Confidential

BRANCH AND GROUP BANKING

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Branch, Group and Chain Banking

Three methods may be distinguished by which the same interests operate a banking business at more than one office -- branch, group and chain systems. In a branch system there is but one legal entity of which the several offices are a part. A group system comprises separately incorporated banks,[1] with or without branches, which are owned or controlled, directly or indirectly, by a corporation, business trust, association, or other similar organization. Chain banking is similar to group banking except that control is held or exercised by an individual or a group of individuals.

On December 31, 1935 [2] each of 804 commercial banks was operating one or more branches.[3] Of the total of 3,114 branches included in these branch systems, 1,617 were located in the same cities as the head offices of the banks, 617 outside the head office cities but in the same counties as the head offices of the banks, 348 in contiguous counties, and 532 in noncontiguous counties. During the past decade there have been numerous liberalizations in the laws with respect to branch operation and the proportion of commercial banking facilities represented by branches has increased considerably.

1/ Official statistics on group banking have always been confined to groups comprising 3 or more banks.

2/ A statistical analysis of branch and group banking as of December 31, 1936 will be undertaken later, if desired. The data needed for such an analysis usually do not become available for several months after the end of the year.

3/ Section 5155 U.S.R.S. defines the term "branch" as "any branch bank, branch office, branch agency, additional office, or any branch place of business ... at which deposits are received, or checks paid, or money lent." The term "branch" is used in that sense in this memorandum, although it is recognized that some State laws make a distinction between "branches" and certain other types of "additional offices."

Because of the difficulty of determining the essential facts, particularly where nonmember banks are involved, fully comparable statistics are not available with respect to group banking. However, a recent survey shows that on December 31, 1935 there were 61 group banking systems consisting of 3 or more banks operating under some form of corporate or similar control. There were 543 banks embraced in these groups. Nearly all of the banks were located in cities other than those in which the principal places of business of the respective groups were located and correspond in many respects, therefore, to branches operating outside the head office cities of their parent banks. Since 1930 numerous group banks have been converted into branch offices of affiliated banks.

No recent survey of chain banking has been made. It would be impossible to determine the extent or degree to which chain banking exists without data obtainable only through questionnaires returned by banks and special reports by the Federal Reserve banks and other supervisory authorities. At the end of 1931, when the last survey of chain banking was made, 176 chains comprising 3 or more banks each were reported. The total number of banks in these chains was 908.

Under existing laws branch operation is not permitted in some States. In others branches are permitted only in the head office city, the head office county, or in groups of counties. In still other States a bank is permitted to operate branches anywhere within the State.

This situation with respect to branch operation is to be contrasted with that of operating a multiple office system through groups, many of which operate banks in two or more States unrestrained by any legal limitations in this respect. Some groups operate in more than one Federal

Reserve district, and there is no legal barrier to their spread across the country. Many of the groups were formed after 1927 and obtained some of the advantages of multiple office banking which were denied by the restrictions placed upon branch operation. Numerous conversions of group banks into branches have occurred in recent years after laws were liberalized with respect to branch banking.

Growth of Branch Banking

Increasing Ratio of Branches to Banks.- The proportion of commercial banking facilities represented by branches is much greater today than it was a decade ago and appears to be increasing. The increase in the ratio of branches to total banking offices of commercial banks in recent years as compared with the condition 15 years ago is striking, as is shown by the following table:

	Number of banks 1/ (head offices)	Number of branches	Total banking offices	Ratio of branches to total banking offices
June 30, 1920	28,659	2/ 1,281	29,940	4.5
June 30, 1925	27,639	3/ 2,524	30,163	8.4
June 30, 1930	23,045	3,518	26,563	13.2
Dec. 31, 1931	19,167	3,334	22,501	14.8
Dec. 31, 1932	17,330	3,191	20,821	15.3
Dec. 31, 1933	14,334	2,752	17,086	16.1
Dec. 31, 1934	15,219	2,973	18,192	16.3
Dec. 31, 1935	15,158	3,114	18,272	17.0
Nov. 30, 1936 4/	15,010	3,194	18,204	17.5

1/Exclusive of Mutual Savings Banks and private banks; inclusive of such Morris Plan and industrial banks, trust companies without deposits, and other banking institutions as are included in State banking abstracts.
2/The figures of branches of individual banks are not as of any uniform date.
3/End-of-year figures; data not available as of June 30.
4/Estimated.

The table shows that branches comprise 17.5 percent of total banking offices, compared with 4.3 percent in 1920. The decreasing number of banking offices is, of course, accounted for principally by the large number of bank suspensions and mergers. Largely because of suspensions and mergers of some of the branch systems, the number of branches also declined during the depression period 1930-1933. The net reduction during 1930-1933 in the

number of branches, however, was only 22 percent, compared with a 38 percent reduction in the number of banks. It is significant that of recent months since the stabilization of banking the number of individual banks continues to decrease and the number of branch offices to increase. During the 11 months ended November 30, 1936, for example, the number of commercial banks has decreased by about 148 while branch offices of commercial banks have increased by about 80, principally as a result of the conversion of 58 banks into branches.

A large part of the recent growth in the number of branches has taken place in States in which the establishment of branches was not permitted a few years ago. For example, in Iowa there were 185 branch offices 1/ on December 31, 1935, in Wisconsin 105, in Indiana 47, and in Oregon 42. The establishment of branch offices in these States has served to replace in part the banking facilities of which many communities were deprived by the disturbances which culminated in the banking holiday of 1933.

Distribution of Branches. - There were 3,114 branches in operation on December 31, 1935, 1,329 being operated by national banks and 1,785 by State banks.

Of the total, 1,617 branches were located in head office cities. This figure is but slightly larger than it was 12 years ago. On the other hand, the number of branches outside the head office cities, 1,497, is almost double that of 1924. Nearly 400 such branches were established during 1934 and 1935.

1/ The laws of Iowa, Wisconsin, Arkansas, and New Mexico permit the establishment of offices that have only limited banking functions. These offices are not termed "branches" by State law; in fact the law of Iowa prohibits "branch banking."

The number of branches located outside of the county of the head office was 880. Of this number 224 were located 25 miles or less from their head offices, 166 from 26 to 50 miles from their head offices, 142 from 51 to 100 miles from their head offices, and 348 more than 100 miles from their head offices. Of the latter number all but 67 were located in California, where State-wide branch banking has had its greatest development.

California accounted for more branches than any other State, 794, located for the most part outside the head office cities. In New York, where branch systems may now operate in areas larger than counties but not State-wide, there were 606 branches, nearly all confined to head office cities. In Ohio, where branches may be established in contiguous counties, 169 branches were in operation, confined mostly to head office cities. In each of 5 other States, Michigan, Iowa, New Jersey, Massachusetts and Wisconsin, there were in operation in excess of 100 branches. In each of 22 other States the number of branches ranged from 10 to 91. In each of 9 other States the number of branches in operation was less than 10, while in the 9 remaining States no branches were operated.

The total number of branches in operation at the end of 1935 and the number outside the head office cities, by States, were as follows:

	Total number	Number outside head office city		Total number	Number outside head office city
California	794	553	Dist. of Col.	30	0
New York	606	15	Kentucky	30	11
Ohio	169	39	Idaho	26	26
Michigan	141	21	Georgia	24	14
Iowa	125	125	Alabama	22	19
New Jersey	114	23	Arizona	21	21
Massachusetts	110	19	South Carolina	21	18
Wisconsin	105	87	South Dakota	15	15
Pennsylvania	91	6	Delaware	12	10
North Carolina	89	82	Vermont	12	12
Maryland	76	41	Utah	10	9
Virginia	64	43	Connecticut	9	5
Maine	58	55	Nevada	7	6
Louisiana	51	28	Arkansas	6	6
Tennessee	48	30	Minnesota	6	0
Indiana	47	28	New Mexico	5	5
Oregon	42	31	West Virginia	2	1
Washington	44	30	Nebraska	2	0
Mississippi	40	40	New Hampshire	1	1
Rhode Island	38	21	North Dakota	1	1
			Total	3,114	1,497

There were no branches reported in operation in the following States: Colorado, Florida, Illinois, Kansas, Missouri, Montana, Oklahoma, Texas, and Wyoming. In one of these States, Montana, the State law permits establishment of branches in the head office county and adjoining counties upon consolidation of banks. The limited area to which branch operation would have to be confined, as well as anti-branch banking sentiment, has operated against the establishment of branches. The Northwest Bancorporation and the First Bank Stock Corporation control most of the larger banks in Montana and, in this manner, provide the substantial equivalent of branch banking.

Status of Group Banking

It is perhaps only natural that the holding company should have found its way into banking as it has into other fields of business enterprise, since in the absence of legislation permitting State-wide branch banking the bank merger or consolidation movement in the 1920's, so pronounced in some of the larger cities, could be approximated in the rural sections only by a holding company. Before the enactment of legislation in recent years permitting the extension of branch banking or broadening the branch banking areas, some group interests expressed the belief that group banking in some respects was a better form of multiple office banking than branch banking. Most of the group heads, however, conceded that group banking was merely an alternative to branch banking. The wide distribution of group systems in non-branch States, and the conversion during 1933-1935 of many group banks into branches in States that have liberalized their branch laws, substantiate this view.

Distribution of Group Banks. - A survey made as of December 31, 1935 on the basis of data available in the records of the Board and the Federal Reserve banks disclosed that there were 61 group banking organizations in operation at that time, each comprising 3 or more banks1/. These 61 groups embraced 314 national banks, 59 State bank members, 155 insured nonmember banks and 15 non-insured banks, or a total of 543 member and nonmember banks.

1/ The survey covered: (1) Banks controlled by a "holding company affiliate" as defined in Section 2(c) of the Banking Act of 1933, as amended; (2) banks which would have been under the control of a holding company affiliate if the Reconstruction Finance Corporation capital investment were disregarded; (3) other banks included in what is generally regarded as a bank group, even though the affiliation did not technically conform to Section 2(c) of the Banking Act of 1933.

Some of the banks in those groups operate branches, notably the Bank of America National Trust and Savings Association, San Francisco, which has over 400 branches. A total of 874 branches were being operated by 71 of the 543 banks included in the 61 groups.

Group banking has had its greatest development in States in which branch banking either has not been permitted at all or only under narrow restrictions. The extension of branch banking privileges in recent years has resulted in the conversion of many group banks into branches. In recent months some group systems have enlarged their fields of operations by purchasing additional banks and converting them into branches.

States in which Branch Banking is Prohibited. - At the end of 1935 there were 154 group banks in 7 of the 9 States in which the establishment of branches is prohibited, distributed as follows:

Minnesota	89	West Virginia	5
Florida	24	Illinois	4
Texas	14	Kansas	0
Nebraska	11	Colorado	0
Missouri	7		
		Total	154

The Northwest Bancorporation controlled 44 of the group banks in Minnesota and the First Bank Stock Corporation controlled 41. Both of these holding companies operate in several States. In Florida 8 of the 24 group banks belonged to the Almours Securities group, 7 to the Atlantic National Bank group of Jacksonville, Florida, and 9 to 2 other groups. In Texas 8 of the 14 group banks

belonged to the Republic National Bank group of Dallas and 5 to the Mercantile National Bank group of Dallas. In Nebraska 7 of the 11 group banks belonged to the Northwest Bancorporation.

The laws of Kansas, in which there are no group banks although branch banking is prohibited, authorize the banking authorities to examine any corporation holding as much as one-fourth of the stock of any bank or trust company. This factor and the agitation of unit banks against both branch and group banking may account for the fact that group banking has had no development there. The laws of Colorado, where there also are no group banks, appear to contain no provisions which might tend to prevent the operation of group banking systems.

States Whose Banking Laws Contain No Provision with Respect to Branch Banking. - There were 43 group banks at the end of 1935 in four of these States, distributed as follows:

North Dakota	30	Wyoming	3
Kentucky	6	Oklahoma	0
New Hampshire	4		
		Total	43

The 30 group banks in North Dakota were all controlled by the Northwest Bancorporation and the First Bank Stock Corporation.

Although there are no group banks in Oklahoma, there appears to be nothing in the laws of the State that would prevent the

development of group banking. There was in fact a fairly large group there before the banking holiday in 1933, and there is a "chain" of 9 banks controlled by Thurmond Brothers.

States in Which Branch Banking is Restricted to the Head Office City or County. - There were 83 group banks in five of these States, distributed as follows:

Massachusetts	23	Indiana	3
Tennessee	22	Delaware	0
New Jersey	18	Louisiana	0
Georgia	17	Alabama	0
		Total	83

In Massachusetts the Old Colony Trust Associates group controlled 15 banks and the National Shawmut group 7. In Tennessee the Hamilton National Associates controlled 12 banks, besides 6 banks in Georgia where branches may be established only in the head office city. In New Jersey the 18 banks belonged to 5 different groups.

There appears to be nothing in the laws of Delaware, Louisiana and Alabama, in which there are no group banks, preventing the development of group banking. A group of 7 banks in Alabama, headed by the First National Bank of Birmingham, was converted into a branch system in 1935 upon the enactment of enabling legislation.

States in Which Branches May Be Established Beyond the Head Office County but Not Throughout the State. - There were 172 group banks at the end of 1935 in six of these States, distributed as follows:

New York	50	Ohio	13
Pennsylvania	47	Arkansas	0
Wisconsin	24	Mississippi	0
Montana	27	New Mexico	0
Iowa	11		
		Total	172

In New York, where a State bank may establish branches only within the banking district, as defined by statute, in which its head office is located, there were 50 group banks, of which 20 belonged to the Marine Midland Corporation and the remainder to 6 different groups. In Pennsylvania the 47 group banks at the end of 1935 are accounted for principally by the Mellbank Corporation and Union Trust Company which controlled 25 banks. The status of the Mellbank Corporation as a holding company affiliate has since been terminated by distribution of stock of the subsidiary banks, but the Union Trust Company, which like the Mellbank Corporation is controlled by the Mellon interests, is still a holding company affiliate with 4 subsidiary banks. Seven other groups in Pennsylvania controlled a total of 22 banks at the end of 1935. In Wisconsin 18 of the 24 group banks belonged to the Wisconsin Bankshares Corporation. In Montana the 27 group banks all belonged to the First Bank Stock Corporation and the Northwest Bancorporation. In Ohio all of the 13 group banks belonged to the BancOhio Corporation. In Iowa 6 of the 11 group banks belonged to the James F. Toy group and 5 to the Northwest Bancorporation.

The existence of group banking systems in some of the States may be explained partly by the fact that the branch banking area, as defined by State laws, is not sufficiently wide to permit the conversion of some of the

group banks into branches. In New York, for example, some of the banking districts fixed by statute are relatively small, comprising as few as three or four counties, while the banks in the Marine Midland group are located in a number of the banking districts. In Wisconsin and Ohio the limitations of the branch banking area effectively prevent the Wisconsin Bankshares Corporation and BancOhio Corporation, respectively, from converting some of their banks into branches. The high capital requirements applicable to national banks establishing branches outside of their head office cities also retard the conversion of banks into branches.

Mississippi, which has no group banking, prohibits the incorporation in the State, or admission to business in the State, of any corporation to operate banks in groups or chains. Arkansas prohibits any person who owns 50 percent or more of the capital stock of three or more banks from borrowing from such banks. There appears to be nothing in the laws of New Mexico to prohibit the development of group banking there.

States in Which State-wide Branch Banking Is Permitted. - There were 91 group banks at the end of 1935 in States which permit State-wide branch banking, distributed as follows:

Washington	22	Connecticut	3
California	17	Michigan	1
South Dakota	17	South Carolina	1
Idaho	15	Arizona	0
Utah	7	Maryland	0
Nevada	1	North Carolina	0
Oregon	1	Vermont	0
Maine	3	Virginia	0
Rhode Island	3		
		Total	91

These banks were distributed through 12 States and belonged to 19 different groups. The existence of group banks side by side with branch banks in some of the States listed above, notably the Western States, is explained partly by the existence of two or more holding companies, each having subsidiary banks, some with branches. It is due also to the fact that legislation permitting State-wide branch banking was not enacted in some of these States until 1933. Since that time many of the banks belonging to groups in these States have been converted into branches. Certain factors tend to postpone the conversion of group banks into branches, such as minimum capital and other requirements made by supervisory authorities, especially with respect to member banks; personnel problems; the desire of the holding company to acquire additional stock of the controlled bank before converting it into a branch; the need of determining whether or not the interests of the holding company would best be served by the conversion; and the existence of strong anti-branch sentiment or desire to test gradually the state of public feeling with respect to branch banking.

In summary, of the 543 banks belonging to groups at the end of 1935,

154 were located in 7 States in which the extension of branch banking was prohibited;

43 in 4 States in which there is no statutory provision for the establishment of branches;

83 in 5 States in which the establishment of branches is restricted to the head office city or county;

172 in 6 States in which branches may be established beyond the limits of the head office county but not throughout the State;

91 in 12 States in which State-wide branch banking is permitted.

Interstate and Inter-district Group Banking. - Only 2 banks in the United States, both national, have interstate branches. All of the 4 branches of these banks were established many years ago, before the operating banks became national associations. In contrast with these isolated instances of interstate branch banking, there are a number of group banking systems that cross not only State but also Federal Reserve district lines.

At the end of 1935 the Northwest Bancorporation controlled 94 banks scattered through Minnesota, North Dakota, Montana, Nebraska, Wisconsin, South Dakota, and Iowa. These banks were located in 3 Federal Reserve districts, Minneapolis, Chicago, and Kansas City, and in 4 different Federal Reserve bank or branch zones, namely, those assigned to the Federal Reserve Banks of Minneapolis and Chicago and to the Federal Reserve branches at Omaha and Helena.

The First Bank Stock Corporation had 83 banks located in Michigan, Minnesota, Montana, South Dakota, and North Dakota. All of them were in the Minneapolis Federal Reserve district, but some of them were located in the zone (the entire State of Montana) assigned to the Helena branch.

The Transamerica Corporation controlled 6 banks operating in California, Oregon, and Nevada at the end of 1935. Since then it has ac-

quired control of a national bank in Washington and additional banks in California and Nevada. The principal bank in the Transamerica group has over 400 branches. The banks and branches in the Transamerica group are all in the San Francisco Federal Reserve district. Some of them are located in the territory assigned to the head office of the Federal Reserve bank and others in the territories assigned to the Los Angeles, Portland, Salt Lake City, and Seattle branches.

Some of the important groups confine their operations to a single State. The Marine Midland Corporation of Buffalo, for instance, has 20 banks, all in the State of New York. Some of them, however, are located in the Buffalo branch zone, and others in the Federal Reserve bank (head office) territory.

The BancOhio Corporation controlled 13 banks at the end of 1935, all located in Ohio. Some were in the Cleveland Federal Reserve bank zone and others in the Cincinnati branch zone.

The Wisconsin Bankshares Corporation of Milwaukee controlled 18 banks, all in Wisconsin. Some were located in the Chicago Federal Reserve district and others in the Minneapolis district.

The following summary table shows the groups which on December 31, 1935 comprised 5 or more banks and which operated in more than one State, in more than one Federal Reserve district, or in more than one Federal Reserve bank or branch zone.

BANK GROUPS WITH 5 OR MORE BANKS WHICH ON DECEMBER 31, 1935 WERE OPERATING IN MORE THAN ONE STATE, MORE THAN ONE FEDERAL RESERVE DISTRICT, OR MORE THAN ONE FEDERAL RESERVE BANK OR BRANCH ZONE

Name and location of principal office of group	Number of banks in group				Number of States, Federal Reserve bank and branch zones, and Federal Reserve districts in which the group has banks or branches		
	Total	National banks	State bank members	Non-member banks	States	Zones	Districts
Northwest Bancorporation Minneapolis, Minnesota	94	60	2	32	7	4	3
First Bank Stock Corporation Minneapolis, Minnesota	83	66	1	16	5	2	1
Transamerica Corporation 1/ San Francisco, Calif.	14	10	1	3	4	5	1
James F. Toy Bank Stock Trust Sioux Falls, S. Dak.	8	5	-	3	3	3	3
First Security Corporation Ogden, Utah	5	2	1	2	3	2	2
Rawlins Securities Company and J. E. Cosgriff Salt Lake City, Utah	7	6	-	1	3	2	2
Vollmer Securities Company Lewiston, Idaho	8	2	-	6	2	1	1
Old National Corporation Spokane, Washington	6	4	-	2	2	1	1
Anglo National Corporation San Francisco, California	11	10	-	1	2	2	1
Windber Trust Company group Windber, Pennsylvania	9	3	4	2	2	3	3
Citizens & Southern Nat. Bank Savannah, Georgia	6	3	-	3	2	3	2
Hamilton National group Chattanooga, Tennessee	18	12	-	6	2	2	1
Marine Midland Corporation Buffalo, New York	20	3	9	8	1	2	1
BancOhio Corporation Columbus, Ohio	13	9	4	-	1	2	1
Wisconsin Bankshares Corp. Milwaukee, Wisconsin	18	10	1	7	1	2	2
First National Bank group Louisville, Kentucky	6	3	2	1	1	2	2

1/ In the case of this group the statement shows the current situation rather than the situation on December 31, 1935.

Changes Since 1931. - The latest previous survey of group banking, made as of the end of 1931, indicated that there were 97 bank groups[1] in operation comprising a total of 978 banks. By the end of 1935, the affiliations in many of these cases had been terminated by the dissolution of the holding company, by disposing of control of subsidiary banks, by closing of some or all of the banks in the group system, or by converting some of the subsidiary banks into branches. In the latter class are the following:

	Number of banks in group on Dec. 31, 1931
Hartford Connecticut Trust Co. group, Hartford, Conn.	9
First National Bank group, Birmingham, Ala.	6
First National Bank group, Seattle, Wash.	6
United States National Corporation, Portland, Ore.	11
Worcester County Bank & Trust Co., Worcester, Mass.	7
First National Investment Co., Boise, Idaho	10

Subsidiary banks in all of these groups were converted into branches upon the enactment of legislation during recent years permitting the establishment of branches[2]. The last two were converted into branch systems partly incident to the reorganization of constituent banks necessitated by their weakened condition.

1/ As previously indicated, the current definition of a "bank group" as used in this memorandum is practically the statutory definition of a "holding company affiliate" contained in the Banking Act of 1933. There was no such legal definition in existence at the end of 1931, and accordingly some of the bank groups surveyed at that time did not necessarily conform to the current definition. In general, however, the 1931 survey, like the present one, covered those situations where 3 or more banks were associated under a centralized corporate or similar control, as distinguished from control exercised by an individual or group of individuals, a relationship commonly termed "chain banking".

2/ Legislation providing for the establishment of branches, or extending the territory in which branches might be established, was enacted during 1931-1935 in 22 States.

In addition to the group banking affiliations which have been completely terminated since 1931 by conversion of subsidiary banks into branches, a number of groups which are still in existence have converted some banks into branches since the enactment of enabling branch legislation. For example:

	Number of banks converted into branches during 1932-1935
Old Colony Trust Associates of Boston, Massachusetts, associated with the First National Bank of Boston	5
Northwest Bancorporation, Minneapolis, Minnesota	15
First Security Corporation, Ogden, Utah	20
Marine Bancorporation, Seattle, Washington	6
Old National Corporation, Spokane, Washington	9
Anglo National Corporation, San Francisco, California	8
Wisconsin Bankshares Corporation, Milwaukee, Wisconsin	13

The movement for conversion of group banks into branches is still in progress. In recent months some groups have acquired additional banks which have been converted into branches.

Among the group relationships that have been terminated since 1931 because of dissolution of the holding company or because of the closing of some or all of the affiliated banks are the following:

	Number of banks and branches in group on December 31, 1931	
	Banks	Branches
Detroit Bankers group	9	188
Guardian Detroit Union group	27	75
Exchange National Bank group, Tulsa, Oklahoma	21	--
Financial Institutions group, Augusta, Maine	12	31
C. J. Weiser, Inc., Decorah, Iowa	8	--
Central Republic Bank & Trust Company group, Chicago, Ill.	10	--
National Republic Bancorporation, Chicago, Ill.	8	--

The relationship between the banks in the last two groups was somewhat tenuous. However, the fact that nearly all of the affiliated banks suspended indicates the existence of a close relationship between them.

Branch Banking Statutes

Federal Law. - The National Bank Act has been liberalized with respect to branch banking twice in the past decade. By the McFadden Act of 1927 national banks were given power to establish branches in the head office city in those States where State institutions had such powers, in addition to continuing the operation of existing branches wherever located. No special capital requirements were stipulated by the McFadden Act for the establishment or operation of branches.

The Banking Act of 1933 extended the power of national banks so that they may establish branches within any area in the State in which the national bank is situated provided that establishment of branches within such area is authorized to State banks by affirmative provisions of State law. They may also continue to operate any branches which were in lawful operation on February 25, 1927, when the McFadden Act was passed.

The Banking Act of 1933 also included certain stipulations with respect to minimum capital for banks establishing branches outside the head office city. These provisions, which have had the effect of preventing the establishment of branches by national banks in some cases, are discussed elsewhere in this memorandum.

State bank members of the Federal Reserve System may establish branches under the same conditions and limitations as national banks. A State bank applying for membership may continue to operate any branch which was in lawful operation on February 25, 1927, without regard to location, but as to any branch established after that date the bank must comply with the capital and other requirements governing the establishment of branches by national banks.

State Laws. - Surveys and digests of State statutes relating to branch banking have been prepared from time to time since 1924 by the Board's Counsel. These surveys show that the number of States authorizing some form of branch banking has increased from 16 in 1924 to 34 in 1936, and the number of States either prohibiting or without provisions regarding branch banking has decreased from 32 in 1924 to 14 in 1936. 1/

As is brought out below, the growth in the number of States authorizing branches has been due to an increase in the number of States permitting branches on a State-wide basis and in the number of States permitting them in areas beyond the city of the head office. These changes in the direction of liberalization have taken place largely during 1931-1936; in such cases the year in which the present provisions were enacted is shown in parentheses after the name of the State. 2/

State-wide Branch Banking. - Branch systems could under the law operate on a State-wide basis in 9 States in 1924. In June 1936 there were 17 such States as follows:

Arizona	Maryland	South Carolina
California	Michigan (1933)	South Dakota (1933)
Connecticut (1933)	Nevada (1933)	Utah (1933)
Idaho (1933)	North Carolina	Vermont
Maine (1933)	Oregon (1933)	Virginia
	Rhode Island	Washington (1933)

1/ Branches or additional offices have also been permitted throughout this period in the District of Columbia, the political boundaries of which are the same as those of the city of Washington.

2/ The classification of States in 1924 and 1936 is not exactly comparable in some instances, due to different interpretations in 1924 and 1936 of the provisions of State branch laws; these differences do not, however, affect the conclusions in an important degree. In Virginia, for example, a bank may establish branches in the head office city without regard to population and in other cities with a population of 50,000 or more. In addition a bank may open branches in the head office county or adjoining counties by purchasing other banks.

Only 2 States, Delaware and Georgia, whose statutes in 1924 authorized State-wide branch banking do not permit it now. The establishment of new branches in both these States is restricted to the head office city. Actions of a restrictive character taken in the years before 1930 were associated among other things with popular sentiment against the chain store movement and with bitterness resulting from a spectacular failure of a branch or chain banking system. There were 12 head office city and 24 other branches in operation in Delaware and Georgia at the end of 1935.

Beyond County of Head Office but Not State-wide. - In 1924 branches could under the law be established beyond the county of the head office but not on a State-wide basis in 1 State, Maine, where State-wide branch banking is now permitted. In June 1936 there were 9 States in which branches could be established beyond the county of the head office but not on a State-wide basis, as follows:

Arkansas (1935)*	Montana (1931)	Ohio (1931)
Iowa (1931)*	New Mexico (1935)*	Pennsylvania (1935)
Mississippi (1934)	New York (1934)	Wisconsin (1932)*

*These States authorize only limited power "offices." As previously indicated, however, these are referred to in this memorandum as "branches," in view of the provisions of Federal law.

Head Office County Only. - Branches were permitted by law to be established within but not beyond the limits of the head office county in 1 State in 1924. In June 1936 there were 6 such States as follows:

Alabama (1935)	Louisiana*	New Jersey (1932)
Indiana (1931)	Massachusetts (1934)	Tennessee

*Banks in Allen, Calcasieu, and Jefferson Davis parishes may operate branches in any one or more of these parishes.

Head Office City Only. - Branches were permitted by law to be established within but not beyond the limits of the head office city in 5 States in 1924. In June 1936 there were only 2 such States, Delaware and Georgia, both of which permitted State-wide branch banking in 1924. Of the 5 States which limited branches to the head office city in 1924, Mississippi, New York, Ohio, and Pennsylvania by June 1936 permitted branches or additional offices beyond the county of the head office but not on a State-wide basis and Massachusetts permitted them within the county of the head office city.

Prohibited. - Branches were prohibited by statute in 17 States in 1924 but in only the following 9 States in June 1936:

Colorado	Kansas	Nebraska
Florida	Minnesota	Texas
Illinois	Missouri	West Virginia

No Statutory Provision. - In 1924, 15 States had no statutory provisions with respect to branch banking. This situation was limited to the following 5 States in June 1936:

Kentucky	North Dakota	Wyoming
New Hampshire	Oklahoma	

In 6 States in which establishment of branches is either prohibited or not provided for by statute, some branch offices existed for one reason or another on December 31, 1935. There were 30 such branches in Kentucky, 6 in Minnesota, 2 each in West Virginia and Nebraska, and 1 each in New Hampshire and North Dakota. The establishment of the 30 branch offices in operation in Kentucky on December 31, 1935, has been

made possible by a court ruling to the effect that a State bank may establish offices separate and apart from its main office for the purpose of receiving deposits, paying checks and keeping records of such transactions.

Branches with Limited Functions. - The laws of Iowa, Wisconsin, Arkansas, and New Mexico permit the establishment of offices that have only limited banking functions. They may receive and pay out deposits but not make loans. It is not known to what extent, if any, these offices receive applications for loans and arrange with the parent bank, by telephone or telegraph, to have the proceeds of the loan credited immediately to the deposit account carried by the applicant at the branch. In any event they are not termed "branches" by State law; in fact the law of Iowa prohibits "branch banking." In South Dakota, North Carolina, and Mississippi full power branches are authorized under some circumstances and limited power offices under other circumstances.

Conditions Under Which Branches May Be Established. - The law of Montana provides that no branch may be established except by consolidation of banks, and the laws of 4 other States contain a similar restriction with respect to branches to be established in certain circumstances.1/ The laws of Arkansas and Iowa provide that no branch may be established in a place where there is already a banking office, the law of Wisconsin provides that no branch shall be established where there are already adequate banking facilities, and the laws of 5 other States contain a similar restriction with respect to the establishment of branches in certain cir-

1/ For example, if the branch is outside the head office city, in a place under a certain population, etc.

cumstances. The statutes of 10 States provide a somewhat less severe restriction to the effect that no branch may be established except by consolidation or in a place where there is no banking office, but in most cases this applies only to branches to be established in certain locations. Some States have one requirement for the establishment of branches in certain circumstances and a different requirement for the establishment of branches in other circumstances, and thus there is a certain amount of duplication in any such compilation. However, 22 different States have statutes which, in at least some circumstances, restrict the establishment of branches to consolidations, places without another bank, or an alternative between these two.

The statutes of 10 States contain provisions restricting the establishment of branches to places of a specified population. In some cases these population restrictions practically confine branch banking to the places in which it now exists. For example, the law of Alabama provides that a State bank may establish a branch at any place within the county in which it is located, but another provision of the law restricts the establishment of branches to counties having a population of over 250,000. This effectively restricts branch banking to Jefferson County, in which the City of Birmingham is located.

Statutes Affecting Group Banking

Federal Law.- Before the enactment of the Banking Act of 1933, Federal law, which has closely restricted the extension of branch banking, contained no provision whatever designed to control the other forms of multiple office banking, namely, group banking and chain banking. The Banking Acts of 1933 and 1935 contain provisions which bring group banking under some degree of Federal control, but they do not restrict the area of operations of a bank group and a "holding company affiliate", accordingly, may operate banks in any part of the country.

The principal restrictive provision in Federal law with respect to holding company affiliates is the requirement that such an organization must obtain a voting permit from the Board of Governors before it can legally vote the stock of member banks controlled by it. In order to obtain such a permit, the holding company affiliate must agree to certain conditions. The principal conditions prescribed in the law are that the holding company affiliate must submit to examination by Federal authorities and must agree to build up a portfolio of readily marketable assets, other than bank stocks, equal to a certain percentage of the bank stocks controlled by it. The Board of Governors also prescribes specific conditions in connection with each voting permit, all designed to strengthen or to maintain the strength of the holding company and the banks controlled by it and to improve their operating practices.

The law also imposes certain restrictions on the amount and conditions under which credit may be extended by a member bank to its holding company, regardless of whether or not the holding company chooses to apply for a voting permit. Holding company affiliates are also required to submit

reports as of the same call dates as condition reports rendered by member banks. These reports must be published by the member banks in the same manner as their condition reports.

These provisions of Federal law and the conditions prescribed pursuant thereto do not, however, prevent the acquisition of additional member and non-member banks, no matter where located. Thus, if a given bank group cannot expand its field of operations by establishing branches because of prohibitory provisions of law, it may accomplish essentially the same thing by acquiring and operating additional banks, provided only that it complies with provisions of law pertaining to voting permits, etc.

State Laws with Regard to Bank Holding Companies[1/]. - Only in the following 5 cases do State laws appear to be designed to prevent the control of banks by holding companies:

State	Prohibition
Mississippi	Formation of any corporation, or the admission of any foreign corporation to do business in the State, for the purpose of operating banks in groups.
West Virginia	Holding of bank stock by a corporation to perfect control of a bank. (The ownership of bank stock for investment purposes is not prohibited.)
New Jersey	Holding by a corporation of more than 10% of the stock of more than 1 bank or trust company.
Washington	Acquisition by a corporation organized or licensed to transact business in the State of more than one-fourth of the stock of any bank or trust company.
Kentucky	Holding by any person of more than one-half of the stock of any bank or trust company.

1/ Discussion based on provisions of State banking laws without regard to other provisions of State law.

In spite of the apparent intent of the law, there are some group banks in each of the above States except Mississippi. It may be that control over the banks in such States is held by a method not specifically prohibited by law. For example, in the case of the First National Bank of Louisville, trustees hold control over several banks. In Washington the existence of some group banking possibly is explained by the fact that the law appears to prohibit a corporation organized or licensed to transact business in the State from acquiring control over additional banks but not from continuing existing control over banks. It is understood from newspaper reports, moreover, that the Transamerica Corporation during 1936 acquired control of the National Bank of Tacoma, Washington. In view of the provisions of State law referred to above, control of this bank may be held by an individual in behalf of the Corporation, or the Corporation may hold it directly on the ground that such holding does not constitute the transaction of business in the State. In West Virginia and New Jersey the existence of some group banking perhaps is partly explained by the fact that the restrictive provisions of law are not very clear, particularly with respect to the acquisition of control of banks and trust companies by other banks and trust companies.

The laws of the following 5 other States contain miscellaneous provisions designed to afford some measure of supervision of the operations of bank holding companies or to control somewhat the relations between the holding company and the controlled banks:

Indiana	Requires a holding company to obtain a voting permit, as the Federal statute does, before it may vote the stock of controlled banks.
Kansas	Authorizes the banking authorities to examine any corporation holding as much as one-fourth of the stock of any bank or trust company.

Arkansas	A person owning 50 percent of the capital stock of three or more banks or trust companies may not obtain loans from such institutions.
Oregon	Restricts dealing between bank holding companies and their banking affiliates.
Wisconsin	Prohibits the holding of more than 10 percent of the stock of any bank or trust company by any corporation unless 75 percent of the stock of both the corporation and the bank or trust company is voted in favor of such relationship.
	A corporation controlling a majority of the stock of any bank or trust company is subject to supervision and examination, must file reports, is subject to double liability, and may be required to correct unsound practices.
	When more than 10 percent of the stock of a bank is controlled by another corporation, the bank may not establish a receiving and paying station, the substantial equivalent of a branch office.

Minnesota law recognizes the existence of group banking by prohibiting any bank from advertising in any way that it derives any financial strength from association with any other bank or banks by way of a holding company or other similar structure. Pennsylvania recognizes the existence of group banking by providing that any corporation owning bank stock may vote the stock by its president. No provision, however, for supervision of holding companies exists in either of these States. There appears to be nothing in the laws of the 36 other States relating to the acquisition of bank stock by holding companies or relating to chain or group banking.

Ownership of Bank Stock by Banks and Trust Companies[1/] - The laws of some States also contain provisions with respect to the acquisition of bank or trust company stock by banks and trust companies. These provisions vary widely from State to State and are difficult to summarize.

1/ Discussion based on provisions of State banking laws without regard to other provisions of State law.

In general, it appears that commercial banks in approximately half the States are prohibited from acquiring any bank or trust company stock or are limited as to the amount that may be acquired; the laws of 19 other States contain no provisions with respect to the acquisition of such stock by commercial banks; and the laws of Arizona, New Jersey, Pennsylvania, and South Carolina permit commercial banks to acquire such stock apparently without limitation, although Arizona requires the approval of the Superintendent of Banks.

The laws of about half the States (though not always the same States that impose similar restrictions on commercial banks) prohibit trust companies from acquiring bank or trust company stock or limit the amount that may be acquired; the laws of 12 States apparently contain no provision with respect to the acquisition of such stock by trust companies; and the laws of Arizona, Arkansas, Colorado, Louisiana, Maryland, Michigan, Montana, Nebraska, New Jersey, Ohio, Oklahoma, Pennsylvania, and Utah permit trust companies to acquire such stock apparently without limitation, although Arizona and Utah require the approval of the State banking department.

Insofar as State law is concerned, therefore, there is no reason why trust companies in a number of States may not acquire control of banks and operate group banking systems. There are, in fact, a number of bank groups that are headed by trust companies which own the controlling interest in the stock of other banks. There are also some groups which are headed either by a national bank or by a State bank, which controls other banks through trustees, subsidiaries or otherwise. Among these two types of group systems are the following:

	Number of banks in group on December 31,1935
Groups controlled through ownership of bank stock by trust companies	
Ogdensburg Trust Co., Ogdensburg, N. Y.	5
Union Trust Company, Pittsburgh, Pa.	5
Commonwealth Trust Co., Pittsburgh, Pa.	3
Peoples-Pittsburgh Trust Co., Pittsburgh, Pa.	3
Eastern Trust & Banking Co., Bangor, Me.	3
United States Trust Company, Paterson, N. J.	3
Groups controlled by a bank through trustees, subsidiaries, or otherwise	
Atlantic National Bank, Jacksonville, Fla.	7
National Shawmut Bank, Boston, Mass.	7
Republic National Bank & Trust Co., Dallas, Texas	3
Mercantile National Bank, Dallas, Texas	5
Citizens & Southern National Bank, Savannah, Ga.	6

It will be noted that some of the groups controlled by a bank or trust company, or by interests which control the dominant bank or trust company, operate in States which have prohibited or restricted branch banking, or which still do so. The group systems in most of these cases doubtless were formed for the purpose of providing a form of multiple office banking.

Capital Requirements for Establishment of Branches

Present Capital Requirements of Federal Law. - The National Bank Act contains two provisions which stipulate special capital requirements for banks establishing branches outside the head office city. One of these provisions fixes a minimum capital based on the population of the State and of the largest city in the State for banks establishing branches outside their head office cities. It reads as follows:

> "No such (national banking) association shall establish a branch outside of the city, town, or village in which it is situated unless it has a paid-in and unimpaired capital stock of not less than $500,000: Provided, That in States with a population of less than one million, and which have no cities located therein with a population exceeding one hundred thousand, the capital shall be not less than $250,000: Provided, That in States with a population of less than one-half million, and which have no cities located therein with a population exceeding fifty thousand, the capital shall not be less than $100,000."

The second provision requires the capital to be fixed also with reference to the number of branches operated and the number of places in which they are situated. It reads as follows:

> "The aggregate capital of every national banking association and its branches shall at no time be less than the aggregate minimum capital required by law for the establishment of an equal number of national banking associations situated in the various places where such association and its branches are situated."

Both of the above provisions are applicable also to State bank members of the Federal Reserve System.

The second provision of the National Bank Act quoted above has been construed to mean that a national bank operating one or more

branches outside its head office city must have one "unit" of capital (that is, the same as is required for a non-branch national bank) for the head office city and for each other city in which it has one or more branches. This interpretation is consistent with the ruling that a national bank with branches only in the head office city is not required to have any more capital than one with no branches whatever.

Capital Requirements of State Laws. - Capital requirements for State banks operating branches vary so widely that it is difficult to analyze them authoritatively. A survey of the applicable State laws indicates, however, that in only 14 States is there a minimum capital requirement for branch systems, apart from a requirement based on the number of branches or the amount of deposits; in only 5 of these States (Maine, Oregon, Washington, Alabama, and Connecticut) is the requirement as high as $500,000. In 11 States the aggregate minimum capital must be the amount required to organize banks located in the head office and branch cities. In about 10 States there are no statutory provisions whatever requiring additional capital to establish branches.

Effect of Present Requirements. - The present provision of the National Bank Act, that no national bank located in a State with a population of 1,000,000 or more may establish any branches outside the head office city unless it has a capital of at least $500,000, effectively prevents the establishment of national bank facilities in small communities, even in the same county, which are deprived of all banking facilities. It does so, furthermore, in spite of the

fact that, except in five States, State banks are not subject to such high capital requirements. In Arkansas, Iowa, and Wisconsin, State banks may establish additional "offices" for the receipt and payment of deposits without being required to increase their capital at all. In contrast, a national bank in any of these States with a capital of $50,000 would have to increase its capital tenfold to establish a branch office in an adjoining town.

The effect of this provision of law is not so restrictive in the case of a national bank located in a State with a population of less than 1,000,000 and no city larger than 100,000, and even less restrictive in the case of a State with a population below 500,000 and no city larger than 50,000. In the latter case a national bank located in a small city and having a capital of $100,000 may establish a branch in another small city without increasing its capital, if State banks are allowed to establish such branches. The law as it stands not only discriminates seriously against national as compared with State banks, but as between national banks which happen to be located in different States.

Of even greater immediate importance is the fact that some State banks are precluded from joining the Federal Reserve System solely by reason of the fact that State bank members may establish branches outside their head office cities only on the same terms as national banks. Furthermore, no State bank being admitted to membership may retain any such branches established after February 25, 1927, the date of the passage of the McFadden Act, unless it meets the capital

requirements above referred to. The Federal Reserve Bank of Chicago recently advised the Board of an informal application for membership that was dropped as soon as the restrictive provisions of law were called to the attention of the inquiring bank. A recent survey indicates that out of something over 400 nonmember banks(other than mutual savings banks) operating one or more branches outside the head office city, over 300 are ineligible for membership by reason of the special capital requirements applicable to such branch systems. This figure includes 93 banks in Iowa, mostly with only one branch office, which would have to increase their capital stock from the present aggregate amount of $4,570,000 to an aggregate of $46,500,000, in spite of the fact that their deposits amounted on December 31, 1935, to only $71,-000,000. In Wisconsin there are 59 nonmember banks in the same situation, in North Carolina 27, in Indiana 21, and in Virginia 20.

Some of the nonmember branch operating banks have deposits of over $1,000,000 and would, therefore, be automatically deprived of deposit insurance after July 1, 1942, because of being ineligible for Federal Reserve membership unless the Board waived the high capital requirements. If, for example, a State bank in Iowa with a capital of $100,000 and deposits of $1,000,000 and operating one branch in an adjoining small city wished to have its deposits insured after July 1, 1942, it would have to become a member of the Federal Reserve System. In order to be eligible for membership from the standpoint of capital requirements, it would have to increase its capital from $100,000 to $500,000 unless the Board waived the capital requirement.

If the Board did waive the capital requirement and admitted the bank with a capital of only one-fifth of the minimum prescribed by law, the bank apparently could continue to operate the branch it already had, but after becoming a member bank it could not establish even one additional branch without increasing its capital to $500,000.

Furthermore, although the Board could, under the existing provisions of law, waive the capital requirements for a bank with deposits of $1,000,000 or more, it could not do so in the case of a bank having lower deposits. As a consequence, another bank in Iowa with a capital of $100,000 and deposits of, say, $500,000 and operating an out-of-city branch could not come into membership under the waiver provision; that is to say, the smaller bank would be required to have a capital of at least $500,000 to be admitted to membership, while the larger bank might, through the exercise of the waiver by the Board, be admitted with a capital of only $100,000.

There are about 400 nonmember banks operating one or more branches outside the head office city, 300 of which would be prevented from joining the Federal Reserve System because of the special capital requirements applicable to branch systems. These requirements also discriminate against national banks as compared with State banks, and against a national bank in a populous State as compared with a national bank in a State with less population. These provisions, moreover, definitely make it impossible for both national and State member banks to establish branches in locations where it might be desirable to provide such facilities either de novo or in replacement of existing small banks.

Possible Modifications in Capital Requirements of Federal Law. - Because of the inequities with respect to the capital requirements for national and State member banks which establish branches, modifications in the law have been suggested from time to time. For example, it has been proposed that the law be amended eliminating the requirements: (1) that a national or State member bank which establishes branches outside the head office city have a minimum capital of $500,000, $250,000 or $100,000, depending on the size of the State of location; and (2) that the aggregate capital of a bank and its branches shall not be less than the aggregate minimum capital required for the establishment of an equal number of national banks in the various places where the bank and its branches are located. For the provisions eliminated, the proposal would substitute the legal requirements: (1) that a bank having branches shall have capital adequate in relation to its deposit liabilities and other corporate responsibilities; and (2) that such capital shall not be less in any case than the amount required by State law of State banks operating the same number of branches in the places where the bank's branches are located.

Provisions of the character proposed are appropriate if the Federal Government continues its policy of permitting each State to define the extent to which national banks may operate branches within its borders. If, on the other hand, the Federal Government should determine upon a national policy with respect to branch banking, it would not be consistent to allow individual States to specify capital requirements with respect to national banks operating branches. In such a circumstance any State could effectively prevent the establishment of branches by a

national bank within its boundaries by setting unreasonably high capital requirements. If Federal authorities were required to fix different capital requirements in different States because of provisions of State laws, the capital requirements would not be determined solely on the basis of adequacy.

Branch Banking Extension

National Policy for Branch Banking Areas. - Because of the developments of the past few years, the possibilities of branch systems operating on a State-wide basis exist in a considerable portion of the country. The outlook at present is for a continued opening up along State lines, if the Federal Government continues to allow the States individually to define the branch banking area for both State and national banks. It would seem appropriate to consider whether it would not be sounder from a national point of view for the Federal Government to adopt a logical area for operation of branches by national banks regardless of State laws. The prohibition or restriction of branch banking has been circumvented to some extent by group banking, which at best is merely a cumbersome style of branch banking.

The Need and Advantages of Additional Branch Banking. There is a steady movement in the direction of converting small unit banks into branches of larger banks. Some that cannot be converted into branches because of legal restrictions are being merged into other banks or are being acquired by bank groups. A large proportion of all commercial banks, however, continues to be in the smaller size groups. As of December 31, 1935, more than 9,000 of the 15,000 commercial banks had total loans and investments of less than $500,000 each. Many of these, of course, are well managed and year after year make excellent returns on their invested capital, but they are the exception which proves the rule. The rate of failure among banks of this size has been relatively high and their earnings record has been so poor on the average as to suggest that their economic justification is dubious. During the decade and a

half ending in 1935, 53 such banks failed for every 100 in existence at the beginning of the period. This record may be contrasted with a rate of failure of 30 per 100 for all banks with more than $1,000,000 of loans and investments. It is true, however, that the high rate of failure among small banks is associated with the fact that they were most numerous in agricultural areas, which have been affected by serious difficulties of readjustment since the war.

It is believed by many that the substitution, slowly and under full control, of branches of strong, well managed banks for weak independent banks should result in a stronger banking structure. A structure changing in this way should bring to the general public (1) greater safety and increased mobility of funds; (2) more uniform and lower money rates; and (3) more efficient banking services, including greater availability of bank credit to borrowers and to local communities. Banks operating branches have greater opportunities for diversification of assets and deposits, better bank management, and economics in operation than small unit banks have. If there were more opportunity for branch operation, the urge to operate groups would be lessened.

There are many localities which today are without banking facilities, especially in the States where the law does not permit branch operation. These communities cannot supply a sufficient amount of business to support a separately incorporated bank. However, branches with either full or limited banking powers could serve them economically.

Because of legal restrictions against branch banking, the only way that banking facilities could be provided in many localities was by the establishment of independent unit banks, even when there was considerable doubt whether the community could support a bank or whether there would

be a permanent need of banking facilities. Once established an independent bank often is continued in operation long after it has ceased to be a profitable venture until finally it becomes insolvent, entailing losses to depositors and stockholders. A branch in similar circumstances not only costs less to establish and operate but is easier to discontinue when the facilities are no longer needed, thereby avoiding the heavy losses that come from continued operation of an obviously unprofitable undertaking. This would be particularly useful in newly developed territories or in communities into which new industries have moved.

If it is found that a given country bank is too small to operate successfully, arrangements sometimes can be made to sell its business to a bank in another community, but in many States under present laws there is no way to replace the first bank by a branch. On the other hand, where the law permits, it is possible to form country branch systems through merger of banks in different communities, thereby strengthening the banking structure and yet continuing to provide banking facilities wherever needed.

Obstacles to Additional Branch Banking. - The outstanding obstacles to obtaining legislation for the extension of branch banking are the opposition of unit banks to being subjected to the competition of branch operating banks, the fear of local interests that foreign control of credit facilities might be used as a means of stifling legitimate local enterprise, and the general objection to any tendency towards monopolistic power. Opponents of branch banking maintain that a bank locally controlled is more familiar with local credit needs and risks,

that in the final analysis no branch system is better than the units which make it up, and that the failure record of branch systems is no better than the record of unit banks. They do not admit that branch banking results in better management or more economical operation. They argue that the Canadian banking structure derives its strength not from the fact that it is composed of a few large branch systems but from the fact that these systems adhere to sounder banking principles. It is maintained also that the people of each State should continue to have the right to decide the extent, if any, to which there should be branch banking in the State; that the greater mobility of credit provided by a branch system will make it easier to transfer funds to the larger centers to the detriment of the local communities; and that a branch system should not be permitted to discontinue banking facilities at will as soon as it appears unprofitable to operate a branch. Some of the large city banks that oppose an extension of the branch banking area doubtless are influenced by the fact that some of the business which they derive by reason of their relationships with numerous country banks would be transacted by the head offices of branch systems.

Every student of banking, however, is conscious of the hazard which would accompany a too rapid amalgamation of banks into branch systems. Supervisory authorities should have and exercise adequate power to prevent this. They should also have adequate power to curtail unneeded banking facilities, whether they be provided by unit banks or by branches.

Advantages and Disadvantages of Group Banking

Advantages. - Many of the advantages over unit banking claimed for branch banking are also urged for group banking. A group system affords a better opportunity for improving bank management; for a wider range of services to its banks' customers, particularly those in outlying towns; and for the shifting of surplus lending power from one community to another.

The investments of the banks in a group may be better managed through the employment of expert investment counsel by the head office of the group. A well managed group can effect economies in operation and increased efficiency by centralizing the purchase of supplies and equipment, by prescribing a uniform accounting procedure for all banks in the group, by centralizing audits, as well as by maintaining central or at least uniform credit files. It is possible for general credit and operating policies to be formulated at the head office of the group, making it unnecessary for each bank to go into these matters and eliminating the need of certain experienced, high salaried personnel at each office. Where the management is cooperative with supervisory authorities, the uniformity of operating methods and accounting procedure, centralization of auditing, periodic credit inspections, and general supervision by the holding company make it easier to examine the banks in a group and examiners' criticisms can be rendered more effective through the group management.

All of these advantages of group banking, however, are also

characteristic of branch banking and usually in greater degree.

There are some who feel that group banking affords more local independence than branch banking--that a bank acquired by a group will continue to be operated by a local board of directors and officers familiar with local problems, while if converted to a branch it will be operated by a manager or other officer who is definitely subject to the orders of the head office. Such a distinction in operating policies does obtain in some cases, at least for a time, after acquisition of a bank by a holding company. It is not uncommon for a branch system to afford a considerable degree of autonomy to its branches, particularly those located outside of the head office city. On the other hand, in order to achieve the advantages peculiar to any multiple office banking system, the bank group must sooner or later bring all of its constituent banks under a substantial measure of central control. When such a situation is reached, the group bank is not much more than a branch except that it usually is more expensive to operate.

A group system should be able to survive periods of strain better than a unit bank without branches although this cannot be substantiated from available statistical evidence. During the recent banking crisis some of the largest bank groups were closed and some were kept open only through large amounts of Government capital and other assistance. The peculiar character of the period during which group banking developed makes this record inconclusive. In the final stages of the deflation

ending in March 1933 many banks failed--banks with and without branches, members and nonmembers of groups--which had been well regarded before the depression began.

Disadvantages and Evils. - The fact that many of the large groups comprise not only national and State bank members of the Federal Reserve System but also nonmember banks is one of the most unfortunate characteristics of group banking. In order to effect a simultaneous examination of all banks in such a group, there must be cooperation among a number of supervisory authorities--the Comptroller of the Currency, Federal Reserve banks, Federal Deposit Insurance Corporation, and State banking departments. The administrative problem of organizing such an examination is considerable, and even if a satisfactory joint examination is made it is almost impossible to enforce uniform standards of correction with respect to the different classes of banks in the group.

The existing statutes, particularly those of States, do not afford adequate control over bank holding companies, though the banks themselves are, of course, subject to at least as much control as non-group banks. The Board of Governors has power to grant or withhold permits to the holding companies to vote the stock of member banks controlled. If a holding company finds it unnecessary, however, as some apparently have, to vote the stock of member banks in order to influence their operating policies, it is under no compulsion to obtain such a permit. In such an event the holding company cannot be subjected to conditions imposed by the

law, or by the Board of Governors pursuant to law, incident to the granting of a voting permit. If, however, the "holding company affiliate" also happens to be a technical "affiliate" within the meaning of the law, it will be subject to the provisions of law applicable to all affiliates of member banks.

The organizers of bank holding companies in some instances have been charged with having evinced too much interest in promotional profits, as well as in the subsequent payments of substantial dividends by the subsidiary banks. In the race for "bigness" the prices paid for bank stocks by holding companies sometimes have been considerably out of line with asset values and earning capacity. In such circumstances the management of the holding company is under temptation to influence the payment of dividends by controlled banks not justified by earnings. The dividends of the holding company depend directly on the dividends paid by the controlled banks and the market price of the holding company stock is affected by the amount of dividends paid. Moreover, in order to maintain the price of the holding company stock, the promoters in the past have had a strong incentive to use the credit of controlled banks for loans on such stock. This is tantamount to the lending of money by banks on their own stocks, a practice that is both improper and illegal. The active trading in holding company stocks, especially if listed on a national exchange, is associated with the danger that sharp market breaks in the price of such stock may lead to loss of confidence by depositors in the safety of the controlled banks.

The wide distribution of the stock of the larger holding companies makes it possible for a minority group of stockholders to hold effective control. In some instances also holding companies have been capitalized

by the issuance of both voting and non-voting shares, with the result that the holders of a small proportion of the shares are able to control the operations of the holding company. In either case a minority group may, by a comparatively modest investment in the shares of a holding company, control the loan, investment and operating policies of many banks.

The possibilities of improper relationship between group banks and other subsidiaries or affiliates of the holding company are also a source of danger. Inter-bank borrowings by means of certificates of deposit, not properly reflected in condition statements, have been charged to some group systems in the past. Various kinds of business enterprise are sometimes affiliated either directly or indirectly with bank holding companies. One or more of the more prominent bank holding companies, for example, are directly or indirectly affiliated with a realty firm, coal company, industrial bank, joint stock land bank, fire insurance company, life insurance company, title insurance company, mortgage company, etc.

A group system has an unfair advantage over an independent national bank in expanding multiple office operations. In most States a national bank cannot establish a branch outside its head office city unless it has a capital of at least $500,000, but a group system can organize and operate a new national bank similarly situated with a capital of as low as $50,000. Thus a group system may by indirection and subterfuge provide multiple banking facilities without complying with the conditions set by Congress.

If Congress should authorize Federal Reserve district-

wide branch banking, for example, the possible field of operations of some of the existing bank groups would be tremendous unless the law provided that no group could operate banks or branches in more than one Federal Reserve district. For example, if national banks were authorized to establish branches at any point in the Federal Reserve districts in which their head offices were located, the Northwest Bancorporation presumably could establish a branch system in each of the three Federal Reserve districts in which it now operates. These districts (Minneapolis, Kansas City, and Chicago) embrace all or parts of 16 States, have an aggregate population of 32 millions, and have more than one-third of the total area of the United States. It would be but a short step from such a combined group and branch banking system to Nation-wide branch banking.

Some of the unfavorable considerations with respect to group banking are not the fault of group banking and some hold true also of branch and unit banking. In any event legislation might be enacted correcting the important defects of group banking. For example, consolidation of Federal supervision over banks would rectify one of the principal problems of group banking, and Federal authorities might be given additional power to supervise bank holding companies or to regulate their operations without regard to whether or not they choose to apply for voting permits. The danger of overvaluing a bank is also present when one bank absorbs another for the purpose of converting it into a branch. The terms of such mergers, however, either have to be approved by supervisory authorities or are more closely scrutinized by such authorities than the purchase

of bank stock by a holding company. Improper relationships between banks and affiliated organizations are not confined to group systems. Even in the case of a large unit bank or branch system a minority group may control the bank if the stock of the bank is widely distributed. It may be conceded that if adequate supervision and regulation has a salutary effect on the practices and soundness of unit banks and branch systems, the same thing might be achieved with respect to group banking by appropriate legislation. The fact remains, nevertheless, that under the existing laws and the existing division of responsibility for bank examination and supervision, group banking is a much less desirable means of providing multiple office banking facilities than branch banking.

Restriction of Group Banking

The circumstances under which group banking has developed and continues to be an important factor in the banking structure of the United States suggest that if Congress wishes to place effective restrictions on the area covered in multiple office operation, it should establish a reasonable area in which banks may operate branches and then either prohibit group banking or restrict its area of operation to that of the legal branch area.

It might be made unlawful for a corporation, business trust, association, or similar organization which holds a working control,[1/] direct or indirect, over any insured bank to acquire a working control, direct or indirect, over any other insured bank located beyond the same limits with respect to the principal place of business of such corporation, business trust, association, or similar organization as the limits prescribed by law for the establishment of branches of a national bank.

Because of certain undesirable characteristics of group banking, public policy would do well to look towards the ultimate disappearance of that form of multiple office operation from the banking structure. To this end it might be made unlawful after the expiration of 5 years from the enactment of the legislation for a corporation, business trust, association, or similar organization to retain working control, direct or indirect, over more than one insured bank. Proponents of the exten-

1/ By "working control" is meant control of a majority of the shares of capital stock of the bank or of 50 percent of the number of shares voted for the election of its directors at the last preceding election; control in any other manner of the election of the majority of the directors of the bank; or a situation where all or substantially all of the capital stock of the bank is held by trustees for the benefit of the controlling organization.

sion of branch banking might, however, argue in good faith against such a drastic prohibition against holding companies. Some of them feel that conversion of banks into branches can be facilitated by permitting a holding company to acquire control of banks which are to be converted into branches, rather than by confining the branch system to direct acquirement of control. It would be necessary, however, to define the privilege very clearly in order to avoid the indefinite continuance of holding company operation as a substitute for branch banking.

A Proper Branch Banking Area

Various suggestions have been made from time to time as to the area within which a national bank should be allowed to operate branches regardless of State laws governing operation of branches by State banks. All of these suggestions contemplate that a national bank should be allowed to establish a branch at any point within the area in which the head office of the bank is located, regardless of how that area may be described. Among the suggested branch banking areas are the following, or combinations of some of the following:

(1) The entire country.

(2) The Federal Reserve district.

(3) The territory assigned to the head office of a Federal Reserve bank or to a branch thereof, as the case may be.

(4) The State.

(5) Adjoining counties, regardless of State or Federal Reserve district lines. Some suggest a proviso that the aggregate population of the head office county and of the adjoining county must not exceed a given number of persons, e.g., 100,000, 250,000, etc.

(6) The head office county.

(7) Any point not more than a given number of miles from the head office of the national bank, regardless of county, State or Federal

Reserve district lines. The distance suggested by some is 50 miles and by others 100 miles.

(8) The "trade area" of the head office city, the "trade area" being left for determination by the Federal banking authorities in the case of each application for the establishment of a branch.

(9) A statutorily defined "trade area", such as the area which is nearer to the head office city of the national bank than to any other city with a given population, e.g., 100,000, 50,000, 25,000, etc.

(10) Any point, regardless of State or Federal Reserve district lines, within such a distance from the head office of the national bank that the counties completely included in the circular area represented by the head office as a center and the branch as the outer point would not have an aggregate population in excess of a given number of persons. The population mentioned in this connection is sometimes 100,000, sometimes 250,000, etc.

Considerations with Respect to Various Branch Banking Areas

Nation-wide branch banking in this country scarcely appears to be a practical consideration in either the near or the distant future. For one thing decades would be required to build up management and personnel to handle a branch banking system operating in all the diverse areas of this country. Moreover, such systems would imply a degree of banking concentration which would not be generally favored. These observations are applicable, although to a lesser extent, to an area for branch operation defined by the boundaries of a Federal Reserve district.

The boundaries of Federal Reserve zones or territories have been fixed with reference to economic and financial rather than political factors and are in a sense homogeneous trade areas. 1/ If an attempt were made by Federal legislation to give national banks the right to operate branches anywhere within the Federal Reserve bank or branch zone, there would be numerous possibilities for national banks to cross State lines. This, of course, would meet determined opposition, particularly from the States' rights elements. Conversely, if Federal statutes should stipulate that an insured State bank could not operate a branch outside of the zone of the Federal Reserve branch, conflicts would arise in certain States which are divided as to zone but in which the State law permits a State bank to operate a branch anywhere within the State. Some of the States now permitting State-wide branch banking which would raise the question are the following:

1/ Branch "zones" in the St. Louis Federal Reserve district are not marked by State and county boundary lines.

Arizona -- divided between Los Angeles and El Paso
California -- divided between San Francisco and Los Angeles
Connecticut -- divided between Boston and New York
Idaho -- divided between Spokane and Salt Lake City 1/
Michigan -- divided between Detroit, Chicago, and Minneapolis
Nevada -- divided between Salt Lake City and San Francisco
North Carolina -- divided between Richmond and Charlotte
South Carolina -- divided between Richmond and Charlotte
Washington -- divided between Portland, Spokane, and Seattle 1/

If some policy were adopted with respect to branch operation in zones, it would appear that a branch operating bank should be permitted to establish an office at any point within 50 or perhaps 100 miles of the head office in order that a bank located at the edge of the zone as otherwise defined would not be prevented from serving a natural trade area which might otherwise be just outside of the zone. Trade areas so defined should be large enough to provide considerable diversification of loans and deposits.

The operation of branches throughout contiguous counties would in some areas of the United States allow a national bank to serve an area with a diameter of as much as 300 miles. In other parts of the country it would mean little more than 25 miles. It is questionable whether in many parts of the country a contiguous county area would serve to provide much diversification in the banking business.

Areas defined by county boundaries or boundaries of a territory assigned to a Federal Reserve bank or branch zone might vary from time to time and raise problems. For example, if a given Federal Reserve branch were discontinued and its territory either reassigned to the

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1/ Recently the Spokane Branch territory, except the city of Spokane, was reassigned to the Seattle Branch.

head office or divided among other branches, this might bring about an important change in the field of operation of some banks. Presumably in such circumstances a bank would be permitted to retain any branches previously established no matter if they were outside the new zone limits. Similar difficulties probably would arise more frequently, though they would not be as important, in connection with changes in the boundary lines of counties. Sometimes a given county is subdivided, but more recently there has been considerable agitation for consolidating counties in the interest of more economic administration of State governments. Such consolidations would, of course, expand the business field of operations of banks located within the counties that consolidated.

Any branch banking area defined in terms of a certain distance from the head office city would raise a number of individual problems. For example, if the area were 50 miles from the head office city, a national bank located in Baltimore might operate a branch in Washington, or vice versa. Several of the largest cities in the United States are within 100 miles of another large city, for example, New York and Philadelphia, and Chicago and Milwaukee. Problems of this character might be met by allowing branches to be operated in other cities the population of which did not exceed 25,000 or 50,000. A branch banking area limited to a distance of 50 miles from the head office city would provide little opportunity for multiple banking facilities in the sparsely settled regions of the country. It takes no account, furthermore, of the differences in accessibility. Places 50 or 100 miles apart by airline distance but separated by a mountain range are much further apart for all practical purposes than places in the prairie sections that are many more miles apart.