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DISCONTINUANCE OF MEMBERSHIP OF NATIONAL  
BANK CONVERTING INTO STATE INSTITUTION

It appears that a certain national bank may convert into a State bank, through voluntary liquidation as a national bank and the transfer of its assets and liabilities to a newly organized State bank; and it is possible that it may then be urged that the newly formed State institution is automatically a member bank of the Federal Reserve System. In order that the Federal Reserve bank of the district in question may not be regarded as acquiescing in this view by any action or course of conduct, it is important that it consider carefully what action it should or should not take in order to see that the membership of the national bank is terminated and in order not to act in any manner inconsistent with the fact that the newly formed State institution is not automatically a member bank.

There are suggested in the following list certain actions which the Federal Reserve bank might well take or avoid for the purpose stated:

Cancellation of Federal Reserve Bank Stock.

Forms for application for the cancellation of Federal Reserve bank stock and the refund of balances due to the national bank should be sent to the bank immediately upon advice of its liquidation and the matter then handled in accordance with the provisions of Regulation I of the Board of Governors. Any other steps customarily taken in connection with the cancellation of stock of a liquidating national bank should also be taken without delay. Of course, no Federal Reserve bank stock should be issued to the newly formed State institution unless it should be admitted to membership in the established manner under the provisions of section 9 of the Federal Reserve Act.

Collections of Cash and Noncash Items.

Collections of cash and noncash items for the old bank should be limited to collections customarily made for member banks which have been placed in liquidation. Likewise, collections of cash or noncash items for the new bank should be made, and items sent to it for payment or collection, only under the same circumstances that items are collected for or sent to other nonmember banks. Of course, it would be in order to treat the newly formed institution as a nonmember clearing institution, if it should so

desire and should properly establish a balance with the Federal Reserve bank for this purpose pursuant to the provisions of section 13 of the Federal Reserve Act. It might be well to advise the new bank in writing of the conditions under which items would be received from it for collection.

#### Reserves.

The application form for cancellation of Federal Reserve bank stock would include application for the return of balances due from the Federal Reserve bank to the liquidating bank. In order to anticipate any suggestion or claim that such balances or any part thereof should be considered as a reserve balance maintained by the newly formed State bank under section 19 of the Federal Reserve Act, consideration might be given to advising both the old and the new banks that this balance is being held for disposition in accordance with duly authorized instructions from the liquidating institution, but that it can not be maintained as a balance for the new institution. Of course, if properly assigned or transferred by operation of law to the new institution, the balance could, under proper instructions, be used as a nonmember clearing balance under section 13 of the Federal Reserve Act.

No deposits should be received from or items placed to the credit of the newly formed State bank unless and until an arrangement for a nonmember clearing balance has been consummated.

#### Credit Accommodations.

The Federal Reserve bank should not extend credit to the new institution, through making any purchase from it or making any loan or discount for it, except in so far as might be done for a person other than a member bank (e.g., under the last paragraph of section 13 of the Federal Reserve Act regarding loans on Government obligations, or in the manner provided in section 13b of the Federal Reserve Act regarding industrial loans).

#### Reports and Examinations.

No reports of condition or similar reports should be called for from the new State institution by the Federal Reserve bank, or examinations or investigations made of it by the Federal Reserve bank (except in connection with an application for membership); nor should any reports be requested from or examinations made of any affiliate or holding company affiliate on the basis of the membership of the new State institution.

Enforcement of Law and Regulations.

It would seem undesirable for the Federal Reserve bank to request or require that the newly formed State bank take any action or refrain from any action with a view to having it conform to any provision of law or regulation applicable to the operations of member banks or their affiliates (unless the provision is equally applicable to nonmember banks or their affiliates) and if any correspondence with the State institution with regard to any such matter should become necessary, it should be based upon the premise that the bank is not a member of the System. Merely as examples of the type of law or regulation in question, attention is directed to the provisions of section 5136, Revised Statutes, and the regulations of the Comptroller of the Currency thereunder, the provisions of law prohibiting member banks from lending on or purchasing their own stock, the provisions of section 23A of the Federal Reserve Act, and the provisions of the Clayton Act and the regulations of the Board of Governors thereunder. There are, of course, many others.

Currency and Coin.

The Federal Reserve bank should not supply currency and coin to the newly organized State bank or receive currency and coin from such bank, or absorb the expense of shipment of currency and coin to and from such bank, except to the same extent and under the same circumstances as for other nonmember banks.

Safekeeping of Securities.

It would seem inadvisable for the Federal Reserve bank to undertake the safekeeping of securities for the newly organized member bank (except perhaps as security for bankruptcy funds with a proper charge), and it should arrange to return to the liquidating national bank any securities held for its account as promptly as possible.

Transfers of Funds by Leased Wire.

Funds should be transferred for the newly organized State bank only to the same extent and under the same restrictions that they are transferred for other nonmember banks.

Purchase and Sale of Securities.

Unless it is the practice of the Federal Reserve bank to place orders for the purchase or sale of Government securities or

other securities for the account of nonmember banks, no such orders for the purchase or sale of securities for the newly organized State bank should be handled by the Federal Reserve bank.

Participation in Elections of Federal Reserve Bank Directors.

Since the new institution as a nonmember would not be entitled to participate in elections of Class A and B directors of Federal Reserve banks, no letter, notice or other advice concerning such elections should be transmitted to the new bank.

Informational Services.

The name of the newly organized State bank should not be placed on the list with member banks to receive any copies of reviews, reports, bulletins, regulations, notices, etc., which are customarily sent to member banks but not to others.

Miscellaneous.

The conversion by the Federal Reserve banks of Canadian currency and coin into United States funds and the sale by the Reserve banks of other foreign currency and coin for the account of member banks are other services which it is understood are performed only for member banks and should, therefore, not be performed for the new State bank.

Federal Reserve exchange drafts could not, of course, be issued for the new State bank, inasmuch as it would have no balance with the Federal Reserve bank available for the purpose.

Inasmuch as the new State bank would not automatically be a member bank, its deposits would not be insured under section 12B of the Federal Reserve Act except upon application and approval by the Federal Deposit Insurance Corporation. Likewise, it would not be eligible to serve as a financial agent of the Government or as a depository of public funds (except in special cases). It is assumed that it would not be necessary to advise the Federal Deposit Insurance Corporation or the Secretary of the Treasury that the new State bank is not a member of the Federal Reserve System; but the point might be considered.

If the new State bank, without being admitted to membership in the Federal Reserve System, should advertise or represent that it is a member of the System in violation of the Act of May 24,

1926 (U.S.C. Title 12, section 586), it would seem that the violation should be reported to the proper authorities in the same manner as other violations of the criminal provisions of the banking laws. Likewise, if the new bank should advertise or represent that it is insured under section 12B of the Federal Reserve Act without having been admitted to the Federal Reserve System or approved by the Federal Deposit Insurance Corporation for insurance, the matter should be brought to the attention of the Board of Governors.