Kaiserreichs (1867/71–1914)*, Franz Steiner Verlag, Stuttgart.

Bracher, K. D. (1973): *The German Dictatorship: The Origins, Structure and Effects of National Socialism*, original title 'Die deutsche Diktatur: Entstehung, Struktur und Folgen des Nationalsozialismus', first published in 1969, Penguin University Books.

Bradford, D. and B. Eichengreen (1993): "The Marshall Plan: History's Most Successful Structural Adjustment Program," in *Postwar Economic Reconstruction and Lessons for the East Today*, ed. by R. Dornbusch, W. Nölling, and R. Layard, MIT Press.

Bresciani-Turroni, C. (1937): *The Economics of Inflation: A Study of Currency Depreciation in Post-War Germany*, original title 'Le Vicende del Marco Tedesco', first published in 1931, translated by Millicent E. Savers, third impression 1968, John Dickens & Co Ltd, Northampton.

Brunnermeier, M. K., A. Crocket, C. Goodhart, A. D. Persaud, and H. Shin (2009): *The Fundamental Principles of Financial Regulation*, vol. available online at http://www.princeton.edu/~markus/research/papers/Geneva11.pdf, retrieved on 03.03.2010, Geneva Reports on the World Economy 11.

Buchanan, J. M. (1975): *The Limits of Liberty: between anarchy and Leviathan*, University of Chicago Press.

Buchanan, J. M. and G. Tullock (1962): *The Calculus of Consent: Logical Foundation of Constitutional Democracy*, Ann Arbor: University of Michigan Press.

Buchheim, C. (1988): "Die Währungsreform 1948 in Westdeutschland," *Vierteljahrshefte für Zeitgeschichte*, 36, 189–231.

——— (1999): "The Establishment of the Bank deutscher Länder and the West German Currency Reform," in *Fifty Year of the Deutsche Mark: Central Bank and the Currency in Germany since 1948*, Oxford University Press, 55–100.

Buchheim, C. and J. Scherner (2006): "The Role of Private Property in the Nazi Economy: The Case of Industry," *Journal of Economic History*, 66, 390–416.

Bundesgesetzblatt (1949): "Grundgesetz für die Bundesrepublik Deutschland, vom 23. Mai 1949," Teil I, Nr. 1, 1–19.

——— (1952): "Gesetz über den Niederlassungsbereich von Kreditinstituten, vom 31. März, 1952," Teil I, Nr. 15, 217–220.

——— (1956): "Gesetz zur Aufhebung der Beschränkung des Niederlassungsbereiches von Kreditinstituten, vom 24. Dezember, 1956," Teil I, Nr. 54, 1073.

——— (1957a): "Gesetz gegen Wettbewerbsbeschränkungen, vom 27. Juli 1957," Teil I, Nr. 41, 1081–1102.

——— (1957b): "Gesetz über die Deutsche Bundesbank, vom 27. Juli 1957," Teil I, Nr. 33, 745–755.

——— (1961): "Gesetz über das Kreditwesen, vom 10. Juli 1961," Teil I, Nr. 49, 881–898.

Bundesverfassungsgericht (1962): "Urteil vom 24. Juli 1962 – 2 BvF 4, 5/61, 1, 2/62 (BVerfGE 14, 197 - Kreditwesen)," .

Bundesverwaltungsgericht (1958): "Urteil vom 10. Juli 1958 – Aktenzeichen: I C 177/54." .

Burhop, C. (2011a): "The historiography of the 1931 crisis in Germany," *Jahrbuch für Wirtschaftsgeschichte*, 52, 9–27.

——— (2011b): *Wirtschaftsgeschichte des Kaiserreichs 1871–1918*, Vandenhoeck & Ruprecht.

Burns, H. M. (1974): *The American Banking Community and New Deal Banking Reforms 1933-1935*, Greenwood Press.

Büschgen, H. E. (1977): "Die Frage der "Macht der Banken" im Spiegel wirtschafts- und gesellschaftspolitischer Ideologien," *Zweites Beiheft zum Bankhistorisches Archiv*, 21–29.

——— (1982): "Zeitgeschichtliche Problemfelder des Bankwesens der Bundesrepublik Deutschland," in *Deutsche Bankgeschichte, Band 3*, Institut für bankhistorische Forschung e. V., Fritz Knapp Verlag, Frankfurt am Main, 359–409.

——— (1995): "Deutsche Bank from 1957 to the Present: The Emergence of an International Financial Conglomerate," in *The Deutsche Bank 1870–1995*, Weidenfeld & Nicolson, London.

Calomiris, C. W. (1990): "Is Deposit Insurance Necessary? A Historical Perspective," *The Journal of Economic History*, 50, 283–295.

——— (2006a): "The origins of banking panics: Models, facts, and bank regulation," in *U.S. Bank Deregulation in Historical Perspective*, ed. by C. W. Calomiris, Cambridge University Press, paperback version, 93–163.

——— (2006b): "Regulation, industrial structure, and instability in U.S. banking: An historical perspective," in *U.S. Bank Deregulation in Historical Perspective*, ed. by C. W. Calomiris, Cambridge University Press, paperback version, 1–92.

——— (2006c): "The Regulatory Record of the Greenspan Fed," *The American Economic Review*, 96, pp. 170–173.

——— (2009): "Banking Crises and the Rules of the Game," NBER Working Paper No. 15403.

——— (2010): "The Political Lessons of Depression-Era Banking Reform," *Oxford Review of Economic Policy*, 26, 540–560.

Calomiris, C. W. and J. R. Mason (2003): "Fundamentals, Panics, and Bank Distress during the Depression," *The American Economic Review*, 93, pp. 1615–1647.

Calomiris, C. W. and E. N. White (1994): "The Origins of Federal Deposit Insurance," in *The Regulated Economy: A Historical Approach to Political Economy*, ed. by C. Goldin and G. D. Libecap, University of Chicago Press, 145–188.

Calzolari, G. and L. Gyongyi (2011): "Regulation of multinational banks: A theoretical inquiry," *Journal of Financial Intermediation*, 20, 178–198.

Carlin, W. (1996): "West Germand growth and institutions, 1945–90," in *Economic Growth in Europe since 1945*, ed. by N. Crafts and G. Toniolo, Cambridge University Press, 455–497.

Carlson, M. and K. J. Mitchener (2009): "Branch Banking as a Device for Discipline: Competition and Bank Survivorship during the Great Depression," *The Journal of Political Economy*, 117, pp. 165–210.

Carosso, V. (1970): "Washington and Wall Street: The New Deal and Investment Bankers, 1933-1940," *The Business History Review*, 44, pp. 425–445.

Carpenter, D. (2009): "Confidence Games: How Does Regulation Constitute Markets?" in *Government and Markets: Toward a New Theory of Regulation*, ed. by E. Balleisen and D. Moss, Cambridge University Press.

Cassese, S. (1984): "The Long Life of the Financial Institutions Set up in the Thirties," *The Journal of European Economic History*, 13, 273–294.

CCG/BE (1949): *Military Government Gazette Germany - British Zone of Control*, Control Commission for Germany/British Element.

Chandler, L. V. (1958): *Benjamin Strong: Central Banker*, The Brookings Institution, Washington D.C.

Chapman, J. M. and R. B. Westerfield (1942): *Branch Banking: Its Historical and Theoretical Position in America and Abroad*, Harper & Brothers.

Čihák, M. and R. Podpiera (2007): "Experience with Integrated Supervisors: Governance and Quality of Supervision," in *Designing Financial Supervision Institutions: Independence, Accountability and Governance*, ed. by D. Masciandaro and M. Quintyn, Edward Elgar.

Clay, L. D. (1950): *Decision in Germany*, 1970 reprint, Greenwood Press, Westport.

Colvin, C. L. and E. McLaughlin (2012): "Raiffeisenism Abroad: Why did German Microfinance Fail in Ireland but Prosper in the Netherlands?" EUI Working Papers MWP 2012/01.

Council of the European Union (2012): "Press Release, 3214th Council meeting, Economic and Financial Affairs, Brussels, 12 December 2012," 17598/12, available online at http://www.consilium.europa.eu/uedocs/cms_Data/docs/pressdata/en/ecofin/134287.pdf, last accessed on 21.02.2013.

Crafts, N. and G. Toniolo (1996): "Postwar growth: an overview," in *Economic Growth in Europe since 1945*, ed. by N. Crafts and G. Toniolo, Cambridge University Press, 1–37.

Cwik, M. (1970): "Das föderalistische Zentralbanksystem in der Bundesrepublik Deutschland vor 1957 (Bank deutscher Länder – BDL) und ein Vergleich mit dem "Federal Reserve System" der Vereinigten Staaten von Amerika in Hinblick auf die Schaffung eines föderalistischen Zentralbanksystems in Europa," study prepared for the European Commission, DG Economic and Financial Affairs, available online at http://ec.europa.eu/economy_finance/emu_history/documentation/chapter5/19700515de67dasdeutscheoder.pdf, last accessed on 11.03.2013.

Davis, A. M. (1910): *The Origin of the National Banking System*, 61st Congress, 2nd Session, Document No. 582, National Monetary Commission.

Deckers, J. (1974): *Die Transformation des Bankensystems in der sowjetischen Besatzungszone-DDR: von 1945 bis 1952*, Duncker & Humblot, Berlin.

Dell'Ariccia, G. and R. Marquez (2006): "Competition among Regulators and Credit Market Integration," *Journal of Financial Economics*, 79, 401–430.

Dessauer, M. (1935): "The German Bank Act of 1934," *The Review of Economic Studies*, 2, 214–224.

Deumer, R. (1933): "Das deutsche Kreditgenossenschaftswesen," in *Untersuchung des Bankwesens 1933, Teil I, Band 1*, Carl Heymanns Verlag, Berlin, 245–331.

Deutsche Bundesbank (1976): *Deutsches Geld- und Bankwesen in Zahlen, 1876–1975*, Fritz Knapp Verlag, Frankfurt.

——— (1988): *30 Jahre Deutsche Bundesbank: Die Entstehung des Bundesbankgesetzes vom 26. Juli 1957 – Dokumentation einer Ausstellung*, Deutsche Bundesbank.

——— (1998): "The Central Bank Council fifty years ago," in *Monthly Report March 1998*, 17–31.

Deutscher Bundestag (1968): "Bericht der Bundesregierung über Wettbewerbsverschiebungen im Kreditgewerbe und über eine Einlagensicherung, vom 18.11.1968," 5. Wahlperiode, Drucksache V/3500.

——— (1975): "Bericht der Bundesregierung über die Ausnahmebereiche des Gesetzes gegen Wettbewerbsbeschränkungen (GWB)," 7. Wahlperiode, Drucksache 7/3206.

Dewey, D. R. (1910): *State Banking Before the Civil War*, National Monetary Commission, 1–226, 61st Congress, 2nd Session, Document No. 581.

Di Martino, Paolo (2010): "Lobbying, Institutional Inertia, and the Efficency Issue in State Regulation: Evidence from the Evolution of Bankruptcy Laws and Procedures in Italy, England and the US (1870–1939)," in *State and Financial Systems in Europe and the USA: Historical Perspectives on Regulation and Supervision in the Nineteenth and Twentieth Centuries*, ed. by S. Battilossi and J. Reis, Ashgate, 42–54.

Dickhaus, M. (1998): "Fostering 'the bank that rules Europe': the Bank of England, the Allied Banking Commission, and the Bank deutscher Länder, 1948–1951," *Contemporary European History*, 7, 161–179.

Die Zeit (1953): "Bankier Robert Pferdmenges," Ausgabe 42/1953, 15.10.1953, available online at http://www.zeit.de/1953/42/bankier-robert-pferdmenges, retrieved on 09.08.2013.

Döring, F. (1933): "Rückblick auf die Zeit vor dem Kriege und im Kriege," in *Untersuchung des Bankwesens 1933, Teil I, Band 2*, Carl Heymanns Verlag, Berlin, 137–158.

Dorn, W. L. (1957): "The Debate Over American Occupation Policy in Germany in 1944-1945," *Political Science Quarterly*, 72, pp. 481–501.

Dornbusch, R. (1993): "The End of the German Miracle," *Journal of Economic Literature*, 31, pp. 881–885.

Doti, L. P. and L. Schweikart (1991): *Banking in the American West: from the Gold Rush to Deregulation*, University of Oklahoma Press.

Draheim, G. (1966): "Freiheit für Bankzinsen?" *Zeitschrift für das gesamte Kreditwesen*, 19, 30–31.

Dumke, R. H. (1990): "Reassessing the *Wirtschaftswunder*: Reconstruction and Postwar Growth in West Germany in an International Context," *Oxford Bulletin of Economics and Statistics*, 52, 451–492.

Duncan, J. P. (1999): "The Course of Federal Pre-Emption of State Banking Law," *Annual Review of Banking Law*, 18, 221–323.

Economides, N., R. G. Hubbard, and D. Palia (1996): "The Political Economy of Branching Restrictions and Deposit Insurance: A Model of Monopolistic Competition among Small and Large Banks," *Journal of Law and Economics*, 39.

Edwards, J. and S. Ogilvie (1996): "Universal Banks and German Industrialization: A Reappraisal," *The Economic History Review*, 49, pp. 427–446.

Eichengreen, B. (1996): "Institutions and economic growth: Europe after World War II," in *Economic Growth in Europe since 1945*, ed. by N. Crafts and G. Toniolo, Cambridge University Press, 38–72.

Eichengreen, B. and A. Ritschl (2009): "Understanding West German Economic Growth in the 1950s," *Cliometrica, Journal of Historical Economics and Econometric History*, 3, 191–219.

Erhard, L. (1958): *Prosperity through competition*, translated and edited by Edith Temple Roberts and John B. Wood, original German title: "Wohlstand für Alle", Greenwood Press, Westport.

European Commission (2012a): "Commission proposes new ECB powers for banking supervision as part of a banking union," press release IP/12/953 from 12.09.2012, available online at http://europa.eu/rapid/press-release_IP-12-953_en.htm, last accessed on 09.01.2013.

——— (2012b): "Proposal for a Directive of the European Parliament and of the Council establishing a framework for the recovery and resolution of credit institutions and investment firms," available online at http://ec.europa.eu/internal_market/bank/docs/crisis-management/2012_eu_framework/COM_2012_280_en.pdf, last accessed on 06.06.2012.

European Council (2012): "Conclusions of the European Council 13/14 December," EUCO 205/12, available online at http://www.consilium.europa.eu/uedocs/cms_Data/docs/pressdata/en/ec/134353.pdf, last accessed on 21.02.2013.

Fear, J. and C. Kobrak (2006): "Diverging Paths: Accounting for Corporate Governance in America and Germany," *Business History Review*, 80, 1–48.

Federal Deposit Insurance Corporation (1984): *The First Fity Years – A History of the FDIC 1933–1983*, Federal Deposit Insurance Corporation, Washington D.C., available online at http://www.fdic.gov/bank/analytical/firstfifty/, last accessed 21.02.2013.

Federal Financial Supervisory Authority (BaFin) (2011): "2010 Annual Report," available online at http://www.bafin.de/SharedDocs/Downloads/EN/Jahresbericht/dl_annualreport_2010.pdf?__blob=publicationFile, last accessed 11.03.2013.

Federal Reserve Board (1915): "Federal Reserve Bulletin, July 1915," available online via FRASER at http://fraser.stlouisfed.org/docs/publications/FRB/1910s/frb_071915.pdf, last accessed on 12.06.2012.

——— (1924): "Federal Reserve Bulletin, April 1924," available online via FRASER at http://fraser.stlouisfed.org/docs/publications/FRB/1920s/frb_041924.pdf, last accessed on 05.02.2013.

——— (1937): "Federal Reserve Bulletin, August 1937," available online via FRASER at http://fraser.stlouisfed.org/docs/publications/FRB/1930s/frb_081937.pdf, last accessed on 04.03.2013.

——— (2012): "Insured U.S.-Chartered Commercial Banks that have Consolidated Assets of $300 Million or More, Ranked by Consolidated Assets. As of September 30, 2012," Federal Reserve Statistical Release, available online at http://www.federalreserve.gov/releases/lbr/, last accessed on 22.02.2013.

Feijen, E. and E. C. Perotti (2005): "The Political Economy of Financial Fragility," CEPR Discussion Papers 5317, C.E.P.R. Discussion Papers.

Feldkamp, M. F. (1995): "Band 8: Die Beziehungen des Parlamentarischen Rates zu den Militärregierungen," in *Der Parlamentarische Rat 1948–1949: Akten und Protokolle*, ed. by R. Schick and F. P. Kahlenberg, Harald Boldt Verlag, Boppard am Rhein.

Feldkamp, M. F. and I. Müller (1999): "Ausschuß für Finanzfragen," in *Band 12: Der Parlamentarische Rat 1948–1949: Akten und Protokolle*, ed. by H.-J. Stelzl and F. P. Kahlenberg, Harald Boldt Verlag im R. Oldenbourg Verlag, München.

Feldman, G. D. (1981): "German interest group alliances in war and inflation, 1914–1923," in *Organizing interests in Western Europe: Pluralism, corporatism, and the transformation of politics*, ed. by S. Berger, Cambridge University Press.

——— (1984): "Die Sozial- und Wirtschaftspolitik der deutschen Unternehmer 1918–1929," in *Studien zur deutschen Wirtschafts- und Sozialgeschichte 1914–1932*, ed. by G. D. Feldman, Vandenhoeck & Ruprecht, Göttingen.

——— (1993): *The Great Disorder: Politics, Economics, and Society in the German Inflation, 1914-1924*, Oxford University Press, New York and Oxford.

——— (1995): "The Deutsche Bank from World War to World Economic Crisis: 1914–1933," in *The Deutsche Bank 1870–1995*, Weidenfeld & Nicolson, London.

Ferguson, T. and P. Temin (2001): "Made in Germany: The German Currency Crisis of July, 1931," MIT Working Paper 01-07.

Financial Crisis Inquiry Commission (2011): "The Financial Crisis Inquiry Report," U.S. Government Printing Office, available online at http://fcic-static.law.stanford.edu/cdn_media/fcic-reports/fcic_final_report_full.pdf, last accessed 11.03.2013.

Fischer, G. C. (1968): *American Banking Structure*, Columbia University Press.

Fischer, K.-H. and C. Pfeil (2003): "Regulation and Competition in German Banking: An Assessment," CFS Discussion Paper 2003/19, Center for Financial Studies, Johann Wolfgang Goethe-Universität, Frankfurt.

Fischer, O. C. (1933): "Die fehlerhafte Kreditpolitik," in *Untersuchung des Bankwesens 1933, Teil I, Band 1*, Carl Heymanns Verlag, Berlin, 493–538.

Fligstein, N. (2009): "Lessons from Europe: Some Reflections on the European Union and the Regulation of Business," in *Government and Markets: Toward a New Theory of Regulation*, ed. by E. Balleisen and D. Moss, Cambridge University Press.

Fohlin, C. (2002): "Regulation, taxation and the development of the German universal banking system, 1884-1913," *European Review of Economic History*, 6, 221–254.

——— (2007): *Finance Capitalism and Germany's Rise to Industrial Power*, Cambridge University Press.

Franke, G. (1999): "The Bundesbank and Financial Markets," in *Fifty Year of the Deutsche Mark: Central Bank and the Currency in Germany since 1948*, Oxford University Press, 219–266.

——— (2000): "Deutsche Finanzmarktregulierung nach dem Zweiten Weltkrieg zwischen Risikoschutz und Wettbewerbssicherung," CoFE Discussion Paper 00-31, Center of Finance and Econometrics, University of Konstanz.

Freixas, X. (2003): "Crisis Management in Europe," in *Financial Supervision in Europe*, ed. by J. Kremers, D. Schoenmaker, and W. P., Cheltenham: Edward Elgar.

Friedman, M. and A. Schwartz (1963): *A Monetary History of the United States 1867-1960*, ninth paperback reprinting in 1993, Princeton University Press.

Frydman, C., E. Hilt, and Z. L. Y. (2012): "Economic Effects of Runs on Early 'Shadow Banks': Trust Companies and the Impact of the Panic of 1907," NBER Working Paper No. 18264.

Furner, M. O. (2009): "From "State Interference" to the "Return of the Market": The Rhetoric of Economic Regulation from the Old Gilded Age to the New," in *Government and Markets: Toward a New Theory of Regulation*, ed. by E. Balleisen and D. Moss, Cambridge University Press.

Gall, L. (1995): "The Deutsche Bank from its Founding to the Great War: 1870–1914," in *The Deutsche Bank 1870–1995*, Weidenfeld & Nicolson, London.

Gerschenkron, A. (1962): *Economic Backwardness in Historical Perspective*, Cambridge, Massachusetts: Harvard University Press.

Gespräch des Tages (1965): "Schrittweise Freilassung," *Zeitschrift für das gesamte Kreditwesen*, 18, 3.

——— (1967): "Zinsen nach "Orientierungshilfen"," *Zeitschrift für das gesamte Kreditwesen*, 20, 3.

Giersch, H., K.-H. Paqué, and H. Schmieding (1992): *The Fading Miracle: Four Decades of Market Economy in Germany*, Cambridge University Press.

Gilligan, T. W., W. J. Marshall, and B. R. Weingast (1989): "Regulation and the Theory of Legislative Choice: The Interstate Commerce Act of 1887," *Journal of Law and Economics*, 32, pp. 35–61.

Gische, D. M. (1979): "The New York City Banks and the Development of the National Banking System 1860-1870," *The American Journal of Legal History*, 23, pp. 21–67.

Glass, C. (1927): *An Adventure in Constructive Finance*, Doubleday, Page and Company, Garden City, N.Y.

Goldin, C. D. and F. D. Lewis (1975): "The Economic Cost of the American Civil War: Estimates and Implications," *The Journal of Economic History*, 35, pp. 299–326.

Golembe, C. H. (1960): "The Deposit Insurance Legislation of 1933: An Examination of Its Antecedents and its Purposes," *Political Science Quarterly*, 75, pp. 181–200.

——— (1967): "Our Remarkable Banking System," *Virginia Law Review*, 53, pp. 1091–1114.

Goodhart, C. (2002): "The Organizational Structure of Banking Supervision," *Economic Notes*, 31, 1–32.

Goodhart, C. and D. Schoenmaker (2009): "Fiscal Burden Sharing in Cross-Border Banking Crises," *International Journal of Central Banking*, 5, 141–165.

Grossman, R. S. (2010): "The Emergence of Central Banks and Banking Supervision in Comparative Perspective," in *State and Financial Systems in Europe and the USA: Historical Perspectives on Regulation and Supervision in the Nineteenth and Twentieth Centuries*, ed. by S. Battilossi and J. Reis, Ashgate, 123–138.

Grüger, F. (1933): "Die Wirkungen des Krieges und der Kriegsfolgen auf das deutsche Bankwesen mit einem Rückblick auf die Vorkriegszeit," in *Untersuchung des Bankwesens 1933, Teil I, Band 1*, Carl Heymanns Verlag, Berlin, 23–55.

Grunenberg, N. (2006): *Die Wundertäter: Netzwerke der deutschen Wirtschaft 1942 bis 1966*, Sielder.

Gruppe Deutsche Bank (1955): "Geschäftsbericht für das Jahr 1955," Available online at http://www.bankgeschichte.de/downloads/gb/gb_1955.pdf, retrieved on 30.03.2011.

Guinnane, T. W. (1994): "A Failed Institutional Transplant: Raiffeisen's Credit Cooperatives in Ireland, 1894-1914," *Explorations in Economic History*, 31, 38 – 61.

——— (2002): "Delegated Monitors, Large and Small: Germany's Banking System, 1800-1914," *Journal of Economic Literature*, 40, 73–124.

Habedank, H. (1981): *Die Reichsbank in der Weimarer Republik: Zur Rolle der Zentralbank in der Politik des deutschen Imperialismus*, Akademie Verlag, Berlin.

Haber, S. (2007): "Political Institutions and Financial Development: Evidence from the Political Economy of Bank Regulation in Mexico and the United States," in *Political Institutions and Financial Development*, Stanford University Press.

Hackley, H. H. (1966a): "Our Baffling Banking System," *Virginia Law Review*, 52, pp. 565–632.

——— (1966b): "Our Baffling Banking System. Part II," *Virginia Law Review*, 52, pp. 771–830.

——— (1969): "Our Discriminatory Banking Structure," *Virginia Law Review*, 55, pp. 1421–1482.

Haller, H. (1976): "Die Rolle der Staatsfinanzen im Inflationsprozeß," in *Währung und Wirtschaft in Deutschland 1876–1975*, ed. by Deutsche Bundesbank, Fritz Knapp Verlag, Frankfurt am Main.

Hammond, B. (1947): "Jackson, Biddle, and the Bank of the United States," *The Journal of Economic History*, 7, pp. 1–23.

——— (1957): *Banks and politics in America: from the Revolution to the Civil War*, Princeton University Press.

Hammond, P. Y. (1962): "Directives for the Occupation of Germany: The Washington Controversy," in *American Civil-Military Decisions: A Book of Case Studies*, ed. by H. Stein, University of Alabama Press, 311–464.

Hanes, C. and P. W. Rhode (2012): "Harvests and Financial Crises in Gold-Standard America," NBER Working Paper No. 18616.

Hansmeyer, K.-H. (1998): "Das Kreditwesen der Deutschen Besatzungszonen (1945-1948)," in *Geschichte der deutschen Kreditwirtschaft seit 1945*, ed. by H. Pohl, Fritz Knapp Verlag, Frankfurt, 1–22.

Hansmeyer, K.-H. and R. Caesar (1976): "Kriegswirtschaft und Inflation (1936–1948)," in *Währung und Wirtschaft in Deutschland 1876–1975*, ed. by Deutsche Bundesbank, Fritz Knapp Verlag, Frankfurt am Main.

Hardach, G. (1976): *Weltmarktorientierung und relative Stagnation: Währungspolitik in Deutschland 1924-1931*, Duncker & Humblot, Berlin.

——— (1984): "Banking and Industry in Germany in the Interwar Period 1919-1939," *The Journal of European Economic History*, 13, 203–234.

——— (1995a): "Banking in Germany, 1918–1939," in *Banking, Currency, and Finance in Europe Between the Wars*, ed. by C. H. Feinstein, Clarendon Press Oxford, 269–295.

——— (1995b): "Zwischen Markt und Macht: Die deutschen Banken 1908-1934," in *Vierteljahrschrift für Sozial- und Wirtschaftsgeschichte, Beiheft: Wirtschaft, Gesellschaft, Unternehmen. Festschrift für Hans Pohl zum 60. Geburtstag, 2. Teilband*, Franz Steiner Verlag, Stuttgart, 120b.

Hardach, K. (1980): *The Political Economy of Germany in the Twentieth Century*, Translation of Wirtschaftsgeschichte Deutschlands im 20. Jahrhundert, University of California Press.

Harding, W. P. (1925): "The Formative Period of the Federal Reserve System (During the World Crisis)," available online via FRASER at http://fraser.stlouisfed.org/docs/publications/books/formperfrs_harding_1925.pdf, last accessed 05.03.2013.

Harriss, C. L. (1951): *History and Policies of the Home Owners' Loan Corporation*, National Bureau of Economic Research.

Hasse, E. (1933): "Die Krisenmaßnahmen des Jahres 1931," in *Untersuchung des Bankwesens 1933, Teil I, Band 2*, Carl Heymanns Verlag, Berlin, 67–88.

Häuser, K. (1998): "Gründung der Bank deutscher Länder und Währungsreform," in *Geschichte der deutschen Kreditwirtschaft seit 1945*, ed. by H. Pohl, Fritz Knapp Verlag, Frankfurt, 25–58.

Heide, K. (1966): "Lockerung des Zinsdirigismus oder Zinsfreiheit," *Zeitschrift für das gesamte Kreditwesen*, 19, 24–34.

Henckel, H. (1966): "Plädoyer für Freiheit der Bankzinsen," *Zeitschrift für das gesamte Kreditwesen*, 19, 7–11.

Hennig, C. (1930): *Die Struktur der deutschen Reichsbank und ihre Geld- und Kreditpolitik unter der Herrschaft des Dawes-Planes: 1924–1928*, Verlag von Emil Ebering, Berlin.

Hentschel, V. (1988a): "Die Entstehung des Bundesbankgesetzes 1949–1957. Politische Kontroversen und Konflikte (Teil I)," *Bankhistorisches Archiv*, 14, 3–31.

——— (1988b): "Die Entstehung des Bundesbankgesetzes 1949–1957. Politische Kontroversen und Konflikte (Teil II)," *Bankhistorisches Archiv*, 14, 79–115.

——— (1998): *Ludwig Erhard: Ein Politikerleben*, Ullstein, Berlin.

Hildreth, R. (1837): *The History of Banks: to Which is Added, a Demonstration of the Advantages and Necessity of Free Competition in the Business of Banking*, reprinted 1968 by Augustus M. Kelley Publishers, New York, Hilliard, Gray & Company.

HM Treasury (2011): "A new approach to financial regulation: building a stronger system," available online at http://www.hm-treasury.gov.uk/d/consult_newfinancial_regulation170211.pdf, last accessed on 12.06.2012.

Hoffmann, J. (1966): "Liberalisierung hängt am Sparzins," *Zeitschrift für das gesamte Kreditwesen*, 19, 21–30.

Hofmann, W., ed. (1949): *Handbuch des gesamten Kreditwesens*, Fritz Knapp Verlag.

Holdsworth, J. T. and D. R. Dewey (1910): "First and Second Banks of the United States," in *National Monetary Commission*, Government Printing Office, Washington, 61st Congress, 2nd Session, Document No. 571, available online via FRASER, http://fraser.stlouisfed.org/docs/historical/nmc/nmc_571_1910.pdf, last accessed on 11.03.2013.

Holtfrerich, C.-L. (1986): *The German Inflation 1914–1923: Causes and Effects in International Perspective*, Translated by Theo Balderston, Walter de Gruyter, Berlin & New York.

——— (1995): "The Deutsche Bank 1945–1957: War, Military Rule and Reconstruction," in *The Deutsche Bank 1870–1995*, Weidenfeld & Nicolson, London.

Holthausen, C. and T. Rønde (2004): "Cooperation in International Banking Supervision," European Central Bank Working Paper Series, No. 316.

Honold, E. (1956): "Die Bankenaufsicht," Doctoral Dissertation at the Wirtschaftshochschule Mannheim.

Horstmann, T. (1985): "Um "das schlechteste Bankensystem der Welt". Die interalliierten Auseinandersetzungen über amerikanische Pläne zur Reform des deutschen Bankwesens 1945/46," *Bankhistorisches Archiv*, 11, 3–27.

——— (1991): *Die Alliierten und die deutschen Großbanken: Bankenpolitik nach dem Zweiten Weltkrieg in Westdeutschland*, Bouvier Verlag Bonn.

House of Representatives (1913): *Report of the Committee Appointed Pursuant to House Resolutions 429 and 504 to Investigate the Concentration of Control of Money and Credit*, 62nd Congress, Senate, 3d Session, Report No. 1593, 62nd Congress, Senate, 3d Session, Report No. 1593.

Hutchinson, H. D. (1975): *Money, Banking and the United States Economy*, Prentice-Hall, Inc., Englewood Cliffs, New Jersey, 3 ed.

Hüttenberger, P. (1976): "Wirtschaftsordnung und Interessenpolitik in der Kartellgesetzgebung der Bundesrepublik 1949-1957," *Vierteljahrshefte für Zeitgeschichte*, 24, 287–307.

Jalil, A. (2012): "A New History of Banking Panics in the United States, 1825-1929: Construction and Implications," Working paper available online at http://www.reed.edu/economics/jalil/Jalil_ANewHistoryOfBankingPanics.pdf, last accessed 03.04.2013.

James, H. (1984): "The Causes of the German Banking Crisis of 1931," *The Economic History Review*, 37, 68–87.

——— (1985): *The Reichsbank and Public Finance in Germany 1924-1933: A study of the Politics of Economics during the Great Depression*, Schriftenreihe des Instituts für Bankhistorische Forschung E.V., Fritz Knapp Verlag.

——— (1986): *The German Slump: Politics and Economics 1924-1936*, Clarendon Press Oxford.

——— (1995): "The Deutsche Bank and the Dictatorship 1933–1945," in *The Deutsche Bank 1870–1995*, Weidenfeld & Nicolson, London.

——— (2012): *Making the European Monetary Union*, Amazon Kindle Edition, ASIN – B00AFS6LQO, Harvard University Press.

Janberg, H. (1966): "Freiheit für Bankzinsen?" *Zeitschrift für das gesamte Kreditwesen*, 19, 17–21.

Jánossy, F. (1966): *Das Ende der Wirtschaftswunder: Erscheinung und Wesen der wirtschaftlichen Entwicklung*, Verlag Neue Kritik Frankfurt.

——— (1971): *The end of the economic miracle: appearance and reality in economic development*, translation by Hedy D. Jellinek of "Das Ende der Wirtschaftswunder: Erscheinung und Wesen der wirtschaftlichen Entwicklung", published originally by Verlag Neue Kritik, Frankfurt in 1966, International Arts and Sciences Press, White Plains, N.Y.

Jaremski, M. (2010a): "Free Bank Failures: Risky Bonds versus Undiversified Portfolios," *Journal of Money, Credit and Banking*, 42, 1565–1587.

——— (2010b): "State Banks and the National Banking Acts: A Tale of Creative Destruction," Job Market Paper, November 2010, available online at http://www.econ.as.nyu.edu/docs/IO/18865/Jaremski_20110218.pdf, last accessed on 14.02.2013.

Jickling, M. and E. V. Murphy (2010): "CRS Report for Congress: Who Regulates Whom? An Overview of U.S. Financial Supervision," Congressional Research Service, R40249, December 8.

Johnson, C. A. (1995): "Wild Card Statutes, Parity, and National Banks – The Renascence of State Banking Powers," *Loyola University Chicago Law Journal*, 26, 351–404.

Joint Chiefs of Staff (1945): "Directive to Commander-in-Chief of United States Forces of Occupation Regarding the Military Government of Germany (JCS 1067)," available online at http://usa.usembassy.de/etexts/ga3-450426.pdf, retrieved on 07.11.2010.

Joskow, P. L. and R. G. Noll (1981): "Regulation in Theory and Practice: An Overview," in *Studies in Public Regulation*, National Bureau of Economic Research, Inc, 1–78.

Kahn, C. M. and J. A. Santos (2005): "Allocating bank regulatory powers: Lender of last resort, deposit insurance and supervison," *European Economic Review*, 49, 2107–2136.

Kalkstein, H. (1966): "Zur Kritik an der Zinsverordnung," *Zeitschrift für das gesamte Kreditwesen*, 19, 11–13.

Kane, E. J. (1984): "Regulatory Structure in Futures Markets: Jurisdictional Competition between the SEC, the CFTC and Other Agencies," *The Journal of Futures Markets*, 4, 367–384.

——— (1996): "De Jure Interstate Banking: Why Only Now?" *Journal of Money, Credit and Banking*, 28, pp. 141–161.

Kemmerer, E. W. (1910): "Seasonal Variations in the Relative Demand for Money and Capital in the United States: A Statistical Study," in *National Monetary Commission*, Government Printing Office, Washington, 61st Congress, 2nd Session, Document No. 588.

Kennedy, S. E. (1973): *The Banking Crisis of 1933*, University Press of Kentucky.

KITCHEN, M. (1978): *The Political Economy of Germany 1815–1914*, Croom Helm, London.

KITTERER, W. (1999): "Public Finance and the Central Bank," in *Fifty Year of the Deutsche Mark: Central Bank and the Currency in Germany since 1948*, Oxford University Press, 165–217.

KLEIN, E. (1982): "Von den Anfängen bis zum Ende des alten Reiches (1806)," in *Deutsche Bankgeschichte, Band 1*, Institut für bankhistorische Forschung e. V., Fritz Knapp Verlag, Frankfurt am Main.

KLEMM, B. AND G. J. TRITTEL (1987): "Vor dem "Wirtschaftswunder": Durchbruch zum Wachstum oder Lähmungskrise? Eine Auseinandersetzung mit Werner Abelshausers Interpretation der Wirtschaftsentwicklung 1945–1948," *Vierteljahrshefte für Zeitgeschichte*, 35, 571–624.

KLUMP, R. (1985): *Wirtschaftsgeschichte der Bundesrepublik Deutschland: Zur Kritik neuerer wirtschaftshistorischer Interpretationen aus ordnungspolitischer Sicht*, Franz Steiner Verlag, Wiesbaden GmbH.

——— (1996): "Wirtschaftsordnung und Wirtschaftspolitik in der Bundesrepublik Deutschland 1949–1990," in *Wirtschaftsordnung und Wirtschaftspolitik in der Bundesrepublik Deutschland 1933–1993*, ed. by J. Schneider and W. Harbrecht, Franz Steiner Verlag, Stuttgart, Beiträge zur Wirtschafts- und Sozialgeschichte, Nr 63., 397–414.

KNOWLES, E. M., ed. (2001): *The Oxford Dictionary of Quotations*, Oxford University Press, 5th ed.

KOCH, A. AND W. ROEDER, eds. (1938): *Das Recht der deutschen Bankwirtschaft*, Der Betriebswirt, Berlin.

KÖNNECKER, W. (1966): "Die Zinsverordnung, ihre Aufgabe und die Grenzen ihrer Wirksamkeit," *Zeitschrift für das gesamte Kreditwesen*, 19, 13–17.

KOPPER, C. (1995): *Zwischen Marktwirtschaft und Dirigismus: Bankenpolitik im "Dritten Reich" 1933-1939*, Bouvier Verlag Bonn.

——— (2006): *Aufstieg und Fall von Hitlers mächtigstem Bankier*, Hanser.

——— (2011): "New perspectives on the 1931 banking crisis in Germany and Central Europe," *Business History*, 53, 216–229.

Kregel, J. A. (1997): "The Role of 1930s Regulations in the Development of Financial Markets in Postwar United States, Germany and Great Britain," in *Regime Changes: Macroeconomic Policy and Financial Regulation in Europe from the 1930s to the 1990s*, ed. by D. J. Forsyth and T. Notermans, Berghan Books, Providence, Oxford, 256–309.

Kreikamp, H.-D. (1977): "Die Entflechtung der I.G. Farbenindustrie A.G. und die Gründung der Nachfolgegesellschaften," *Vierteljahrshefte für Zeitgeschichte*, 25, 220–251.

Kroszner, R. S. (2001): "The Motivations Behind Banking Reform: Why do Lawmakers pursue deregulation?" *Regulation*, 24, 36–41.

Kroszner, R. S. and R. G. Rajan (1994): "Is the Glass-Steagall Act Justified? A Study of the U.S. Experience with Universal Banking Before 1933," *The American Economic Review*, 84, pp. 810–832.

——— (1997): "Organization structure and credibility: Evidence from commercial bank securities activities before the Glass-Steagall Act," *Journal of Monetary Economics*, 39, 475 – 516.

Kroszner, R. S. and P. E. Strahan (1999): "What Drives Deregulation? Economics and Politics of the Relaxation of Bank Branching Restrictions," *The Quarterly Journal of Economics*, 114, pp. 1437–1467.

——— (2001): "Obstacles to Optimal Policy: The Interplay of Politics and Economics in Shaping Bank Supervision and Regulation Reforms," in *Prudential Supervision: What Works, What Doesn't*, ed. by F. S. Mishkin, University of Chicago Press, 232–272.

Kroszner, R. S. and T. Stratmann (1998): "Interest-Group Competition and the Organization of Congress: Theory and Evidence from Financial Services' Political Action Committees," *American Economic Review*, 88, 1163–1187.

Künsberg, A. (2012): *Vom "Heiligen Geister der Elektrizitätswirtschaft" – Der Kampf um die Regulierung der Strompreiswirtschaft in der Bundesrepublik Deutschland*, Berliner Wissenschafts-Verlag.

KUNZ, J. L. (1950): "The Status of Occupied Germany under International Law: A Legal Dilemma," *The Western Political Quarterly*, 3, 538–565.

LA PORTA, R., F. LOPEZ-DE-SILANES, AND A. SCHLEIFER (2002): "Government Ownership of Banks," *Journal of Finance*, 57, 265–301.

LAFFONT, J.-J. AND D. MARTIMORT (1999): "Separation of regulators against collusive behavior," *RAND Journal of Economics*, 30, 232–262.

LAFFONT, J.-J. AND J. POUYET (2003): "The subsidiarity bias in regulation," *Journal of Public Economics*, 88, 255–283.

LAFFONT, J.-J. AND J. TIROLE (1991): "The Politics of Government Decision-Making: A Theory of Regulatory Capture," *The Quarterly Journal of Economics*, 106, 1089–1127.

LAITENBERGER, V. (1986): *Ludwig Erhard: der Nationalökonom als Politiker*, Muster-Schmidt Verlag, Göttingen.

LAUGHLIN, L. J. (1912): *Banking Reform*, The National Citizens' League, Chicago.

LEE, G. A. (1951): "The Establishment of the Office of the U.S. High Commissioner for Germany," in *Germany – Territory under Allied Occupation, 1944-1955: U.S. Zone*, Office of the United States High Commissioner for Germany. Office of the Executive Secretary, Historical Division, Bad Godesberg-Mehlem.

LEGLER, J. B., R. SYLLA, AND J. J. WALLIS (1987): "Banks and State Public Finance in the New Republic: The United States, 1790–1860," *The Journal of Economic History*, 47, 391–403.

——— (1994): "The Interaction of Taxation and Regulation in Nineteenth-Century U.S. Banking," in *The Regulated Economy: A Historical Approach to Political Economy*, ed. by C. Goldin and G. D. Libecap, University of Chicago Press, 121–144.

LEIGHT, J. (2009): "Public Choice: A Critical Reassessment," in *Government and Markets: Toward a New Theory of Regulation*, ed. by E. Balleisen and D. Moss, Cambridge University Press.

LINDLAR, L. (1997): *Das mißverstandene Wirtschaftswunder*, Mohr Siebeck.

Lo, A. W. (2012): "Reading About the Financial Crisis: A Twenty-One-Book Review," *Journal of Economic Literature*, 50, 151–178.

Loehr, R. C. (1952): "The West German banking system," in *Germany – Territory under Allied Occupation, 1944-1955: U.S. Zone*, Office of the United States High Commissioner for Germany. Office of the Executive Secretary, Historical Division, Bad Godesberg-Mehlem.

Löffler, B. (2002): *Soziale Marktwirtschaft und administrative Praxis: Das Bundeswirtschaftsministerium unter Ludwig Erhard*, Franz Steiner Verlag, Stuttgart, Vierteljahrschrift für Sozial- und Wirtschaftsgeschichte, Beiheft Nr. 162.

Looff, R. (1973): *Die Auswirkungen der Zinsliberalisierungen in Deutschland*, Duncker & Humblot, Berlin.

Luther, H. (1964): *Vor dem Abgrund 1930-1933: Reichsbankpräsident in Krisenzeiten*, Propyläen Verlag, Berlin.

Macey, J. R. (1984): "Special Interest Groups Legislation and the Judicial Function: The Dilemma of Glass-Steagall," *Emory Law Journal*, 33, 1–40.

Macey, J. R. and G. P. Miller (1992): "Double Liability of Bank Shareholders: History and Implications," *Wake Forrest Law Review*, 23, 31–62.

Machiavelli, N. (1950): *The Prince and the Discourses*, translated by Luigi Ricci, revised by E.R.P. Vincent, The Modern Library, Random House Inc.

Manâa, M. (2011): "Die Wirtschaftskrise von 1931 als Wendepunkt? Deutschlands Weg vom organisierten zum regulierten Kapitalismus," *Jahrbuch für Wirtschaftsgeschichte*, II, 95–116.

Manz, M. (1968): *Stagnation und Aufschwung in der französischen Besatzungszone von 1945 bis 1948*, PhD Dissertation at the University of Mannheim.

Markham, J. W. (2002): *A Financial History of the United States: Volume I - From Christopher Columbus to the Robber Barons (1492–1900)*, M.E. Sharpe.

Marsh, D. (1992): *The Bundesbank*, Heinemann, London.

Martin, J. S. (1950): *All Honorable Men*, Little, Brown and Company.

Masciandaro, D. (2009): "Politicians and financial supervision unification outside the central bank: Why do they do it?" *Journal of Financial Stability*, 5, 124–146.

McJimsey, G. T. (2001): "The Bank Holiday and the Emergency Banking Act, March 1933," in *Documentary History of the Franklin D. Roosevelt presidency*, University Publications of America, vol. 3.

Meltzer, A. H. (2003): *A History of the Federal Reserve*, The University of Chicago Press.

Meyer, J. R., M. Peck, J. Stenason, and C. Zwick (1959): *The Economics of Competition in the Transportation Industries*, Harvard University Press.

Mierzejewski, A. C. (2004): *Ludwig Erhard: A Biography*, The University of North Carolina Press, Chapel Hill and London.

Million, J. W. (1894): "The Debate on the National Bank Act of 1863," *Journal of Political Economy*, 2, pp. 251–280.

Miron, J. A. (1986): "Financial Panics, the Seasonality of the Nominal Interest Rate, and the Founding of the Fed," *The American Economic Review*, 76, pp. 125–140.

Mishkin, F. S. (2010): *The Economics of Money, Banking and Financial Markets*, Pearson, ninth global ed.

Mitchener, K. J. and G. Richardson (2013): "Does "Skin in the Game" Reduce Risk Taking? Leverage, Liability and the Long-Run Consequences of New Deal Banking Reforms," NBER Working Paper No. 18895.

Moen, J. and E. W. Tallman (1992): "The Bank Panic of 1907: The Role of Trust Companies," *The Journal of Economic History*, 52, pp. 611–630.

——— (1999): "Why didn't the United States establish a central bank until after the panic of 1907?" Working Paper 99-16, Federal Reserve Bank of Atlanta.

——— (2000): "Clearinghouse Membership and Deposit Contraction during the Panic of 1907," *The Journal of Economic History*, 60, pp. 145–163.

Moltmann, G. (1967): "Zur Formulierung der amerikanischen Besatzungspolitik in Deutschland am Ende des Zweiten Weltkrieges," *Vierteljahrshefte für Zeitgeschichte*, 15, pp. 299–322.

Morgenthau, Henry, J. (1945): *Germany is Our Problem*, Harper & Brothers.

——— (1946): "Postwar Treatment of Germany," *Annals of the American Academy of Political and Social Science*, 246, pp. 125–129.

Möschel, W. (1972): *Das Wirtschaftsrecht der Banken; Die währungs-, bankaufsicht-, kartell- und EWG-rechtliche Sonderstellung der Kreditinstitute*, Athenäum Verlag.

Moss, D. and J. Cisternino, eds. (2009): *New Perspectives on Regulation*, One Mifflin Place, Cambridge, Cambridge, MA 02138, USA: The Tobin Project.

Moss, D. and M. Oey (2009): "The Paranoid Style in the Study of American Politics," in *Government and Markets: Toward a New Theory of Regulation*, ed. by E. Balleisen and D. Moss, Cambridge University Press.

Müller, C. (2003): *Die Entstehung des Reichsgesetzes über das Kreditwesen vom 5. Dezember 1934*, Duncker & Humblot, Berlin.

Müller, F. (1933): "Stabilisierung und Sicherung der Währung (einschl. Kontingentierung)," in *Untersuchung des Bankwesens 1933, Teil I, Band 2*, Carl Heymanns Verlag, Berlin, 187–214.

Murach-Brand, L. (2004): *Antitrust auf deutsch: Der Einfluß der amerikanischen Alliierten auf das Gesetz gegen Wettbewerbsbeschränkungen (GWB) nach 1945*, Mohr Siebeck.

Muthesius, V. (1966): ""Ideologie" oder Erfahrung?" *Zeitschrift für das gesamte Kreditwesen*, 19, 1–3.

——— (1967): "Jacta Est Alea," *Zeitschrift für das gesamte Kreditwesen*, 20, 1–3.

National Monetary Commission (1908-1913): "Documents of the National Monetary Commission," available online via FRASER at http://fraser.stlouisfed.org/topics/?tid=13, last accessed on 11.03.2013.

——— (1910a): *German Bank Inquiry of 1908 - Stenographic Reports: Proceedings of the Entire Commission on Points I to V of the Question Sheet*, 61st Congress, 2nd Session, Document No. 407, Government Printing Office, Washington.

——— (1910b): *Miscellaneous Articles on German Banking*, 61st Congress, 2nd Session, Document No. 407, Government Printing Office, Washington.

——— (1911): *German Bank Inquiry of 1908-9 - Stenographic Reports, Vol. II: Proceedings of the Entire Commission on Point VI of the Question Sheet*, 61st Congress, 2nd Session, Document No. 407.

——— (1912): *Letter From Secretary of the National Monetary Commission Transmitting, Pursuant to Law, the Report of the Commission from January 9, 1912*, 62nd Congress, Senate, 2nd Session, Document No. 243, Government Printing Office, Washington.

Natter, R. and K. Wechsler (2012): "Dodd-Frank Act and National Bank Preemption: Much Ado About Nothing," *Virginia Law Review & Business Review*, 7, 301–364.

Neal, L. (1971): "Trust Companies and Financial Innovation, 1897-1914," *The Business History Review*, 45, pp. 35–51.

Neumann, E. (1933): "Die deutschen Sparkassen," in *Untersuchung des Bankwesens 1933, Teil I, Band 1*, Carl Heymanns Verlag, Berlin, 333–359.

Nordhoff, K. (1933a): "Die Maßnahmen der Reichsbank zur Verbesserung der Publizität, Liquidität und Solidarität der Banken," in *Untersuchung des Bankwesens 1933, Teil I, Band 2*, Carl Heymanns Verlag, Berlin, 243–268.

——— (1933b): "Über die Liquiditätsfrage," in *Untersuchung des Bankwesens 1933, Teil I, Band 1*, Carl Heymanns Verlag, Berlin, 475–491.

Odell, K. A. and M. D. Weidenmier (2004): "Real Shock, Monetary Aftershock: The 1906 San Francisco Earthquake and the Panic of 1907," *Journal of Economic History*, 64, 1002–1024.

Olson, M. (1971): *The Logic of Collective Action: Public Goods and the Theory of Groups*, Harvard University Press, revided edition ed.

——— (1982): *The Rise and Decline of Nations: Economic Growth, Stagflation, and Social Rigidities*, Yale University Press.

——— (1996): "The Varieties of Eurosclerosis: the Rise and Decline of Nations since 1982," in *Economic Growth in Europe since 1945*, ed. by N. Crafts and G. Toniolo, Cambridge University Press, 73–94.

OMGUS (1949a): *Military Government Gazette Germany - United States Area of Control*, Office of the Military Government for Germany (U.S.).

——— (1949b): *Monthly Report of Military Governor US Zone - Finance, No. 1–32*, Office of the Military Government for Germany (U.S.).

Padoa-Schioppa, T. (1999): "EMU and banking supervision," lecture at the London School of Economics, Financial Markets Group on 24 February 1999, available online at https://www.ecb.int/press/key/date/1999/html/sp990224.en.html, last accessed 21.03.2013.

Paersch, F. (1933): "Maßnahmen des Staates hinsichtlich einer Beaufsichtigung und Reglementierung des Bankwesens," in *Untersuchung des Bankwesens 1933, Teil I, Band 2*, Carl Heymanns Verlag, Berlin, 31–66.

Paqué, K.-H. (1993): "How Clean Was the Slate? Some Notes on the Olsonian View of the Postwar German Economic Miracle," Kiel Working Papers, No. 588.

——— (1996): "Why the 1950s and not the 1920s? Olsonian and non-Olsonian interpretations of two decades of German economic history," in *Economic Growth in Europe since 1945*, ed. by N. Crafts and G. Toniolo, Cambridge University Press, 95–106.

Partridge, M. J. C. G. (2011): "Competition Policy in Occupied West Germany and Japan 1945-55: Context, Aims, Narrative and Case Studies," Ph.D. thesis, The London School of Economics and Political Science.

Paulson, H. M. (2010): *On the Brink: Inside the Race to Stop the Collapse of the Global Financial System*, Headline Publishing Group.

Peltzman, S. (1976): "Toward a More General Theory of Regulation," *Journal of Law and Economics*, 19, 211–240.

——— (1989): "The Economic Theory of Regulation after a Decade of Deregulation," *Brookings Papers on Economic Activity. Microeconomics*, pp. 1–41.

Perino, M. (2010): *The Hellhound of Wall Street: How Ferdinand Pecora's Investigation of the Great Crash Forever Changed American Finance*, The Penguin Press.

Pfleiderer, O. (1976): "Die Reichsbank in der Zeit der großen Inflation, die Stabilisierung der Mark und die Aufwertung von Kapitalforderungen," in *Währung und*

Wirtschaft in Deutschland 1876–1975, ed. by Deutsche Bundesbank, Fritz Knapp Verlag, Frankfurt am Main.

Pierce, J. L. (1977): "The FINE Study," *Journal of Money, Credit and Banking*, 9, pp. 605–618.

Pigou, A. C. (1932): *The Economics of Welfare*, London: Macmillan and Co., 4th edition ed.

Plischke, E. (1952): "Allied High Commission Relations with the West German Government," in *Germany – Territory under Allied Occupation, 1944-1955: U.S. Zone*, Office of the United States High Commissioner for Germany. Office of the Executive Secretary, Historical Division, Bad Godesberg-Mehlem.

Plumpe, G. (1990): *Die I.G. Farbenindustrie AG: Wirtschaft, Technik und Politik 1904–1945*, Duncker & Humblot, Berlin.

Pohl, H. (1982a): "Das deutsche Bankwesen (1806–1848)," in *Deutsche Bankengeschichte*, Institut für bankhistorische Forschung e. V., Fritz Knapp Verlag, Frankfurt am Main, vol. Band 2, 11–142.

Pohl, H., ed. (1998): *Geschichte der deutschen Kreditwirtschaft seit 1945*, Fritz Knapp Verlag, Frankfurt.

Pohl, H. and G. Jachmich (1998): "Verschärfung des Wettbewerbs (1966–1973)," in *Geschichte der deutschen Kreditwirtschaft seit 1945*, ed. by H. Pohl, Fritz Knapp Verlag, Frankfurt, 203–248.

Pohl, H., B. Rudolph, and G. Schulz (2005): *Wirtschafts- und Sozialgeschichte der deutschen Sparkassen im 20. Jahrhundert*, Deutscher Sparkassenverlag.

Pohl, M. (1982b): "Die Entwicklung des deutschen Bankwesens zwischen 1848 und 1870," in *Deutsche Bankgeschichte, Band 2*, Institut für bankhistorische Forschung e. V., Fritz Knapp Verlag, Frankfurt am Main, 143–220.

——— (1982c): "Festigung und Ausdehnung des deutschen Bankwesen zwischen 1870 und 1914," in *Deutsche Bankgeschichte, Band 2*, Institut für bankhistorische Forschung e. V., Fritz Knapp Verlag, Frankfurt am Main, 221–356.

——— (1982d): *Konzentration im deutschen Bankwesen*, Fritz Knapp Verlag, Frankfurt am Main.

Poole, K. T. and H. Rosenthal (1993): "The Enduring Nineteenth-Century Battle for Economic Regulation: The Interstate Commerce Act Revisited," *Journal of Law and Economics*, 36, pp. 837–860.

President of the United States (1931): *Message of the President of the United States: Communicated to the two Houses of Congress at the Beginning of the First Session of the Seventy-Second Congress*, United States Government Printing Office, Washington.

Preston, H. H. (1933): "The Banking Act of 1933," *The American Economic Review*, 23, pp. 585–607.

Prollius, M. v. (2006): *Deutsche Wirtschaftsgeschichte nach 1945*, Vandenhoeck & Ruprecht.

Puppo, R. (1988): *Die Wirtschaftsrechtliche Gesetzgebung des Dritten Reichs*, Hartung-Gorre Verlag.

Quityn, M., S. Ramirez, and M. W. Taylor (2007): "The Fear of Freedom. Politicians and the Independence and Accountability of Financial Supervisory," in *Designing Financial Supervision Institutions: Independence, Accountability and Governance*, ed. by D. Masciandaro and M. Quintyn, Edward Elgar.

Rajan, R. G. and R. Ramcharan (2009): "Land and Credit: A Study of the Political Economy of Banking in the United States in the Early 20th Century," NBER Working Paper No. 15083.

Redlich, F. (1947): *The Molding of American Banking: Men and Ideas - Part I (1781–1840)*, Hafner Publishing Company, Inc.

——— (1951): *The Molding of American Banking: Men and Ideas - Part II (1840–1910)*, Hafner Publishing Company, Inc.

Reichsbank (1933a): *Untersuchung des Bankwesens 1933, Teil I, Band 1*, Carl Heymanns Verlag, Berlin.

——— (1933b): *Untersuchung des Bankwesens 1933, Teil I, Band 2*, Carl Heymanns Verlag, Berlin.

Reichsgesetzblatt (1871): "Gesetz betreffend die Verfassung des Deutschen Reiches," Band 1871, Nr. 16, 63–85.

——— (1875): "Bankgesetz. Vom 14. März 1875," Nr. 15, 177–198.

——— (1889): "Gesetz, betreffend die Erwerbs- und Wirtschaftsgenossenschaften. Vom 1. Mai 1889." Nr. 11, 55–93.

——— (1899): "Hypothekenbankgesetz. Vom 13. Juli 1899." Teil I, 375–391.

——— (1919): "Gesetz gegen die Kapitalflucht. Vom 8. September 1919." 1540–1542.

——— (1920a): "Gesetz gegen die Kapitalflucht. Vom 24. Dezember 1920." 33–42.

——— (1920b): "Zweite Verordnung über Maßnahmen gegen die Kapitalflucht. Vom 14. Januar 1920," 50–54.

——— (1921): "Gesetz betreffend Abänderung des Gesetzes gegen die Kapitalflucht. vom 24. Dezember 1920. Vom 4. Juli 1921." 808.

——— (1922a): "Gesetz über die Autonomie der Reichsbank. Vom 26. Mai 1922." Teil II, Nr. 8, 135–136.

——— (1922b): "Gesetz zur Abänderung des Gesetzes gegen die Kapitalflucht. Vom 22. März 1922." Teil I, 282.

——— (1922c): "Gesetz zur Ergänzung und Abänderung des Gesetzes gegen die Kapitalflucht. Vom 22. Dezember 1922." Teil I, 968–971.

——— (1923): "Bekanntmachung der Fassung des Gesetzes gegen die Kapitalflucht. Vom 26. Januar 1923." Teil I, Nr. 9, 968–971.

——— (1924a): "Bankgesetz. Vom 30. August 1924," Teil II, Nr. 32, 235–246.

——— (1924b): "Verordnung des Reichspräsidenten auf Grund des Artikel 48 der Reichsverfassung über die Aufrechterhaltung von Vorschriften des Kapitalfluchtgesetzes und des Weinsteuergesetzes. Vom 29. Dezember 1924." Teil I, Nr. 77, 967.

——— (1925a): "Gesetz über Depot- und Depositengeschäfte. Vom 26. Juni 1925," Teil I, Nr. 27, 89–91.

——— (1925b): "Gesetz über die Aufrechterhaltung von Vorschriften des Kapitalfluchtgesetzes. Vom 16. April 1925." Teil I, Nr. 15, 43.

——— (1926): "Gesetz zur Änderung des Bankgesetzes. Vom 8. Juli 1926," Teil II, Nr. 30, 355.

——— (1930): "Gesetz zur Änderung des Bankgesetzes. Vom 13. März 1930," Teil II, Nr. 7, 355–356.

——— (1931a): "Dritte Verordnung des Reichspräsidenten zur Sicherung von Wirtschaft und Finanzen und zur Bekämpfung politischer Auschreitungen. Vom 6. Oktober 1931." Teil I, Nr. 67, 537–568.

——— (1931b): "Verordnung des Reichspräsidenten über Aktienrecht, Bankenaufsicht und über eine Steueramnestie. Vom 19. September 1931," Teil I, Nr. 63, 493–509.

——— (1931c): "Vierte Verordnung des Reichspräsidenten zur Sicherung von Wirtschaft und Finanzen und zum Schutze des inneren Friedens. Vom 8. Dezember 1931." Teil I, Nr. 79, 699–745.

——— (1934): "Reichsgesetz über das Kreditwesen. Vom 5. Dezember 1934," Teil I, Nr. 132, 1203–1214.

——— (1939a): "Reichsgesetz über das Kreditwesen. Vom 25. September 1939," Teil I, Nr. 192, 1955–1964.

——— (1939b): "Verordnung zur Änderung des Reichsgesetzes über das Kreditwesen. Vom 15. September 1939," Teil I, Nr. 19, 1953–1954.

——— (1940): "Verordnung zur Änderung des Reichsgesetzes über das Kreditwesen. Vom 23. Juli 1940," Teil I, Nr. 135, 1047.

——— (1944): "Verordnung zur Änderung des Reichsgesetzes über das Kreditwesen. Vom 18. September 1944," Teil I, Nr. 45, 211–213.

Reinhardt, S. (2000): *Die Reichsbank in der Weimarer Republik*, Peter Lang.

Rezende, M. (2012): "The Effects of Bank Regulator Switching on Supervisory Ratings," Board of Governors of the Federal Reserve System, mimeo September 2012.

Rheinstein, M. (1948): "The Legal Status of Occupied Germany," *Michigan Law Review*, 47, 23–40.

Riesser, J. (1911): *The German Great Banks and their Concentration*, 61st Congress, 2nd Session, Document No. 593, National Monetary Commission.

Ritschl, A. (2002): "Deutschlands Krise und Konjunktur 1924-1934," in *Jahrbuch für Wirtschaftsgeschichte, Beiheft 2*, Akademie Verlag, Berlin.

——— (2004): "Der lange Schatten des Hjalmar Schachts: Zu den langfristigen Wirkungen des Dritten Reichs auf die Wirtschaftsordnung Deutschlands seit dem Kriege," *Vierteljahrschrift zur Sozial- und Wirtschaftsgeschichte*, 6, 409–493.

——— (2005): "Der späte Fluch des Dritten Reichs: Pfadabhängigkeiten in der Entstehung der bundesdeutschen Wirtschaftsordnung," *Perspektiven der Wirtschaftspolitik*, 6, 151–170.

——— (2012): "Reparations, Deficits and Debt Default: The Great Depression in Germany," Economic History Working Paper 163/12, London School of Economics.

Ritschl, A. and S. Sarferaz (2010): "Crisis? What Crisis? Currency vs. Banking in the Financial Crisis of 1931," SFB 649 Discussion Paper No. SFB649DP2010-014.

Ritter von Georg, J. (2013): *Die Entstehung des Kreditwesengesetzes von 1961*, Europäische Hochschulschriften, Peter Lang.

Robertson, J. L. (1966): "Federal Regulation of Banking: A Plea for Unification," *Law and Contemporary Problems*, 31, pp. 673–695.

Robertson, R. M. (1968): *The Comptroller and Bank Supervision: A Historical Appraisal*, The Office of the Comptroller of the Currency, Washington D.C.

Rockoff, H. (1974): "The Free Banking Era: A Reexamination," *Journal of Money, Credit and Banking*, 6, pp. 141–167.

Rodkey, R. G. (1934): "Banking Reform by Statute," *Michigan Law Review*, 32, 881–908.

Rodrik, D. (2007): *One Economics, Many Recipes Globalization, Institutions, and Economic Growth*, Princeton University Press.

ROSEN, R. J. (2003): "Is Three a Crowd? Competition among Regulators in Banking," *Journal of Money, Credit and Banking*, 35, pp. 967–998.

ROUSSEAU, P. L. (2002): "Jacksonian Monetary Policy, Specie Flows, and the Panic of 1837," *The Journal of Economic History*, 62, 457–488.

SAMUELSON, P. A. (1954): "The Pure Theory of Public Expenditure," *The Review of Economics and Statistics*, 36, 387–389.

SARGENT, T. J. (2012): "Nobel Lecture: United States Then, Europe Now," *Journal of Political Economy*, 120, pp. 1–40.

SCHACHNER, D. R. (1910): "The State and Communal Savings Bank Legislation of Recent Times," in *Miscellaneous Articles on German Banking*, National Monetary Commission, 61st Congress, 2nd Session, Document No. 407, 417–428.

SCHACHT, H. (1934): "Nationalsozialistische Bankreform," Vortrag im Institut für Weltwirtschaft an der Universität Kiel am 26. Januar 1934.

SCHÄFFER, H. (2008): "Marcus Wallenberg und die Deutsche Bankenkrise 1931 – ein Insider berichtet: Marcus Wallenberg zum 5. März 1939," in *Wirtschafts- und Bankenkrise: 1929/31 und notwendige Einsichten für Heute*, Verlag Edmund Steinschulte, 5–113.

SCHLESINGER, ARTHUR, M. (1960): *The Age of Roosevelt, Volume 2: The Coming of the New Deal*, William Heinemann Ltd.

SCHNABEL, I. (2004): "The German Twin Crisis of 1931," *The Journal of Economic History*, 64, 822–871.

——— (2005): "The Role of Liquidity and Implicit Guarantees in the German Twin Crisis of 1931," Working Paper Series of the Max Planck Institute for Research on Collective Goods 2005-5, Max Planck Institute for Research on Collective Goods.

SCHOENMAKER, D. (2011): "The financial trilemma," *Economic Letters*, 111, 57–59.

SCHREIHAGE, H. (1961): "Das neue Gesetz über das Bankwesen," *Zeitschrift für das gesamte Kreditwesen*, 14, 9–12.

SCHWEIKART, L. (1987): *Banking in the American South: from the Age of Jackson to Reconstruction*, Louisiana State University Press.

——— (1991): "U.S. Commercial Banking: A Historiographical Survey," *The Business History Review*, 65, 606–661.

SCOTT, K. E. (1977): "The Dual Banking System: A Model of Competition in Regulation," *Stanford Law Review*, 30, pp. 1–50.

SEEGER, M. (1968): *Die Politik der Reichsbank von 1876–1914*, Duncker & Humblot, Berlin.

SHENG, A. (2009): *From Asian to Global Financial Crisis: An Asian Regulator's View of Unfettered Finance in the 1990s and 2000s*, Cambridge University Press.

SHERMAN, J. (1895): *Recollections of Forty Years in the House, Senate and Cabinet*, Sampson Low, Marston & Company.

SHLEIFER, A. (1994): "Politicians and Firms," *The Quarterly Journal of Economics*, 109, 995–1025.

SIMON, M. C. (1998): "The Rise and Fall of Bank Control in the United States: 1890-1939," *The American Economic Review*, 88, pp. 1077–1093.

SMITH, J. E., ed. (1974): *The Papers of General Lucius D. Clay – Germany 1945-1949*, vol. 1, Indiana University Press.

SOLOW, R. M. (1957): "Technical Change and the Aggregate Production Function," *The Review of Economics and Statistics*, 39, 312–320.

SPEER, A. (1933): "Die Inflationszeit," in *Untersuchung des Bankwesens 1933, Teil I, Band 2*, Carl Heymanns Verlag, Berlin, 159–186.

SPRAGUE, O. M. W. (1903): "Branch Banking in the United States," *The Quarterly Journal of Economics*, 17, pp. 242–260.

——— (1910): "History of Crises under the National Banking System," in *National Monetary Commission*, Government Printing Office, Washington, 61st Congress, 2nd Session, Document No. 538.

——— (1913): *Banking Reform in the United States: A Series or Proposals including a Central Bank of limited scope*, Harvard University Press, Cambridge.

Stern, K. (1999): "The Note-Issuing Bank within the State Structure," in *Fifty Year of the Deutsche Mark: Central Bank and the Currency in Germany since 1948*, Oxford University Press, 103–164.

Stigler, G. J. (1971): "The Theory of Economic Regulation," *The Bell Journal of Economics and Management Science*, 2, 3–21.

Stigler, G. J. and C. Friedland (1962): "What Can Regulators Regulate? The Case of Electricity," *Journal of Law and Economics*, 5, 1–16.

Stolleis, M. (2008): "Besatzungsherrschaft und Wiederaufbau deutscher Staatlichkeit 1945-1949," in *Handbuch des Staatsrechts - Band I: Historische Grundlagen*, ed. by J. Isensee and P. Kirchhof, C.F. Müller, chap. 7, 269–313.

Sylla, R. (1969): "Federal Policy, Banking Market Structure, and Capital Mobilization in the United States, 1863-1913," *The Journal of Economic History*, 29, pp. 657–686.

——— (1999): "Shaping the US financial system, 1690–1913: the dominant role of public finance," in *The State, the Financial System and Economic Modernization*, ed. by R. Sylla, R. Tilly, and G. Tortella, Cambridge University Press.

Sylla, R., R. Tilly, and G. Tortella, eds. (1999): *The State, the Financial System and Economic Modernization*, Cambridge University Press.

Temin, P. (1976): *Did Monetary Forces Cause the Great Depression?*, W. W. Norton, New York.

——— (1991): "Soviet and Nazi Economic Planning in the 1930s," *Economic History Review*, 44, 573–93.

——— (2002): "The Golden Age of European growth reconsidered," *European Review of Economic History*, 6, 3–22.

——— (2008): "The German crisis of 1931: Evidence and Tradition," *Cliometrica, Journal of Historical Economics and Econometric History*, 2, 5–17.

TEWAAG, C. (1933): "Versuche zur Beeinflussung des Kapitalmarktes," in *Untersuchung des Bankwesens 1933, Teil I, Band 2*, Carl Heymanns Verlag, Berlin, 119–133.

THE ECONOMIST (1934): "Nazi Banking Policy Abandoned," December 8, 1934, page 1091, The Economist Historical Archive, available online at http://find.galegroup.com/econ/infomark.do?&source=gale&prodId=ECON&userGroupName=lse_ttda&tabID=T003&docPage=article&docId=GP4100634174&type=multipage&contentSet=LTO&version=1.0, retrieved on 29.11.2012.

——— (2012a): "The Dodd-Frank act: Too big not to fail," from the print edition, February 18th, available online at http://www.economist.com/node/21547784, last accessed on 15.01.2013.

——— (2012b): "Slouching towards a banking union: The prospects of big bank-outs are intensifying calls for a central fund," from the print edition, available online at http://www.economist.com/node/21556624, last accessed on 12.06.2012.

THE NEW YORK TIMES (1901): "The Leipziger Bank Failure," The New York Times, June 27, 1901, electronic archive, last accessed on 17.03.2011.

THOMAS SKINNER & CO., ed. (1931): *The Bankers' Almanac and Year Book for 1931-32*, Waterlow & Sons Ltd.

——— (1951): *The Bankers' Almanac and Year Book for 1951-52*, Waterlow & Sons Ltd.

TILLY, R. (1986): "German Banking, 1850-1914: Development Assistance for the Strong," *Journal of European Economic History*, 15, 113–152.

——— (1999): "Public policy, capital markets and the supply of industrial finance in nineteenth-century Germany," in *The State, the Financial System and Economic Modernization*, ed. by R. Sylla, R. Tilly, and G. Tortella, Cambridge University Press.

TOOZE, A. (2007): *Ökonomie der Zerstörung*, Bundeszentrale für politische Bildung, Bonn, original Title: "The Wages of Destruction. The Making and Breaking of the Nazi Economy", Allen Lane, London.

——— (2011): "Reassessing the Moral Economy of Post-war Reconstruction: The Terms of the West German Settlement in 1952," *Past and Present*, Supplement 6, 47–70.

TSUTSUI, W. M. (1988): *Banking Policy in Japan: American efforts at reform during the Occupation*, Routledge, London and New York.

U.S. CONGRESS (1913): "On H.R. 7837 (S. 2639): A Bill to provide for the establishment of Federal Reserve Banks, For Furnishing an Elastic Currency, Affording means of rediscounting commercial paper, and to establish a more effective supervision of banking in the United States and for other purposes," in *Banking and Currency Hearings Before the Committee on Banking and Currency*, Senate, 63rd Congress, 1st Session, Document No. 232, United States Government Printing Office, Washington, vol. I–III.

——— (1926): "Inquiry on Membership in Federal Reserve System," in *Joint Hearings Before the Committee on Banking and Currency, Congress of the United States, conducted in 1923*, 68th Congress, United States Government Printing Office, Washington, Part 1.

——— (1927): "McFadden-Pepper Act," P.L. 69-639, 44 STAT. 1224–1234.

——— (1930): "Branch, Chain and Group Banking," in *Hearings Before the Committee on Banking and Currency of the House of Representatives*, United States Government Printing Office, Washington, vol. 1, Part 1.

——— (1932a): *Hearings Before the Subcommittee of the Committee on Banking and Currency United States Senate on the Operation of National and Federal Reserve Banking Systems, Part 1*, United States Government Printing Office, Washington.

——— (1932b): "Operation of the National and Federal Reserve Banking Systems, Part 2," in *Hearings Before the Committee on Banking And Currency of the United States Senate*, United States Government Printing Office, Washington, Mar. 28-30.

——— (1932c): *Report to accompany S. 4412 submitted by Mr. Glass*, 72d Congress, 1st Session, Report No. 584.

——— (1933a): "Banking Act of 1933," P.L. 73-66, 48 STAT. 162.

——— (1933b): *Report to accompany S. 1631 submitted by Mr. Glass*, 73d Congress, 1st Session, Report No. 77.

U.S. DEPARTMENT OF COMMERCE (1949): *Historical Statistics of the United States, 1789–1945*, United States Government Printing Office, Washington.

U.S. Department of State (1985): "Declaration Regarding the Defeat of Germany and the Assumption of Supreme Authority by the Allied Powers, Signed at Berlin, June 5, 1945," in *Documents on Germany, 1944-1985.*, Washington: Department of State, 33–38.

U.S. Department of the Treasury (1863): "Annual Report of the Comptroller of the Currency 1863," in *Report of the Secretary of the Treasury on the state of the finances, for the year ending June 30, 1863*, available online via FRASER at http://fraser.stlouisfed.org/docs/publications/comp/1860s/compcurr_1863.pdf, last accessed 21.01.2013: Government Printing Office, Washington, 49–61.

——— (1864): "Annual Report of the Comptroller of the Currency 1864," in *Report of the Secretary of the Treasury on the state of the finances, for the year 1864*, available online via FRASER at http://fraser.stlouisfed.org/docs/publications/comp/1860s/compcurr_1864.pdf, last accessed 21.01.2013: Government Printing Office, Washington, 46–55.

——— (1932): *Annual Report of the Comptroller of the Currency: December 7, 1931*, United States Government Printing Office, Washington.

——— (1944): "Suggested Post-Surrender Program for Germany (Washington D.C., September 1, 1944)," memorandum available online from the Franklin D. Roosevelt Presidential Library at http://docs.fdrlibrary.marist.edu/psf/box31/a297a01.html, retrieved on November, 6, 2010.

Verhandlungen und Berichte des Unterausschusses für Geld- Kredit und Finanzwesen (V. Unterausschuss) (1930): "Der Bankkredit," in *Ausschuß zur Untersuchung der Erzeugungs- und Absatzbedingungen der deutschen Wirtschaft*, E.S. Mittler & Sohn, Berlin.

Viscusi, W. K., J. E. Harrington, and J. M. Vernon (2005): *Economics of Regulation and Antitrust*, The MIT Press, 4th edition ed.

Volkswirtschaftliche und Statistische Abteilung der Reichsbank (1933): "Die Bankenkrisen in England, Frankreich, Italien und den Vereinigten Staaten von Amerika: Schlußbemerkungen," in *Untersuchung des Bankwesens 1933, Teil I, Band 2*, Carl Heymanns Verlag, Berlin, 348–350.

VONYÓ, T. (2008): "Post-war reconstruction and the Golden Age of economic growth," *European Review of Economic History*, 12, 221–241.

VREELAND, EDWARD, B. (1912): "The Plan of The National Monetary Commission for the Revision of our Banking and Currency Laws," Speech in the House of Representatives on February 6.

WAGNER, J. V. (1975): "Vorgeschichte," in *Band 1: Der Parlamentarische Rat 1948–1949: Akten und Protokolle*, ed. by H. Booms and K. G. Wernicke, Harald Boldt Verlag, Boppard am Rhein.

WALB, E. (1933): "Übersetzung und Konkurrenz im deutschen Kreditapparat," in *Untersuchung des Bankwesens 1933, Teil I, Band 1*, Carl Heymanns Verlag, Berlin, 113–195.

WALL, L. D., M. J. NIETO, AND D. MAYES (2011): "Creating an EU-Level Supervisor for Cross-Border Banking Groups: Issues Raised by the U.S. Experience with Dual Banking," Federal Reserve Bank of Atlanta, Working Paper Series, No. 2011-06.

WALLACE, E. S. (1938): "Survey of Federal Legislation Affecting Private Home Financing Since 1932," *Law and Contemporary Problems*, 481–509.

WANDEL, E. (1980): *Die Entstehung der Bank deutscher Länder und die deutsche Währungsreform 1948*, Fritz Knapp Verlag, Frankfurt.

——— (1982a): "Das deutsche Bankwesen im Dritten Reich (1933–1945)," in *Deutsche Bankgeschichte, Band 3*, Institut für bankhistorische Forschung e. V., Fritz Knapp Verlag, Frankfurt am Main, 147–203.

——— (1982b): "Die deutsche Bankengesetzgebung vom Beginn der Industrialisierung bis zur Weltwirtschaftskrise in ihren zeitgeschichtlichen Zusammenhängen," in *Bankhistorisches Archiv, 8. Beiheft*, Fritz Knapp Verlag, Frankfurt, 13–20.

WEBER, W. E. (2006): "Early State Banks in the United States: How Many Were There and Where Did They Exist?" *Journal of Economic History*, 66, 433–455.

WEINGAST, B. R. AND W. J. MARSHALL (1988): "The Industrial Organization of Congress; or, Why Legislatures, Like Firms, Are Not Organized as Markets," *Journal of Political Economy*, 96, pp. 132–163.

WERNER, W. (1986): "Band 3: Ausschuß für Zuständigkeitsabgrenzung," in *Der Parlamentarische Rat 1948–1949: Akten und Protokolle*, ed. by K. G. Wernicke and H. Booms, Harald Boldt Verlag, Boppard am Rhein.

WEST, R. C. (1977): *Banking Reform and the Federal Reserve 1863–1923*, Cornell University Press, Ithaca and London.

WHEELOCK, D. C. (2008): "The Federal Response to Home Mortgage Distress: Lessons from the Great Depression," *Federal Reserve Bank of St. Louis Review*, 133–148.

WHITE, E. N. (1982): "The Political Economy of Banking Regulation, 1864-1933," *The Journal of Economic History*, 42, 33–40.

——— (1983): *The Regulation and Reform of the American Banking System, 1900–1929*, Princeton University Press.

——— (1984): "A Reinterpretation of the Banking Crisis of 1930," *The Journal of Economic History*, 44, pp. 119–138.

——— (1986): "Before the Glass-Steagall Act: An analysis of the investment banking activities of national banks," *Explorations in Economic History*, 23, 33–55.

——— (2010): "Regulation and Governance: A Secular Perspective on the Development of the American Financial System," in *State and Financial Systems in Europe and the USA: Historical Perspectives on Regulation and Supervision in the Nineteenth and Twentieth Centuries*, ed. by S. Battilossi and J. Reis, Ashgate, 55–78.

——— (2011): ""To Establish a More Effective Supervision of Banking": How the Birth of the Fed Altered Bank Supervision," NBER Working Paper 16825.

WICKER, E. (1996): *The Banking Panics of the Great Depression*, Cambridge University Press.

——— (2000): *Banking Panics of the Gilded Age*, Cambridge University Press.

WIKIMEDIA COMMONS (2008): "Occupation zone borders in Germany, 1947," file published under Creative Commons Attribution-ShareAlike license (CC-BY-SA-2.5), authored by user 52 Pickup, available online at http://en.wikipedia.org/wiki/File:Map-Germany-1945.svg, updated on 17.03.2008, retrieved on 07.11.2010.

——— (2011): "Location map of Federal Republic of Germany. Map shows West-Germany as of April 1952 till August 1955." file published under Creative Commons Attribution-ShareAlike license (CC-BY-SA), Version 1.2, authored by user TUBS, available online at http://commons.wikimedia.org/wiki/File:Germany,_Federal_Republic_of_location_map_April_1952_-_August_1955.svg, updated on 17.10.2011, retrieved on 11.09.2012.

Willis, H. P. (1923): *The Federal Reserve System: Legislation, Organization and Operation*, The Ronald Press Company.

——— (1934): "The Banking Act of 1933–An Appraisal," *The American Economic Review*, 24, pp. 101–110.

——— (1935): "The Banking Act of 1933 in Operation," *Columbia Law Review*, 35, pp. 697–724.

Wilson, J. W., R. Sylla, and C. P. Jones (1990): "Financial Market Panics and Volatility in the Long Run, 1830–1988," in *Crashes and Panics: The Lessons from History*, ed. by E. N. White, Dow Jones-Irwin.

Wilz, A. (1933): "Die Bankenkrise in den Vereinigten Staaten von Amerika," in *Untersuchung des Bankwesens 1933, Teil I, Band 2*, Carl Heymanns Verlag, Berlin, 335–347.

Winkler, H. A. (1993): *Weimar 1918–1933: Die Geschichte der ersten deutschen Demokratie*, C.H. Beck, München.

——— (2006): *Germany: The Long Road West*, vol. Volume 1: 1789–1933, translated by Alexander J. Sager, Oxford University Press.

Wittman, D. (2009): "The End of Special Interests Theory and the Beginning of a More Positive View of Democratic Politics," in *Government and Markets: Toward a New Theory of Regulation*, ed. by E. Balleisen and D. Moss, Cambridge University Press.

Wolf, H. (1995): "Das Fundament wird gelegt: 1945–1995," in *Die Bank – Dienstleister im Wandel: 125 Jahre Commerzbank*, Fritz Knapp Verlag, Frankfurt.

——— (1998a): "Vom Großbankengesetz bis zur "Normalisierung" (1953-1958)," in *Geschichte der deutschen Kreditwirtschaft seit 1945*, ed. by H. Pohl, Fritz Knapp Verlag, Frankfurt, 111–148.

——— (1998b): "Von der Währungsreform bis zum Großbankengesetz (1948-1952)," in *Geschichte der deutschen Kreditwirtschaft seit 1945*, ed. by H. Pohl, Fritz Knapp Verlag, Frankfurt, 59–110.

WOLF, H. C. (1993): "The Lucky Miracle: Germany 1945–1951," in *Postwar Economic Reconstruction and Lessons for the East Today*, ed. by R. Dornbusch, W. Nölling, and R. Layard, MIT Press.

WÜNSCHE, H. F. (1982): *Standard texts on the social market economy: 2 centuries of discussion*, Ludwig-Erhard-Stiftung e.V. Bonn, translated by Derek Rutter, Gustav Fischer Verlag.

——— (1986): *Ludwig Erhards Gesellschafts- und Wirtschaftskonzeption: Soziale Marktwirtschaft als Politische Ökonomie*, Bonn Aktuell GmbH.

——— (2001): "Die Verwirklichung der Sozialen Marktwirtschaft nach dem Zweiten Weltkrieg und ihr Verfall in den sechziger und siebziger Jahren," in *Soziale Marktwirtschaft*, ed. by O. Schlecht and G. Stoltenberg, Herder Verlag, Konrad-Adenauer-Stiftung e.V., 61–114.

WYATT, W. (1932): "Constitutionality of Legislation Providing a United Commercial Banking System for the United States," *Annual Report of the Federal Reserve Board*, 229–259.

ZIEGLER, D. AND H. WIXFORTH (1994): "The niche in the universal banking system: the role and significance of private bankers within Germany industry, 1900–1933," *Financial History Review*, 99–119.

ZILCH, R. (1980): "Zum Plan einer Zwangsregulierung im deutschen Bankwesen vor dem ersten Weltkrieg und zu seinen Ursachen. Dokumentation," in *Forschungsergebnisse zur Geschichte des deutschen Imperialismus vor 1917*, ed. by B. A. Aisin and W. Gutsche, Akademie Verlag, Berlin.

ZINK, H. (1957): *The United States in Germany: 1944-1955*, D. Van Nostrand Company, Inc., Princeton.

Archival Sources

BUNDESFINANZMINISTERIUM (Various Years): "Record Group B126," Archived at the Bundesarchiv in Koblenz, various files.

BUNDESKANZLERAMT (Various Years): "Record Group B136," Archived at the Bundesarchiv in Koblenz, various files.

BUNDESWIRTSCHAFTSMINISTERIUM (Various Years): "Record Group B102," Archived at the Bundesarchiv in Koblenz, various files.

GENERAL RECORDS OF THE DEPARTMENT OF THE TREASURY (Various Years): "Record Group 56," Archived at the National Archives and Records Administration in College Park, Maryland, various containers.

RECORDS OF THE FOREIGN SERVICE POSTS OF THE DEPARTMENT OF STATE (Various Years): "Record Group 84," Archived at the National Archives and Records Administration in College Park, Maryland, various containers.

RECORDS OF THE US HIGH COMMISSION FOR GERMANY (Various Years): "Record Group 466," Archived at the National Archives and Records Administration in College Park, Maryland, various containers.

RECORDS OF UNITED STATES OCCUPATION HEADQUARTERS, WORLD WAR II (Various Years): "Record Group 260," Archived at the National Archives and Records Administration in College Park, Maryland, various containers.

REICHSBANK (Various Years): "Record Group R2501," Archived at the Bundesarchiv in Berlin-Lichterfelde, various files.

REICHSFINANZMINISTERIUM (Various Years): "Record Group R2," Archived at the Bundesarchiv in Berlin-Lichterfelde, various files.

Reichskanzlei (Various Years): "Record Group R43," Archived at the Bundesarchiv in Berlin-Lichterfelde, various files.

Reichswirtschaftsministerium (Various Years): "Record Group R3101," Archived at the Bundesarchiv in Berlin-Lichterfelde, various files.