2021.10.18 Vardaman Scandal 1958 Leaks

Original tweet

Follow-up tweet

Fed Scandal thread.

Ten years into the founding of the Fed, back when there was still a chance that the whole system could be undone at the end of the original 20-year charter like its predecessors, the first New York Fed leader urged his colleagues to govern ethically. 1/

issue of charter renewal. Although the original charter did not expire until 1933, Congress had started consideration. Strong urged the governors to make sure that no scandals would be uncovered if Congress examined the System's operations before renewal. His list includes issues of discrimination for religious or political belief, nepotism, favoritism for one or another person or group in purchasing, dealing in securities, and similar matters. No officer at the New York bank was allowed to borrow money without Strong's approval. He urged the other governors to adopt similar standards.

(Meltzer, v1, Ch4, FN120)

In written testimony to Congress 30yrs later, Strong's successor Allan Sproul proudly pointed to the lack of scandals. Sproul's words, often verbatim, have been repeated recently, rightfully so. Given the power of the Fed, it has had very few scandals in its 100+ year history. 2/

I share the belief that it was the original intent of those who created the Federal Reserve System, that the Federal Reserve banks should function somewhere between private enterprise and the Government. I believe that it has been the continuing intent of each succeeding Congress that the Federal Reserve banks should be allied to Government but not part of Government. I believe that there has been and is wisdom in this segregation. It has generally protected the Federal Reserve banks from partisan political pressure; it has enabled the Federal Reserve banks to repel the pressure of private interests; and it has provided the country with a central banking system staffed by men who have made central banking a career, and operated the Federal Reserve banks according to standards of efficiency and service which compare favorably with the best in Government undertakings and private enterprise. It is significant that there have been no scandals, no charges of influence peddling, no evidence of favors given and received, in connection with the operations of the Federal Reserve banks.

https://fraser.stlouisfed.org/files/docs/publications/mpmpd/1952jc_mpmpd_replies_pt2.pdf

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However, the number of Fed scandals is obviously not zero.

Today, I'll briefly describe a forgotten scandal that shook the Fed and possibly cost a Governor his job. And all this just a few years after Sproul's proud "no scandals" statement. 3/

It's July 1958 and Fed Chair Martin organizes an emergency FOMC conference call. He had recently returned to Washington and been informed by the Treasury that US Marines were deploying to Beirut and the FOMC should prepare for action in the gov securities market. 4/
https://www.brookings.edu/blog/order-from-chaos/2019/10/29/beirut-1958-americas-origin-story-in-the-middle-east/

In the following two weeks the FOMC would hold 11 more emergency conference calls monitoring and responding to significant movements in the gov securities market. Fed Governor James K. Vardaman, Jr. attended and participated in many of these conference calls. 5/ pic

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At the regular FOMC meeting in September, Gov Vardaman participated as usual. There are no hints that this would be his last meeting.

On October 2, Vardaman announces his resignation. 6/

In the Times the following day, Vardaman gives some strange reasons for resigning. He says it's not because of a Fed policy disagreement, but that he believes Fed Governors shouldn't serve more than 10 years...even though he passed the 10 year mark 2.5 years previously… 7/
https://timesmachine.nytimes.com/timesmachine/1958/10/03/110082656.pdf?pdf_redirect=true&ip=0

Days later the Times publishes Vardaman's resignation letter and Pres Eisenhower's response.

"I would very much like to retire and devote the rest of my time to private interests in the calm and comfortable climate of my home areas of south Georgia and south Mississippi" 8/
https://timesmachine.nytimes.com/timesmachine/1958/10/08/80785430.pdf?pdf_redirect=true&ip=0

Although the reasons are somewhat strange, so far there's nothing scandalous about the months leading up to the resignation or the resignation itself. That would soon change. Here's a line from Allan Meltzer's history, 9/

"investigation of 'leaks' pointed to Vardaman. This was a serious scandal for the Federal Reserve. Confronted with the evidence by an irate chairman, Vardaman chose to leave"

From resignation letter to his final day (Dec 1) Vardaman does not attend FOMC meetings. 10/

A broad, Fed-wide leaking scandal rocked the central bank Fall 1958. On October 15, the Times reported "Stocks Sell Off on Huge Volume". The article cited rumors that "the Federal Reserve System might increase margin requirements - the cash that must be put up to buy stocks." 11/
https://timesmachine.nytimes.com/timesmachine/1958/10/15/81890011.pdf?pdf_redirect=true&ip=0

Sure enough, on October 16, "Federal Reserve Raises Margins on Stocks to 90%" 12/
https://timesmachine.nytimes.com/timesmachine/1958/10/16/82213641.pdf?pdf_redirect=true&ip=0

The US Senate opened an investigation into leaks at the Fed. They found that "the Reserve's security system is so lax that at least a hundred persons...have access to decisions directly affecting the stock market." 13/
http://www.treespot.net/Dynamic/showmedia.php?mediaID=3211&medialinkID=6100

However, contemporary news reports (I haven't been able to get my hand on the investigation report itself yet), *do not* name Vardaman directly regarding the leaks. It's more an indictment on the operations of the FOMC as a whole. But… 14/

The investigators did reveal that Vardaman "had used his official car and chauffeur for a lot of cross-country touring."

There's a shockingly damning folder in Chair Martin's papers called "Removal of Governor Vardaman from FRB". 15/
https://fraser.stlouisfed.org/files/docs/historical/martin/martin_s05_a_20_02.pdf

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It's a six-page SLAM on what a horrible Governor Vardaman is. Besides being generally cantankerous (some great lines in this newspaper article about one of his "feuds" https://www.newspapers.com/clip/34293995/usn-commodore-james-k-vardaman-faults/), the memo includes data backing up the senate investigation's claims about car/chauffeur use. 16/

It also includes data about Vardaman's long distance phone call abuses.

But the thing is - despite the folder being titled "Removal of Vardaman" it is dated 1950… 17/ pic of folder.

I haven't found any evidence that Vardaman was involved in any specific leak or series of leaks beyond the loosey goosey way the FOMC handled confidential information. So I'm not sure Meltzer is correct in claiming he was booted because of the leaks of Oct 1958 (or before). 18/

This was certainly a very consequential scandal for the Fed. The FOMC mentioned the leaks and investigation in their first few meetings of 1959, then spent an entire session on the topic in March. 19/

As I see it, there are 2 theories for Vardaman's scandalous resignation:

1. Meltzer is correct and evidence I haven't seen ties Vardaman to earlier leaks (Beirut related?), and it's just a coincidence there was a broader leaks scandal at the FOMC two weeks later. 20/

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2. Chair Martin and others had been angry with Vardaman for a very long time, finally got him to go, and then Vardaman's previous bad behavior misusing Fed resources came out alongside the broader leaks scandal. 21/

I'll continue to dig into this story, but I wanted to take a minute to highlight a Fed scandal from the past that has gone largely ignored.

To repeat, the Fed has had few scandals, but not zero. I have a working list of scandals I can share w/anyone interested. Thanks for reading! /end

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Leaks from the Fed

- **1950**: Chair Martin papers has a very damning folder on Vardaman, "Removal of Governor Vardaman from FRB"
- **July 1958**: Series of intermeeting conference calls to handle issues with the government securities market (FOMC, 1958) following US marine deployment to Beirut (Brookings)
- **Sep 9, 1958**: Governor Vardaman's last FOMC meeting (no mention of last meeting) (FOMC)
- **Oct 2, 1958**: Governor James K. Vardaman, Jr announces resignation. Weird reasoning, not policy related, but no Governor should serve more than ten years, even though he'd served for twelve already (NYT)
- **Oct 7, 1958**: in exchange of letters with Eisenhower, Vardaman gives reason, "I would very much like to retire and devote the rest of my time to private interests in the calm and comfortable climate of my home areas of south Georgia and south Mississippi". Eisenhower specifically thanked "for your concern for the public service role of banking in the nation". (NYT)
- **Oct 15, 1958**: "Stocks Sell Off on Huge Volume". Rumors, including that "the Federal Reserve System might increase margin requirements - the cash that must be put up to buy stocks." (NYT)
- **Oct 16, 1958**: "Federal Reserve Raises Margins on Stocks to 90%" NYT, frontpage screenshot
- **Nov 30, 1958**: Meltzer claims that, "investigation of 'leaks' pointed to Vardaman... Confronted with the evidence by an irate chairman, Vardaman chose to leave" (Meltzer, v2b1, Ch2, FN225)
- **Dec 1, 1958**: Gov Varaman last day (FedHistory)
- **January, 1959**: Congressional investigation led by Senator John McClellan, Paper
- **Jan 6, 1959**: California newspaper reports that the Senate investigation into the leaks also unearthed other issues, directly related to former Governor Vardaman. That he "had used his official car and chauffeur for a lot of cross-country touring. Vardaman told the

probers these trips were for official purposes. He made the same claim regarding scores of long distance calls." (Appeal Democrat)

- **Jan 27, 1959**: discusses after the regular meeting (FOMC Mar 3, 1959, p66)
- **Feb 10, 1959**: Chair Martin briefly cautions about leaks (FOMC Mar 3, 1959, p38) and agrees with Governor Balderston who said, "If it were humanly possible, he hoped that all connected with the System would refrain from making remarks that could be quoted in the press. While rumors cannot be prevented, those in the System should endeavor to keep from feeding them." (FOMC Mar 3, 1959, p34)
- **Between**: Chair Martin has one-on-one convos with many FOMC members (FOMC Mar 3, 1959, p67)
- **Mar 3, 1959**: a whole session dedicated to the issue (FOMC Mar 3, 1959, p66)

Follow-up info

- Suspicion was that Vardaman leaked Fed Treasury accord inappropriately (p39)
- Discount Window changes leak reported on March 8, 1958 by NYT and Texas and NY congressmen
- Reported leak mentioned in Board meeting minutes March 10, 1958, "At the conclusion of the discussion, it was understood that Chairman Martin would state to Mr. Spence that the members of the Board had no information or evidence of a leak of information but that they 'would, of course, be available for any investigation of the matter that might be undertaken by the Banking and Currency Committee."
- A Board meeting on April 4, 1958, "In view of Governor Vardaman's prospective absence from his office, Chairman Martin called upon him for preliminary comment with respect to the proposed amendments" (p4) But this could be referring to his leaving the meeting later (p10).